

Sheffield City Council Report to Audit and Standards Committee

Update on the audit for the year
ended 31 March 2022

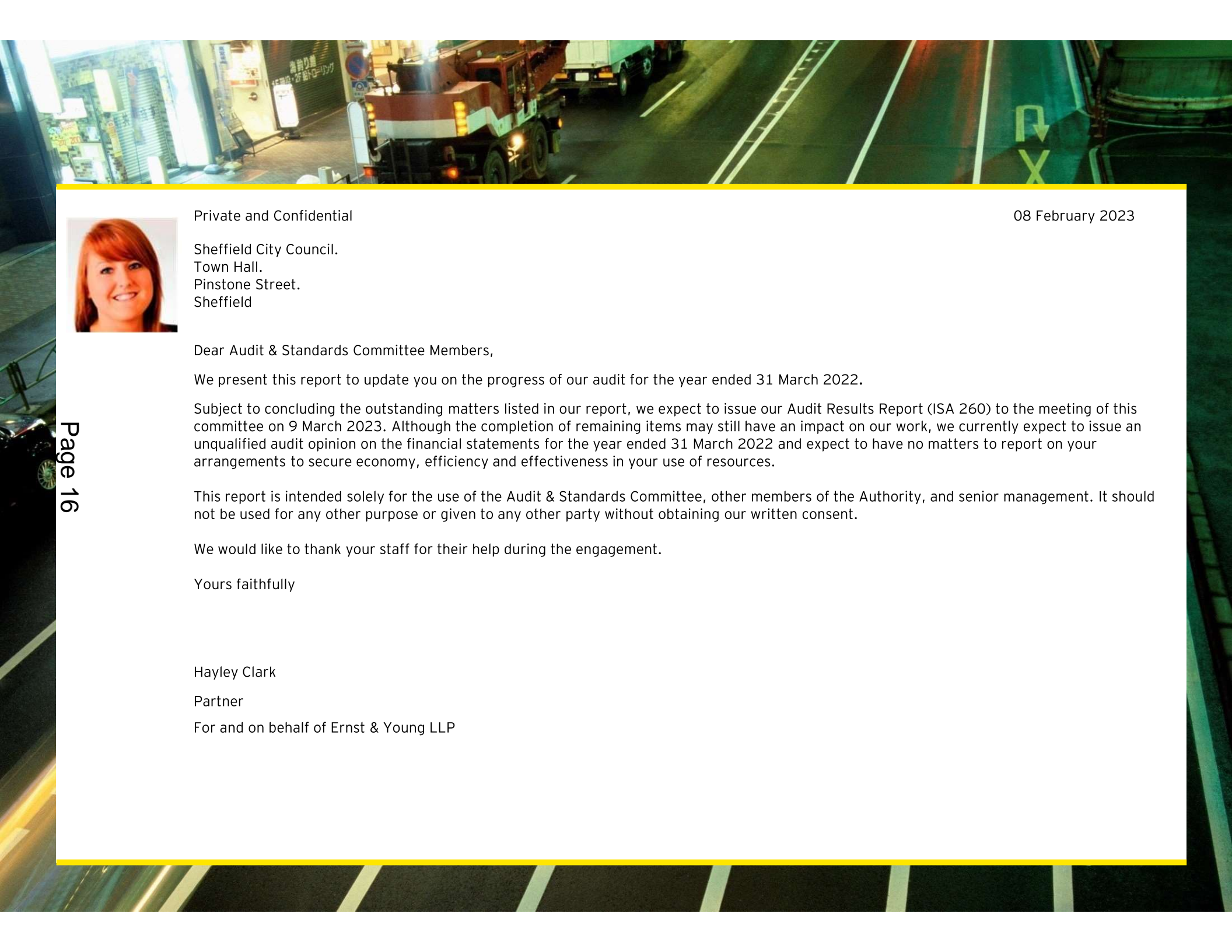
February 2023

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The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow triangle is positioned above the 'Y', pointing downwards towards the letters.

Building a better
working world

Agenda Item 6



Private and Confidential

08 February 2023



Sheffield City Council.
Town Hall.
Pinstone Street.
Sheffield

Dear Audit & Standards Committee Members,

We present this report to update you on the progress of our audit for the year ended 31 March 2022.

Subject to concluding the outstanding matters listed in our report, we expect to issue our Audit Results Report (ISA 260) to the meeting of this committee on 9 March 2023. Although the completion of remaining items may still have an impact on our work, we currently expect to issue an unqualified audit opinion on the financial statements for the year ended 31 March 2022 and expect to have no matters to report on your arrangements to secure economy, efficiency and effectiveness in your use of resources.

