



# Audit Completion Report

Sunderland City Council

Year ending 31 March 2019



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Our reports are prepared in the context of the 'Statement of responsibilities of auditors and audited bodies' and the 'Appointing Person Terms of Appointment' issued by Public Sector Audit Appointments Limited.

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Sunderland City Council  
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SR2 7DN

15 July 2019

Dear Members

**Audit Completion Report – year ended 31 March 2019**

We are pleased to present our Audit Completion Report for the year ended 31 March 2019. The purpose of this document is to summarise our audit conclusions.

The scope of our work, including identified significant audit risks, key audit matters and other areas of management judgement, was outlined in our Audit Strategy Memorandum which we presented on 8 February 2019. We have reviewed our Audit Strategy Memorandum and concluded that the original significant audit risks, key audit matters and other areas of management judgement remain appropriate.

We would like to express our thanks for the assistance of your team during our audit.

If you would like to discuss any matters in more detail then please do not hesitate to contact me on 0191 383 6314 or 0781 375 2053.

Yours faithfully



Cameron Waddell  
For and on behalf of Mazars LLP

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# 1. EXECUTIVE SUMMARY

## Purpose of this report and principal conclusions

The Audit Completion Report sets out the findings from our audit of Sunderland City Council ('the Council') for the year ended 31 March 2019, and forms the basis for discussion at the Audit and Governance Committee meeting on 26 July 2019.

The detailed scope of our work as your appointed auditor for 2018/19 is set out in the National Audit Office's (NAO) Code of Audit Practice. Our responsibilities and powers are derived from the Local Audit and Accountability Act 2014 and, as outlined in our Audit Strategy Memorandum, our audit has been conducted in accordance with International Standards of Auditing (UK) and means we focus on audit risks that we have assessed as resulting in a higher risk of material misstatement.

Sections 3 and 6 of this report outline the detailed findings from our work on the financial statements and our conclusion on the Council's arrangements to achieve economy, efficiency and effectiveness in its use of resources. Section 3 also includes our conclusions on the audit risks and areas of management judgement in our Audit Strategy Memorandum, which include:

- Property, Plant and Equipment and Investment Properties valuations (Key Audit Matter);
- defined benefit liability valuation (Key Audit Matter);
- management override of control;
- revenue recognition: fees, charges and other income;
- valuation of unquoted equity instruments (including the airport shares); and
- impairment of debtors allowance.

## Status of our work

As we outline on the following page, our work is substantially complete. Subject to the satisfactory completion of the outstanding work, at the time of issuing this report we have the following conclusions:

### Opinion on the financial statements

We anticipate issuing an unqualified opinion, without modification, on the financial statements. Our proposed audit opinion is included in the draft auditor's report in Appendix B.

### Value for Money conclusion

We anticipate concluding that the Council had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources, except for the areas assessed as inadequate by Ofsted in their report on children's services in July 2018. Our draft auditor's report, including proposed conclusion, is provided in Appendix B.

### Whole of Government Accounts (WGA)

We anticipate completing our work on your WGA submission, in line with the group instructions issued by the NAO, by the deadline of 13 September 2019. We anticipate reporting that the WGA submission is consistent with the audited financial statements.

### Wider powers

The 2014 Act requires us to give an elector, or any representative of the elector, the opportunity to question us about the accounting records of the Council and to consider any objection made to the accounts. There have been no objections or questions from local electors during the audit.

# 1. EXECUTIVE SUMMARY

## Status of our audit work

We have substantially completed our work on the financial statements and Value for Money conclusion for the year ended 31 March 2019.

Given the very tight timescales between the publication of the draft financial statements (on 31 May 2019) and the final date for issuing our audit report in compliance with the statutory timetable (31 July 2019), our work will continue up to the point of signing off. At the time of preparing this report the following matters remain outstanding:

Audit area	Status	Description of outstanding matters
Pensions	Green	Work to be finalised; consideration of the revised pension liabilities arising as a result of the McCloud judgement which have already been reflected in the revised financial statements. The assurance from the Pension Fund auditor has not yet been received and considered.
Property, plant and equipment and investment properties	Amber	Work to be finalised including consideration of the Council's rolling programme and the Valuer's overall report.
Other areas	Green	Our work is on-going in a number of areas, including the valuation of unquoted equity investments and some disclosure notes. We are also completing cut-off testing.
Group accounts	Green	Work to be finalised, including final assurance from the significant component auditor.
Closing procedures	Green	Review and closure processes, including consideration of post balance sheet events and checking the revised financial statements.

