Appendix 1

Sheffield City Region Mayoral Combined Authority

Audit progress report

Year ended 31 March 2020

16 July 2020

EY

Building a better working world

Contents

Overview of our 2019/20 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit and Standards Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Risk of fraud in revenue and expenditure recognition	Fraud risk	No change in risk or focus	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.
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	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.
Local Government Pension Scheme – Pension Liability Valuation	Other financial statement risk	Increase in risk or focus	The accounting entries relating to the Local Government Pension Schemes are underpinned by significant assumptions and estimates. There is therefore an increased risk of misstatement and error. For the standalone SCRMCA entity this is also the first year of accounting for the defined benefit liability.
Valuation of Property, Plant and Equipment	Other financial statement risk	No change in risk or focus	The Group has a material asset base that is subject to management judgements. Valuation of assets is an area subject to professional estimation and therefore a higher inherent risk of misstatement.
Preparation for IFRS 16	Other financial statement risk	New risk for 2019/20	The CIPFA Code of Practice requires all local authorities to apply IFRS 16 from 1 April 2020. In order to hit this deadline the Group will need to undertake the necessary preparation work in 2019-20 and make disclosures of the impact of adopting IFRS 16 in the 2019-20 financial statements.
Financial Ledger upgrade	Other financial statement risk	New risk for 2019/20	**RISK ONLY APPLICABLE TO SOUTH YORKSHIRE PASSENGER TRANSPORT EXECUTIVE** SYPTE has upgraded the Epicor General Ledger system from version 7.4 to version 10, with the new system going live in January 2020. We will be required to perform procedures over the transfer of data to obtain assurance that the financial statements are based on a complete set of transactions.

01 Executive Summary

Executive Summary

Status of the audit

We have substantially completed our audit of the Authority and Group's financial statements for the year ended 31 March 2020 and have performed the 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 financial statements. However until work is complete, further amendments may arise:

- Completion of work on disclosures relating to South Yorkshire Pensions Authority
- completion and review of transaction testing in a number of areas impacting the CIES and Balance Sheet (Creditors, Grant Income, Payroll)
- Receipt of third party confirmations for the bank and investment balances (Federated, Lloyds, Santander, Invesco, Other Local Authorities)
- Review of consolidation workings
- Review of workings for the Expenditure and Funding Analysis (EFA)
- review of the final version of the financial statements
- completion of subsequent events review
- receipt of the signed management representation letter

We expect to issue the audit certificate at the same time as the audit opinion.

We expect to be able to provide a verbal update on the progress of a number of the above areas by the time of the meeting on 16 July.

Audit differences

There are currently two adjustments of which we are aware. We have been made aware of an error relating to the treatment of recharges within the CIES; we are still working with management to establish the full impact of this amendment, but it will be purely presentational and not impact the net deficit on provision of services. The second error that will improve the deficit on provision of services, by reducing a provision made in relation to the impact of COVID-19. This will instead be represented as an earmarked reserve for the Authority. The identified provision will require adjustment in both the single–entity statements and also as part of a larger error including a similar adjustment for SYPTE.

We have made a number of suggestions for amendments for disclosures and the narrative statements that have been agreed by management.

We have identified one low-level recommendation in relation to the recharges adjustment noted above. this will be reported more fully in our Audit Results Report.

02 Areas of Audit Focus

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Risk of fraud in revenue and expenditure recognition*

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income and expenditure accounts. These accounts had the following balances in the 2018/19 financial statements:

Income Account: £248m

Expenditure Account: £233m

What is the risk?

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 APN10 issued by the FRC, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

We consider that this significant risk is associated to the following specific areas:

- Improper capitalisation of revenue expenditure in order to reduce the impact on the general fund
- Understatement of expenditure recognised as liabilities in the balance sheet at the year-end
- Improper application of revenue cut-off

What will we do?

We will carry out substantive procedures in response to this risk. The procedures designed to address the identified risk are set out below:

- Document our understanding of processes and controls in place to mitigate the risks.
- Identify and walk through those processes and controls, confirming our understanding.
- Review income and expenditure recognition policies and confirm consistency of application through performance of testing.
- Identify significant accounting estimates for revenue and expenditure, discussing assumptions and calculation methodology with management
- Test the identified significant accounting estimates to confirm appropriateness and consistency with supporting records considering evidence of bias.
- Sample test material revenue and expenditure streams with a focus on assets and liabilities at the year-end.
- Testing of revenue cut-off at the period end date.
- Conduct testing to identify unrecorded liabilities at the year-end.
- Testing a sample of Property Plant and Equipment additions to confirm that the expenditure has been appropriately capitalised.