This report is intended solely for the use of the Audit & Standards Committee, other members of the Authority, and senior management. It should not be used for any other purpose or given to any other party without obtaining our written consent.

We would like to thank your staff for their help during the engagement.

Yours faithfully

Hayley Clark

Partner

For and on behalf of Ernst & Young LLP

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01 Executive Summary

Executive Summary

Scope update

In our audit planning report tabled at the September 2022 Audit and Standards Committee meeting, we provided you with an overview of our audit scope and approach for the audit of the financial statements. We carried out our audit in accordance with this plan.

Status of the audit

Audit work on Sheffield City Council's financial statements for the year ended 31 March 2022 is nearing completion. We performed the majority of procedures outlined in our Audit planning report. Subject to satisfactory completion of the following outstanding items we expect to issue an unqualified opinion on the Authority's financial statements. However until work is complete, further amendments may arise. The remaining tasks are:

- ▶ Completion of work on the PPE Valuations including queries relating to Investment Properties and work to audit updated Council Dwellings valuations;
- ▶ Consultation on, and review of, accounting treatment and disclosures made by management in relation to Infrastructure Assets;
- ▶ Finalisation of work in relation to Journals;
- ▶ Finalisation of the remaining queries relating to disclosures concerning the Local Government Pension Scheme;

Testing of remaining outstanding items delayed due to receipt of information from schools' payroll providers - this includes testing of Starters and Leavers and Officers Remuneration disclosures;

Completion of testing in relation to Schools' bank balances due to delays in the receipt of third-party confirmations;

Completion of a substantive testing of the Cash Flow Statement;

Conclusion on issues identified in relation to lodgements held on the year-end bank reconciliation;

- ▶ Finalisation and update of our work in relation to going concern to as close to the date of signing our opinion as possible;
- ▶ Partner and Senior Manager review of areas of audit work;
- ▶ Completion of subsequent events review;
- ▶ Receipt and review of the updated financial statements and signed management representation letter; and
- ▶ Completion of procedures required by the National Audit Office (NAO) regarding the Whole of Government Accounts (WGA) submission. It should be noted that we cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Council's WGA consolidation pack.

Value for money

We have considered your arrangements to take informed decisions; deploy resources in a sustainable manner; and work with partners and other third parties. In our audit plan, we identified significant risks concerning financial sustainability and regeneration schemes. Based on the work we have completed to date, we expect to issue a unqualified value for money conclusion. We will set out our conclusions against each risk in our Audit Results Report in March.

We plan to issue the VFM commentary, incorporating the work carried out against the risks identified in our 2021/22 audit plan by the end of April 2023 as part of issuing the Auditor's Annual Report. This will include any observations and recommendation on the financial resilience of the Council during 2022/23.



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Areas of Audit Focus

Overview of our 2021/22 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in our Audit Planning Report. Below we have provided an update in each area on the status of the work and what is required for each to be completed.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Details	Status
Misstatements due to fraud or error	Fraud risk	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.	Work is significantly complete in this area, with evidence for three journals currently being discussed with management. No issues have been identified to bring to your attention.
Risk of fraud in revenue recognition Overstatement of income - dwelling rents, fees & charges, other income and grant income (including Covid-19).	Fraud risk	Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. We consider the risk to be relevant to those significant revenue streams other than taxation receipts and non-specific grant income, where management is able to apply more judgement. Specifically, our risk is focused on: <ul style="list-style-type: none"> ▶ The occurrence of other income (including fees and charges, dwelling rentals, social care income and other income). ▶ The occurrence of grant income, including Covid-19 grants, when based on conditions that are required to be met. 	We have one remaining query that the finance and audit teams are working through in relation to lodgements on the year end bank reconciliation. In our Audit Results Report to the March committee, we will report differences identified relating to income recognition, however we currently expect to conclude that there is no evidence of management bias or fraud.
Risk of fraud in expenditure recognition <ul style="list-style-type: none"> ▶ Inappropriate capitalisation of expenditure ▶ Understatement of expenditure 	Fraud risk	As set out above, under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. We consider that this risk is more prevalent in the following areas; <ul style="list-style-type: none"> ▶ Over the medium term we consider this is likely to occur through the capitalisation of expenditure that should be accounted for in the Comprehensive Income and Expenditure Statement (CIES); and ▶ Understatement of other operating expenditure (Premises Expenditure, Transport Expenditure, Supplies and services, Third party payments, Transfer payments, Support services) to manage the financial position year on year. 	In our Audit Results Report to the March committee, we will report differences identified relating to expenditure recognition, however we currently expect to conclude that there is no evidence of management bias or fraud.