## Status key

R = likely to result in material adjustment or significant change to disclosures within the financial statements

A = potential to result in material adjustment or significant change to disclosures within the financial statements

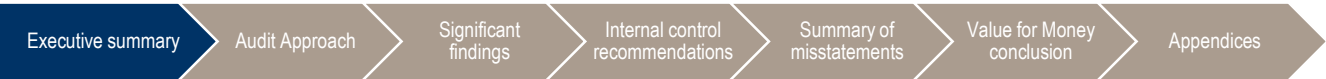
G = not considered likely to result in material adjustment or change to disclosures within the financial statements

We will provide the Audit and Governance Committee with an update in relation to these outstanding matters in a follow-up letter, prior to signing the auditor's report.

## Misstatements and internal control recommendations

Section 4 sets out the internal control recommendations that we make, together with an update on any prior year recommendations.

Section 5 outlines the misstatements noted as part of our audit as at the time of issuing this report. If any additional misstatements are noted on completion of the outstanding work, these will be reported to the Audit and Governance Committee in a follow-up letter.



# 2. AUDIT APPROACH

## Our audit approach

We provided details of our intended audit approach in our Audit Strategy Memorandum (ASM) in January 2019. We have not made any changes to our audit approach since we presented our Audit Strategy Memorandum, other than the following:

- appointment of our own expert to consider the valuation of Newcastle Airport shares (for which the Council obtained an external expert's valuation); and
- considering the impact of the buy-out of Siglion (changing from a joint venture to a wholly owned subsidiary – however no impact overall on our group audit approach).

## Materiality

We set materiality at the planning stage of the audit at £14.722 million for the Group financial statements and £14.077 million for the Council financial statements, using a benchmark of 2% of gross expenditure at the Surplus/Deficit at Net Cost of Services level.

Our final assessment of materiality, has been updated based upon the final 2018/19 financial statements. Qualitative factors are unchanged from that at the planning stage for both the Group and Council financial statements. Qualitative factors considered included the level of understanding of key stakeholders of materiality and inherent uncertainties and judgements in the financial statements as well as taking into account the Council being classed as a 'public interest entity'.

Our final materiality levels are set out in the table below including our trivial threshold (the level under which individual errors are not communicated to the Audit and Governance Committee which is based on 3% of overall materiality).

Materiality element	Group materiality £000s	Council single-entity materiality £000s
Overall materiality	13,861	13,320
Performance materiality	10,811	10,389
Trivial threshold for reporting to Audit and Governance Committee	416	400

We have also calculated materiality for specific classes of transactions, balances or disclosures where we determine that adjustments of a lesser amount than materiality for the financial statements as a whole, could reasonably be expected to influence the decisions of users taken on the basis of the financial statements. We set specific materiality for the following items of account/disclosures:

Item of account/disclosure	Basis of materiality	Specific materiality £000s
Officers' remuneration	25% of total	221
Officers' remuneration (bandings table)	Bandings (£5,000)	5
Members' allowances and expenses	25% of total	287
Exit packages (termination benefits) – single entity	25% of total	564
Exit packages (termination benefits) – Group (including single entity)	25% of total	874

## 2. AUDIT APPROACH

### Key summary of audit approach and findings

We have summarised the key information regarding our approach, risks and significant findings for the Comprehensive Income & Expenditure Statement and Balance Sheet in the table below. Further information on the findings is provided in sections 3 and 5.