Testing of revenue and expenditure will be supported through the use of data analytics tools to support sample selection. The data analysis tools enable the full population of income and expenditure to be included within the sample population. The population will be filtered to enable testing to focus on higher risk areas, high value and unusual transactions.

Current status

Our work is broadly complete in this area and we currently have no items that will, or are likely to, be brought to your attention.

Our response to significant risks (continued)

Misstatements due to fraud or error*

Financial statement impact

Misstatements that occur in relation to the risk of fraud or error could affect both the Comprehensive Income and Expenditure Statement and the Balance Sheet. We deem the risk to be most prevalent when reviewing journals involved in the Financial Statement Close Process.

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 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 otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What will we do?

We will carry out substantive procedures in response to this risk. The procedures designed to address the identified risk are set out below:

- Identifying fraud risks during the planning stages.
- Inquiry of management about risks of fraud and the controls put in place to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- Determining an appropriate strategy to address those identified risks of fraud.
- Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements.
- Testing of journals from the accounting period that are identified from application of specified audit risk criteria.
- Consider the existence of significant unusual transactions during the year, and performing review and testing as required.
- Consider the results of testing relating to revenue and expenditure recognition in order to identify indicators of management override of controls.

Current status

Our work is broadly complete in this area and we currently have no items that will, or are likely to, be brought to your attention.

Other areas of audit focus

What is the risk/area of focus?	What will we do?
Pension Liability Valuation The Local Authority Accounting Code of Practice and IAS19 requires the entity to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by South Yorkshire Pensions Authority (SYPA). The deficit is a material estimated balance and the Code requires that this liability be disclosed on the balance sheet. At 31 March 2019 this totalled £42.5 million. The information disclosed is based on the IAS 19 report issued to management by the actuary to SYPA (Mercers). Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates. The Combined Authority, as a standalone entity became a constituent employing authority for the first time in 2019/20. We understand that there is no opening deficit being inherited by the Combined Authority for the staff who have transferred under TUPE arrangements.	We will: • Liaise with the auditors of SYPA, to obtain assurances over the information supplied to the actuary in relation to the Group; • Agree the nil opening position for the staff who have transferred to the Combined Authority on 1 April 2019 to notification from SYPA; • Assess the work of the Pension Fund actuary (Mercers) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team; and • Review and test the accounting entries and disclosures made within the Group's financial statements in relation to IAS19.

Current status
We are not in a position to provide any conclusive statements in this area. Our work in this area will require assessment of the work performed by the auditors of South Yorkshire Pensions Authority, which is not yet finished.

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements.

What is the risk/area of focus?	What will we do?
Valuation of Land and Buildings The fair value of Property, Plant and Equipment (PPE) represents a significant balance in the Group's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.	We will: • Consider the work performed by the Group's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work; • Sample testing key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre); • Consider the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code. We have also considered if there are any specific changes to assets that have occurred and that these have been communicated to the valuer; • Review assets not subject to valuation in the year to confirm that the remaining asset base is not materially misstated; • Consider changes to useful economic lives as a result of the most recent valuation; and • Test accounting entries have been correctly processed in the financial statements,

Current status
We have broadly completed our work in this area without any findings to report. Our audit opinion will highlight the disclosed material valuation uncertainty that has been included by the professional external valuer in their report.

Other areas of audit focus (continued)