Overview of our 2021/22 audit strategy

Audit risks and areas of focus			
Risk / area of focus	Risk identified	Details	Status
Page 22 Valuation of Highways Infrastructure assets	Significant risk	<p>Due to significant practical accounting difficulties, there is a risk that the depreciation and derecognition policies employed by local authorities do not fairly represent the rate in which these assets are consumed or replaced. If records held by the Council do not allow for sufficient appropriate evidence to be obtained to gain assurance over the gross and net positions in respect of these assets, it increases the risk that material assurance cannot be provided within our opinion.</p>	<p>On 25 December 2022, the Department for Levelling Up, Housing and Communities (DLUHC), issued a statutory instrument (“the SI”) to cover all audits starting on or before 1 April 2024. This gave the option for authorities to apply the SI or continue to apply the code. Management continue to perform significant work in this area to meet the requirements of the amendment to the CIPFA Code which has been supplemented by the Local Authority Accounting Panel (LAAP) Bulletin 12. This was released on 11 January 2023. The Council had done a large amount of work prior to this bulletin was released, however, following this, a new disclosure note and briefing paper has been necessitated. We have been working closely with management throughout to provide challenge to this process and consulted informally internally to ensure we are in the best position for when the disclosure note is ready to audit.</p> <p>Management have identified three buckets into which the Highways Infrastructure assets can be categorised; Assets that the Council have sufficient confidence have been replaced by subsequent spend; Assets that the Council is seeking the relieve provided by the temporary resolution set out in the SI; and Assets that the Council have detailed underlying records to support the existence of.</p> <p>We have performed the majority of our audit work on the underlying assets disclosed. Once we are able to audit the disclosure note and review the updated accounting policies, we will need to consult, formally, with our technical and professional practice directorate to be able to provide assurance in this area. This could take up to two weeks following the receipt of the disclosures. Once this work is concluded we will provide an update to the committee.</p>
Property, Plant and Equipment - Valuation of Fair Value assets	Significant risk	<p>The Council has a large and complex asset base that makes up a significant proportion of its balance sheet. The valuation process incorporates significant judgements, which if inappropriate could result in a material misstatement. We consider the significant risk to be focused on those PPE assets that are valued at fair value due to the higher degree of estimation involved by the property valuers in calculating the valuation of the assets at the balance sheet date.</p>	<p>As part of our audit approach, we engage our internal valuation specialists to perform a detailed and specialised review of a sample of assets. The work performed by our specialist team has identified a number of issues relating to both methodology driven and input driven errors and we expect to include, in our Audit Results Report, a schedule of errors which will include amendments made by management to Assets reviewed by our specialist. Once our team have provided their report to us, we will consider their conclusions and we will provide a verbal update at the February meeting as appropriate.</p>

Overview of our 2021/22 audit strategy

Audit risks and areas of focus (continued)			
Risk / area of focus	Risk identified	Details	Status
Property, Plant and Equipment - Valuation of EUV, EUV-SH and DRC assets	Other financial statement risk (Higher inherent risk)	Given their more formulaic nature and less reliance on market value, we do not consider there to be a significant risk associated with the valuation of PPE assets where the valuation methodology is Depreciated Replacement Cost (DRC), Existing Use Valuations (EUV) and Existing Use Valuation for Social Housing (EUV-SH). However, as there is still an element of judgment and estimation involved we do consider there to be a higher inherent risk.	As part of our audit approach, we engage our internal valuation specialists to perform a detailed and specialised review of a sample of assets. The work performed by our specialist team has identified a number of issues relating to both methodology driven and input driven errors and we expect to include, in our Audit Results Report, a schedule of errors which will include amendments made by management to Assets reviewed by our specialist. Once our team have provided their report to us, we will consider their conclusions and we will provide a verbal update at the February meeting as appropriate.
Investment property valuation	Other financial statement risk (Higher inherent risk)	Investment property assets are valued at fair value. Whilst there is a greater estimation risk associated with these assets, and more judgement exercised by property valuers, the Council's portfolio comprises of two assets, which in total are less than our planning materiality, but are still significant at a value of £19 million at 31 March 2022. As there is still an element of judgment and estimation involved we do consider there to be a higher inherent risk.	We have selected one investment property in the work performed by our specialist team, therefore, although we can inform the committee that we expect there to be no items in this area to bring to your attention, until the work of our expert is finalised, further issues may be brought to our attention.
Local Government Pension Scheme (LGPS)	Other financial statement risk (Higher inherent risk)	The accounting entries relating to the LGPS are underpinned by significant assumptions and estimates. There is therefore an increased risk of misstatement and error. The estimation of the defined benefit obligations is sensitive to a range of assumptions such as rates of pay and pension inflation, mortality and discount rates. The pension fund valuations separately involve external specialists, to provide these actuarial assumptions. The estimation of the defined benefit assets involves estimation on the expected asset returns for the year based on the movement in the underlying Pension Authority total assets. A small movement in these assumptions could have a material impact on the value in the balance sheet.	Our Audit Results Report to the March committee will identify a schedule of adjusted and unadjusted errors, which will include items relating to the balances and disclosures associated with the LGPS. However, subject to Partner Review, we expect to have no material items to bring to your attention.
PFI accounting treatment	Other financial statement risk (Higher inherent risk)	The Council has a number of PFI and service concession arrangements which include several judgements made by management resulting in the accounting treatment shown in the financial statements. Such arrangements are complex and substantial in value and there is a risk that they have not been accounted for correctly.	Although we have identified a disclosure adjustment relating to a PFI transaction occurring in year, we expect that there will be no material items to bring to your attention