Account area	Material misstatement risk	Risk description	Key Audit Matter	Changes to audit approach	Internal control issue arising	Significant audit findings / recommendations
CIES: net cost of services – single entity	Significant	Revenue recognition – fees, charges and other income only	No	None	Yes	Amendment as a result of accrual for pensions liabilities (McCloud). Recommendation (medium) raised in respect of evidencing senior officers' review of material journals. Recommendation (medium) also raised in respect of evidencing income assessments for housing benefits expenditure.
CIES: net cost of services – group	Significant	Revenue recognition – fees, charges and other income only	No	None	No	As per above. No net impact, but amendment between three lines in the Group due to consolidation adjustment required.
Other operating expenditure	Standard	-	No	None	No	
Financing and Investment I&E	Standard	-	No	None	No	Amendment as a result of change in valuation basis of the Council's investment in Siglion (see long-term investments below). Also amendment as a result of accrual for pensions liabilities (McCloud).
Taxation and non-specific grant I&E	Standard	-	No	None	No	
Property, Plant and Equipment / Investment Properties	Significant (Key Audit Matter)	Valuations	Yes	None	No	Brought forward non-material valuations error. Amendment to Group balance sheet for omitted leisure centre.
Long-term Investments	Enhanced	Valuation of unquoted equity investments	No	None	No	Adjusted non-material misstatement – changing valuation basis of Siglion investment from fair value to 'at cost'. Impacting on Group and single entity Balance Sheets and also both Movement in Reserves Statements.



## 2. AUDIT APPROACH (CONTINUED)

Account area	Material misstatement risk	Risk description	Key Audit Matter	Changes to audit approach	Internal control issue arising	Significant audit findings / recommendations
Long-term debtors	Standard	-	No	None	No	
Short-term investments	Standard	-	No	None	No	Level 3 (low) recommendation raised – evidencing monthly reconciliation review.
Debtors	Enhanced	Enhanced risk for impairment of debtors allowance only	No	Yes	No	
Cash and cash equivalents	Standard	-	No	None	Yes	Amended presentation so overdraft not shown separately. Level 3 (low) recommendation raised in respect of completeness of bank confirmations.
Borrowing	Standard	-	No	Yes	Yes	Recommendation as set out for short-term investments.
Creditors	Standard	-	No	None	No	
Provisions	Standard	-	No	None	No	
Defined benefit pension liability	Significant (Key Audit Matter)	High estimation uncertainty	Yes	None	No	Amendment to include pensions liabilities in respect of the McCloud judgement. Amendment to correct several disclosure errors (no net impact).
PFI liabilities	Standard	-	No	None	No	
Usable reserves	Standard	-	No	None	No	
Group reserves	Standard	-	No	None	No	
Unusable Reserves	Standard	-	No	None	No	Amendments for: pensions, Siglion valuation basis change and omitted leisure centre as set out earlier.

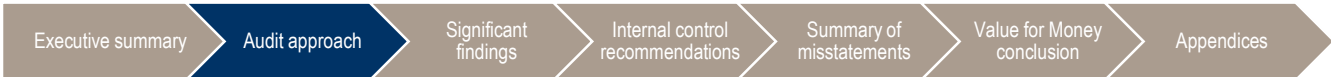


## 2. AUDIT APPROACH (CONTINUED)

### Overview of our group audit approach

Our Audit Strategy memorandum provided details of our intended group audit approach, including our initial assessment of group materiality. The table below confirms the approach we have taken to auditing the Council's consolidated financial statements.