What is the risk/area of focus?	What will we do?
Preparation for IFRS16 – leases IFRS 16 Leases was issued by the IASB in 2016. Its main impact is to remove (for lessees) the traditional distinction between finance leases and operating leases. Finance leases have effectively been accounted for as acquisitions (with the asset on the balance sheet, together with a liability to pay for the asset acquired). In contrast, operating leases have been treated as "pay as you go" arrangements, with rentals expensed in the year they are paid. IFRS 16 requires all substantial leases to be accounted for using the acquisition approach, recognising the rights acquired to use an asset. Implementation of IFRS 16 will be included in the Code of Practice on Local Authority Accounting in the United Kingdom (the Code) for 2020/21. This Code has yet to published, but in July 2019 CIPFA/LASAAC issued 'IFRS 16 leases and early guide for practitioners'. This early guidance provides comprehensive coverage of the requirements of the forthcoming provisions, including: • the identification of leases • the recognition of right-of-use assets and liabilities and their subsequent measurement • treatment of gains and losses • derecognition and presentation and disclosure in the financial statements, • the management of leases within the Prudential Framework. The guidance also covers the transitional arrangements for moving to these new requirements, such as: • the recognition of right-of-use assets and liabilities for leases previously accounted for as operating leases by lessees • the mechanics of making the transition in the 2020/21 financial statements (including the application of transitional provisions and the preparation of relevant disclosure notes).	IFRS 16 – leases introduces a number of significant changes which go beyond accounting technicalities. For example, the changes have the potential to impact on procurement processes as more information becomes available on the real cost of leases. The key accounting impact is assets and liabilities in relation to significant lease arrangements previously accounted for as operating leases will be recognised on the balance sheet. Although the new standard will not be included in the CIPFA Code of Practice until 2020/21, work will be necessary to secure information required to enable authorities to fully assess their leasing position and ensure compliance with the standard from 1 April 2020. In particular, full compliance with the revised standard for 20/21 is likely to require a detailed review of existing lease and contract documentation prior to 1 April 20 in order to identify: • all leases which need to be accounted for • the costs and lease term which apply to the lease • the value of the asset and liability to be recognised as at 1 April 2020 where a lease has previously been accounted for as an operating lease. We will discuss progress made in preparing for the implementation of IFRS 16 – leases with the finance team over the course of our 2019/20 audit.

Current status
Due to the COVID-19 outbreak, the decision has been made to defer implementation of IFRS 16 by 12 months, therefore we have nothing further to report in our 19/20 audit cycle.

Other matters

What is the risk/area of focus?	What will we do?
Going Concern Compliance with ISA 570 This auditing standard has been revised in response to enforcement cases and well-publicised corporate failures where the auditor's report failed to highlight concerns about the prospects of entities which collapsed shortly after. The revised standard is effective for audits of financial statements for periods commencing on or after 15 December 2019, which for the Group will be the audit of the 2020/21 financial statements. The revised standard increases the work we are required to perform when assessing whether the Group is a going concern. It means UK auditors will follow significantly stronger requirements than those required by current international standards; and we have therefore judged it appropriate to bring this to the attention of the Audit and Standards Committee . The CIPFA Guidance Notes for Practitioners 2019/20 accounts states 'The concept of a going concern assumes that an authority's functions and services will continue in operational existence for the foreseeable future. The provisions in the Code in respect of going concern reporting requirements reflect the economic and statutory environment in which local authorities operate. These provisions confirm that, as authorities cannot be created or dissolved without statutory prescription, they must prepare their financial statements on a going concern basis of accounting.' 'If an authority were in financial difficulty, the prospects are thus that alternative arrangements might be made by central government either for the continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year. As a result of this, it would not therefore be appropriate for local authority financial statements to be provided on anything other than a going concern basis.'	The revised standard requires: • auditor's challenge of management's identification of events or conditions impacting going concern, more specific requirements to test management's resulting assessment of going concern, an evaluation of the supporting evidence obtained which includes consideration of the risk of management bias; • greater work for us to challenge management's assessment of going concern, thoroughly test the adequacy of the supporting evidence we obtained and evaluate the risk of management bias. Our challenge will be made based on our knowledge of the Authority obtained through our audit, which will include additional specific risk assessment considerations which go beyond the current requirements; • improved transparency with a new reporting requirement for public interest entities, listed and large private companies to provide a clear, positive conclusion on whether management's assessment is appropriate, and to set out the work we have done in this respect. While Sheffield City Region Mayoral Combined Authority is not one of the three entity types listed, we will ensure compliance with any updated reporting requirements; • a stand back requirement to consider all of the evidence obtained, whether corroborative or contradictory, when we draw our conclusions on going concern; and • necessary consideration regarding the appropriateness of financial statement disclosures around going concern. The revised standard extends requirements to report to regulators where we have concerns about going concern. We will discuss the detailed implications of the new standard with finance staff during 2019/20 ahead of its application for 2020/21.

Current status
Outlined further in section 03.