03

Value for Money Update



Value for money

The Authority's responsibilities for value for money (VFM)

The Council is required to maintain an effective system of internal control that supports the achievement of its policies, aims and objectives while safeguarding and securing value for money from the public funds and other resources at its disposal.

As part of the material published with its financial statements, the Council is required to bring together commentary on its governance framework and how this has operated during the period in a governance statement. In preparing its governance statement, the Council tailors the content to reflect its own individual circumstances, consistent with the requirements set out in the CIPFA code of practice on local authority accounting. This includes a requirement to provide commentary on its arrangements for securing value for money from their use of resources.

Risk assessment

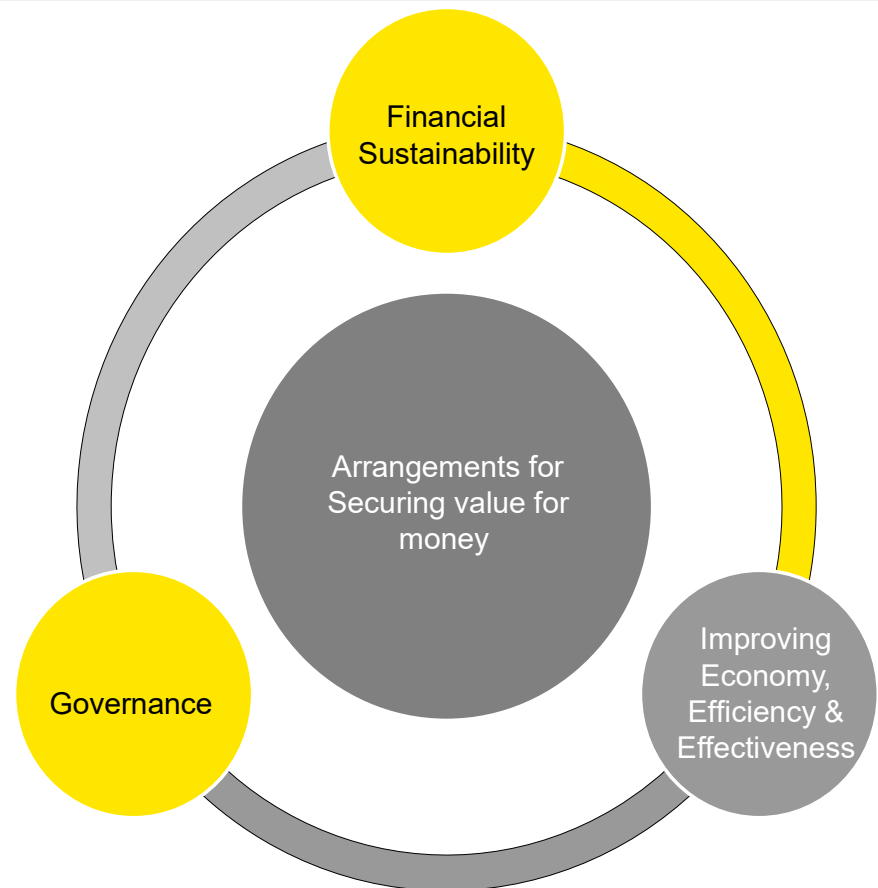
We identified three significant risks related to the Council's arrangements, these were set out in Audit Planning Report.