Entity	Nature of entity audit	Auditor	Description of audit procedures undertaken on the component	Changes to audit approach
Sunderland City Council (parent)	NAO Code audit	Mazars LLP	Full scope audit as described in this report.	None
Together for Children Sunderland Limited (subsidiary)	Full scope audit and review of key component auditor working papers.	Robson Laidler LLP	Identified as a significant component. <ul style="list-style-type: none"><li>We set a component materiality level and discussed significant risks with the component auditor.</li><li>We ensured that the statutory audit of this significant component provided sufficient assurance for the group audit.</li><li>We reviewed the work of the component auditor to ensure that the work was completed satisfactorily.</li></ul>	None
Sunderland Care and Support Ltd (SCAS) (subsidiary)	Group analytical procedures	Mazars LLP	Analytical procedures at group audit level; review of the consolidation process; reasonableness checks; review of consolidation adjustments and disclosures.	None.
Sunderland Homes Ltd (subsidiary)	Group analytical procedures	Robson Laidler LLP	Analytical procedures at group audit level; review of the consolidation process; reasonableness checks; review of consolidation adjustments and disclosures.	None.
Siglion LLP – developments and investment companies (subsidiary)	Group analytical procedures	Robson Laidler LLP	Analytical procedures at group audit level; review of the consolidation process; reasonableness checks; review of consolidation adjustments and disclosures. We note the change from a joint venture to a 100% owned subsidiary, following the Council's buy-out of the partner's share of Siglion. No impact on our testing strategy; valuation of the Council's investment in Siglion already an area identified as an enhanced risk.	None.
Sunderland Lifestyle Partnership Limited (joint venture)	Specified audit procedures in respect of the leisure assets accounting adjustment upon consolidation.	RSM UK	Identified as a material but not significant component, with review of consolidation adjustments including revaluation of the leisure assets in 2018/19. Analytical procedures at group audit level; review of the consolidation process; reasonableness checks; review of consolidation adjustments and disclosures.	None.
IAMP (International Advanced Manufacturing Park) LLP (joint venture)	Group analytical procedures	Robson Laidler LLP	Analytical procedures at group audit level; review of the consolidation process; reasonableness checks; review of consolidation adjustments and disclosures.	None.

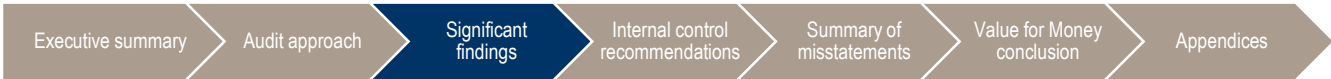


### 3. SIGNIFICANT FINDINGS

This section sets out the significant findings from our audit. These findings include:

- our findings on key audit matters, including:
  - why the matter was considered to be one of the most significance to the audit and therefore determined to be a key audit matter;
  - how the matter was addressed in the audit. including a summary of our response;
  - where relevant, key observations arising with respect to each matter; and
  - a clear reference to the relevant disclosures in the financial statements.
- our audit conclusions regarding significant risks and key areas of management judgement outlined in the Audit Strategy Memorandum;
- our comments in respect of the accounting policies and disclosures that you have adopted in the financial statements. On page 13 we have concluded whether the financial statements have been prepared in accordance with the financial reporting framework and commented on any significant accounting policy changes that have been made during the year;
- any further significant matters discussed with management; and
- any significant difficulties we experienced during the audit.

As part of our planning procedures we considered the risks of material misstatement in the Council’s financial statements that required special audit consideration. Although we report identified key audit matters and significant risks at the planning stage of the audit in our Audit Strategy Memorandum, our risk assessment is a continuous process and we regularly consider whether new key audit matters and significant risks have arisen and how we intend to respond to these risks. No new risks have been identified since we issued our Audit Strategy Memorandum.



# 3. SIGNIFICANT FINDINGS

## Key audit matters

<b>Key audit matter:</b> <b>defined benefit liability valuation</b>	<p><b>Description of the key audit matter</b></p> <p>The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.</p> <p>Due to the high estimation uncertainty of pension calculations, we consider this to be a 'key audit matter'.</p>
	<p><b>How we addressed the key audit matter:</b></p> <ul style="list-style-type: none"><li>• we critically assessed the competency, objectivity and independence of the Actuary;</li><li>• we liaised with the auditors of the Pension Fund to gain assurance that the controls in place at the Pension Fund were operating effectively;</li><li>• we gained assurance over the processes and controls put in place by management to ensure data provided to the Actuary by the Pension Fund for the purposes of the pension valuation was complete and accurate;</li><li>• reviewed the appropriateness of the pension asset and liability valuation methodologies applied by the Pension Fund Actuary and the key assumptions included within the valuation;</li><li>• we compared assumptions to expected ranges, using information provided by the consulting actuary engaged by the National Audit Office;</li><li>• we agreed the data in the Actuary's valuation report for accounting purposes to the pension accounting entries and disclosures in the Council's financial statements; and</li><li>• we challenged the Council on the completeness of pension liabilities in relation to the McCloud judgement and guaranteed minimum pension equalisation.</li></ul> <p>The Council has amended its financial statements for additional pension liabilities arising from the McCloud judgement and other disclosure points. We have gained the assurance sought with no other significant issues arising.</p>
	<p><b>Observations and conclusions</b></p> <p>Subject to completion of outstanding work and the amendments detailed in section 5 (in respect of the McCloud judgement as well as other amendments impacting on the disclosures only), we have obtained the assurance required, with no other significant issues arising we are required to highlight to you.</p>