Other areas of audit focus (SYPTE only)

What is the risk/area of focus?	What will we do?
Financial Ledger upgrade SYPTE has upgraded the Epicor General Ledger system from version 7.4 to version 10, with the new system going live in January 2020. We will be required to perform procedures over the transfer of data to obtain assurance that the financial statements are based on a complete set of transactions.	We will: • Review work performed by management and internal audit to obtain assurance over the completeness of the data transfer; • Review and test the reconciliations performed between systems as part of the data transfer; and • Liaise with our IT audit colleagues to support us in obtaining assurance that data transferred between systems is complete and accurate.

Current status
Our work in this area has been completed. We have performed checks on the completeness of data transfers including substantive procedures to agree balances between systems. In order to achieve efficiencies, we planned alongside management that our data analytics work was performed in two distinct and separate parts. This meant that the data extraction exercises required to obtain transaction populations for testing, was done in a way that eliminated the need for reconciling our interim testing to the testing performed at our final accounts visit. The remaining data analytics work to assess completeness of data was therefore able to utilise the same approach to completeness as our substantive audit work. We have no findings to report to the Audit and Standards Committee in relation to this work. Due to their being additional work necessary in performing additional testing and two sets of data analytics work, our final Audit Results Report will include a proposed Scale Fee Variation.

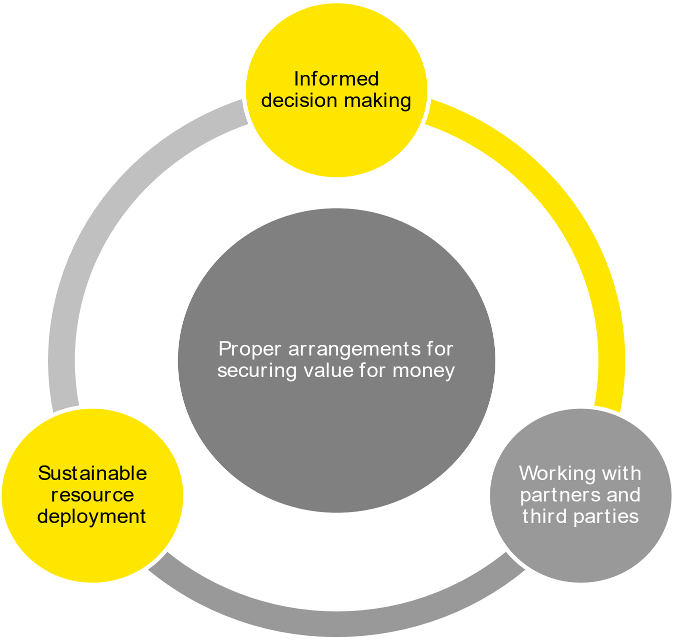
03 Audit Report

Status of opinion

Current status
The work required to be completed in relation to the area of focus around IAS 19 Pension Liability Valuation, means that we are currently unable to provide an accurate assessment of the opinion we are likely to be able to provide on the financial statements. There are a range of issues that may arise, which are out of the control of the Authority. In other areas, the COVID-19 outbreak has increased uncertainty in markets; the professional valuer for the Authority's PPE, has identified a material valuation uncertainty, as raised by all RICS members, which should be disclosed by management. The inclusion of this statement will mean that we will draw attention to this uncertainty in our Audit Opinion. Similarly, COVID-19 has increased the likelihood of changes, namely reductions, to the funding of Public Sector bodies. We have done, and will continue to do, work to assess the going concern status of the Authority in relation to the cashflow forecasting and short to medium-term financial sustainability. We have also performed a thorough review of the disclosures made by management in relation to the issues being raised by the pandemic and its impact on service potential, use of reserves and the strain it may put on the constituent authorities who fund the Authority. Our current view, although subject to change, is that the disclosures provide a clear and balanced view of the impact of COVID-19 and what it means for the Authority in the current term. The pervasive nature of this event means that we are likely to draw attention to these disclosures in our audit report. Both of the above would be regarded to modifications to our audit report whilst allowing us to still provide, notwithstanding other issues noted, a clean opinion on the financial statements.

04 Value for Money Risks

Value for Money



Background

We are required to consider whether the Combined Authority has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

For 2019/20 this is based on the overall evaluation criterion:

“In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people”

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

Overall conclusion

We did not identify any significant risks around these criteria.

We therefore expect having no matters to report about your arrangements to secure economy, efficiency and effectiveness in your use of resources.

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