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Status of our VFM work

We have now completed our VFM risk assessment and we have not identified a significant weakness. Subject to review process and concluding our work, we anticipate we will have no matters to report by exception. We will include our conclusions in each of the areas within our Audit Results Report in March.

Under the Code of Audit Practice 2020 we are required to issue our commentary on the Council's VFM arrangements in the Auditor's Annual Report (AAR). The AAR is issued on the conclusion of the audit and we anticipate doing so by the end of April 2023.





04 Audit timeline



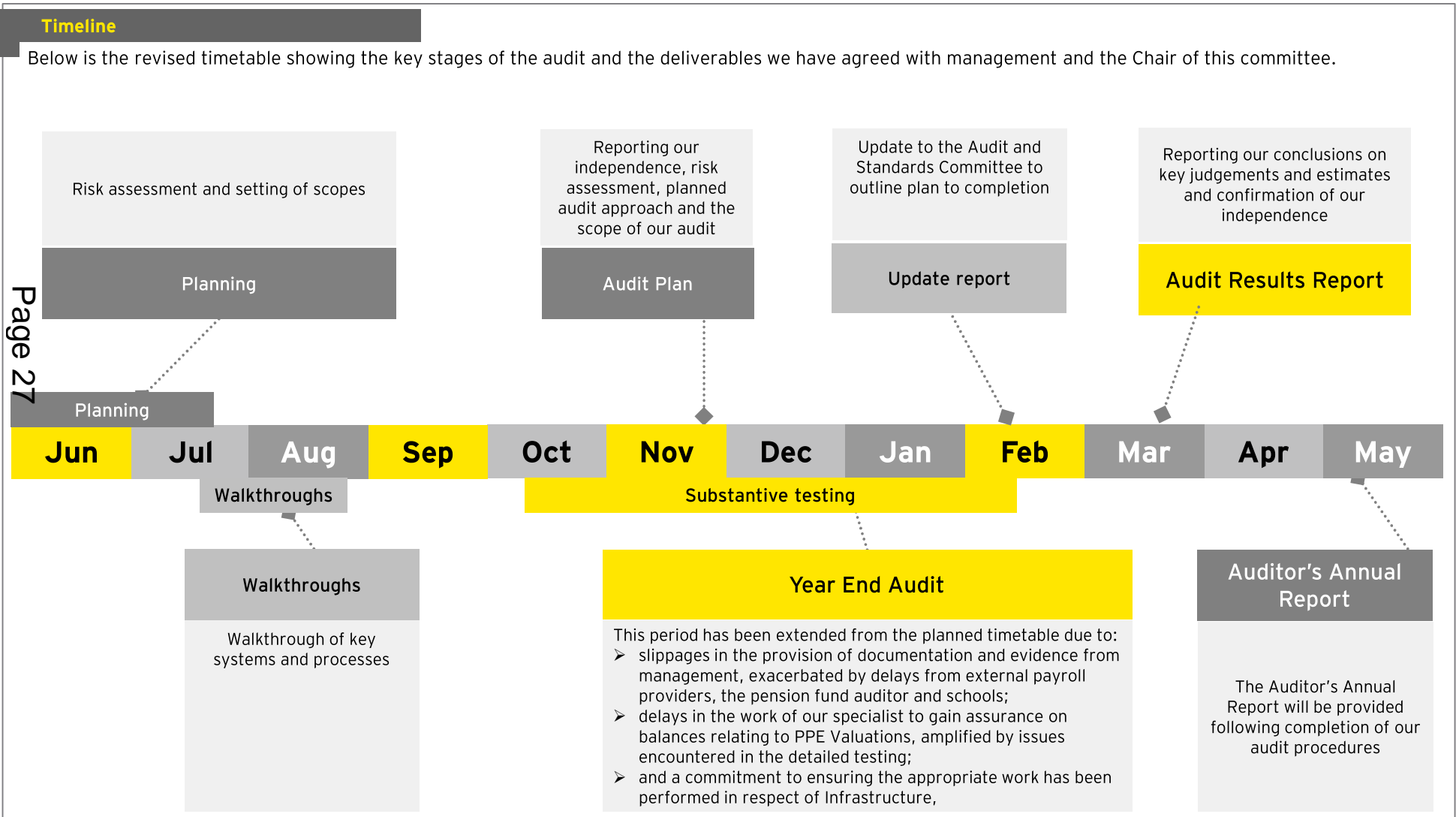


Audit timeline

Timetable of communication and deliverables

Timeline

Below is the revised timetable showing the key stages of the audit and the deliverables we have agreed with management and the Chair of this committee.



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