### 3. SIGNIFICANT FINDINGS (CONTINUED)

#### Key audit matters (continued)

Key audit matter: Property, Plant and Equipment and Investment Property valuations	Description of the key audit matter
	<p>The financial statements contain material entries on the balance sheet as well as material disclosure notes in relation to the Council's holding of Property, Plant and Equipment (PPE) and Investment Properties. Due to the volatility of valuations, we consider this area to be a 'key audit matter'.</p> <p>The Council employs a valuation expert to provide information on valuations, however there remains a high degree of estimation uncertainty associated with the (re)valuations of PPE and Investment Properties due to the significant judgements and number of variables involved.</p>
	<p><b>How we addressed this key audit matter:</b></p> <ul style="list-style-type: none"><li>• we critically assessed the Council's arrangements for ensuring that PPE and Investment Property valuations are reasonable;</li><li>• we critically assessed the data provided by Gerald Eve (an expert commissioned by the NAO), as part of our challenge of the reasonableness of the valuations provided by the Council's Valuer;</li><li>• we considered the competence, skills and experience of the Valuer and the instructions issued to the Valuer, including checking whether planned revaluations had taken place;</li><li>• substantively tested capital expenditure additions and disposals during the year;</li><li>• substantively tested the Council's PPE and Investment Properties to gain assurance that they existed and were owned by the Council;</li><li>• substantively tested revaluations, including critically reviewing the Council's own consideration of assets not revalued in the year and why they were not materially misstated; and</li><li>• where necessary, performed further audit procedures on individual assets to ensure the basis of valuations was appropriate.</li></ul>
	<p><b>Observations and conclusions</b></p> <p>Testing identified an omitted leisure centre from the Group balance sheet consolidation adjustment for the leisure joint venture. Subject to the completion of our testing, there are no significant issues arising from our work to date that we are required to report to you.</p>

### 3. SIGNIFICANT FINDINGS (CONTINUED)

#### Significant risks

<b>Significant risk: management override of controls</b>	<b>Description of the risk</b> <p>Management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur there is a risk of material misstatement due to fraud on all audits.</p>
	<b>How we addressed this risk</b> <p>We addressed the management override of controls risk through performing audit work over accounting estimates, journal entries and significant transactions outside the normal course of business or otherwise unusual.</p> <p>We raised a recommendation during the audit that senior officers carry out a review of material journals during the year; this was appropriately actioned.</p>
	<b>Audit conclusion</b> <p>There are no significant issues arising from our work that we are required to report to you.</p>

<b>Significant risk: risk of fraud in revenue recognition - fees, charges and other income</b>	<b>Description of the risk</b> <p>Our audit methodology incorporates this risk as a significant risk at all audits, although based on the circumstances of each audit, it is rebuttable. We have concluded that we can rebut the presumption of a revenue recognition risk for the majority of the Council's revenue streams, consisting largely of taxation, business rates and grant income.</p> <p>However, we do not feel that sufficient scope exists to rebut this risk in respect of the recognition of fees, charges and other income. This does not imply that we suspect actual or intended manipulation but that we continue to deliver our audit work with appropriate professional scepticism.</p>
	<b>How we addressed this risk</b> <ul style="list-style-type: none"><li>• we substantively tested fees, charges and other income to ensure they had been correctly classified and recognised;</li><li>• we tested journals; and</li><li>• we obtained direct confirmation of year-end bank balances and tested the reconciliations to the ledger.</li></ul>
	<b>Audit conclusion</b> <p>There are no significant issues arising from our work to date that we are required to report to you.</p>

# 3. SIGNIFICANT FINDINGS (CONTINUED)

## Areas of management judgement

Judgement:  
unquoted equity  
investment  
valuations

Description of the management judgement

The Council has to make judgements in respect of the fair value measurements of unquoted equity investments it holds, including those in Newcastle Airport and several joint ventures.

The underlying accounting requirements are subject to change in 2018/19, which increases the risk in respect of these valuation judgements, therefore they have been assessed as enhanced risks.

How our audit addressed this area of management judgement:

- we critically reviewed the basis of valuation for the Council’s unquoted equity investments; and
- we assessed whether disclosures were in line with the Code of Audit Practice.

Following the audit, the Council decided to change the basis of measurement of its investment in Siglion from fair value to cost, which is permitted by the Code.

Audit conclusion

Subject to the amendments to the financial statements in respect of the changed basis of valuing the Council’s investment in Siglion and the amendments to the valuation of the Airport shares, we have obtained the assurance sought, with no significant issues arising from our work that we are required to report to you.

Judgement:  
impairment of  
debtor’s  
allowance

Description of the management judgement

The Council has disclosed its impairment of debtors allowance as an area of estimation uncertainty.

The underlying accounting requirements are subject to change in 2018/19, which increases the risk in respect of the assumptions and uncertainties relevant to this area, therefore they have been assessed as enhanced risks.

How our audit addressed this area of management judgement:

- we critically reviewed the Council’s calculation of its impairment of debtors allowance; and
- we assessed whether disclosures were in line with the Code of Audit Practice, including any exemptions relevant to non-contractual debt.

Audit conclusion

We have obtained the assurance sought, with no significant issues arising which we are required to report to you.

### 3. SIGNIFICANT FINDINGS (CONTINUED)

#### Qualitative aspects of the Council's accounting practices

The Council is required to prepare its financial statements on a going concern basis by the Code of Practice on Local Authority Accounting (the Code). We have considered the appropriateness of the use of the going concern assumption and have reviewed the Council's accounting policies and disclosures and concluded they comply with the requirements of the Code, appropriately tailored to the Council's circumstances.

The Council has disclosed the changes in respect of financial instruments in its accounting policies due to the implementation of IFRS 9.

Draft accounts were received from the Council by the deadline of 31 May 2019 and were of a good quality and supported by comprehensive working papers.

#### Significant matters discussed with management

Over and above our challenge of management's judgements and assertions made in producing the financial statements, the following significant matters were discussed with management:

- the Council's estimation of the pension liabilities arising in respect of guaranteed minimum pension changes and also following on from the McCloud judgement, noting the Council had already accrued for GMP liabilities;
- the external valuation and the assumptions made in valuing the Airport shares;
- the purchase by the Council of its partner's share of the joint venture Siglion;
- the completeness of the joint venture leisure assets consolidated in the Group balance sheet;
- the required restatement of the Comprehensive Income and Expenditure (and associated notes) to align with the new portfolios arising from the Council's restructuring in 2018/19;
- the useful economic life assigned to the new Northern Spire Bridge; and
- the direct confirmation received from Salix for loans the Council had with them, which was higher than the value the Council had recorded by £1.274 million, which the Council provided evidence to show this was due to an error by Salix.

#### Significant difficulties during the audit

During the course of the audit we did not encounter any significant difficulties and we have had the full co-operation of management.

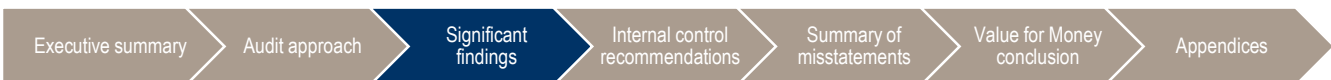
#### Wider responsibilities

Our powers and responsibilities under the 2014 Act are broad and include the ability to:

- issue a report in the public interest;
- make statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

We have not exercised any of these powers as part of our 2018/19 audit.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. There have been no objections or questions from local electors during the audit.





# 4. INTERNAL CONTROL RECOMMENDATIONS

The purpose of our audit is to express an opinion on the financial statements. As part of our audit we have considered the internal controls in place relevant to the preparation of the financial statements. We do this in order to design audit procedures to allow us to express an opinion on the financial statements and not for the purpose of expressing an opinion on the effectiveness of internal controls, nor to identify any significant deficiencies in their design or operation.

The matters reported are limited to those deficiencies and other control recommendations that we have identified during our normal audit procedures and that we consider to be of sufficient importance to merit being reported. If we had performed more extensive procedures on internal controls we might have identified more deficiencies to be reported or concluded that some of the reported deficiencies need not in fact have been reported. Our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

Our findings and recommendations are set out below (including one recommendation arising from our Value for Money conclusion work, reported here for completeness). We have assigned priority rankings to each of them to reflect the importance that we consider each poses to your organisation and, hence, our recommendation in terms of the urgency of required action. In summary, the matters arising fall into the following categories:

Priority ranking	Description	Number of issues
1 (high)	In our view, there is potential for financial loss, damage to reputation or loss of information. This may have implications for the achievement of business strategic objectives. The recommendation should be taken into consideration by management immediately.	0
2 (medium)	In our view, there is a need to strengthen internal controls or enhance business efficiency. The recommendations should be actioned in the near future. <i>Note this includes one recommendation arising from our VfM conclusion work.</i>	3
3 (low)	In our view, internal controls should be strengthened in these additional areas when practicable.	2

## Review of Internal Audit against Public Sector Internal Audit Standards

During the year, the Council requested that we carry out a more comprehensive review of Internal Audit as part of our audit assessment of the Council’s internal control environment. Following discussion of our Audit Strategy Memorandum with the Audit and Governance Committee on 8 February 2019, we have clarified that this work was undertaken as part of the external audit engagement. There were no significant issues arising from this review.



# 4. INTERNAL CONTROL RECOMMENDATIONS (CONTINUED)

## Other deficiencies in internal control - Level 2

### Description of deficiency - housing benefits system walkthrough

Our walkthrough of a new claim within the housing benefits system identified two errors, namely:

- evidence of Child Tax Credit income was not retained on the system as required; and
- the assessment of income incorrectly included a figure for the claimant's capital, resulting in an underpayment of benefit.

We were able to obtain evidence for the Child Tax Credit income at the time of our walkthrough, however this should have been retained on file. We note the assessment of income for benefits is prone to error due to its complexity.

### Potential effects

Non-compliance with DWP subsidy requirements. Incorrect calculation of benefits.

### Recommendation

The Authority should consider strengthening quality assurance and training in relation to the assessment of income.

### Management response

Further instructions and reminders have been issued to staff regarding the retention of evidence of income on a claim and regarding the importance of ensuring that the assessment of income used in the calculation of a claim is correct. More targeted checks on income assessment are planned and any identified areas of concern will be addressed. Training and/or coaching will be delivered where appropriate, and this will be followed up with additional monitoring of staff and procedures.

### Description of deficiency – journal controls

Journals are a key control to prevent and detect fraud and / or error. Within the Council's general ledger, the same person can input and authorise a journal.

There are various controls in place around journals, including a review of year-end journals over £1m by senior officers. This control should be extended to cover the full-year including any year-end journals post-March. It is also important that evidence is retained of this check i.e. a clear audit trail.

### Potential effects

Risk of fraud and / or error.

### Recommendation

The review of material journals should cover the full year, including the closedown period.

### Management response

This was actioned during the year.



# 4. INTERNAL CONTROL RECOMMENDATIONS (CONTINUED)

## Other recommendations on internal control – Level 2 (continued)

### Description of deficiency – reporting actual versus planned savings at the year-end

The Council has robust monitoring arrangements for the delivery of savings required during the year. At the year-end, the Council reports its outturn position overall, which takes into account the achievement of savings. However, it is not clear which savings were achieved and which were compensated for by other budget underspends.

### Potential effects

Lack of clarity on savings, impacting on decision-making.

### Recommendation

The Council should expand existing monitoring reports on planned and actual savings to report on year-end outcomes.

### Management response

The Council has refreshed its budget monitoring and reporting approach with the aims of improved transparency and understandability. This recommendation will be considered in line with these aims.

## Other recommendations on internal control – Level 3

### Description of deficiency – evidence of Treasury Management reconciliation review

A monthly reconciliation of the Treasury Management system to the general ledger is carried out. This is checked and authorised by a second person, however no evidence is retained of this review. Treasury Management is a key system, with highly material figures, therefore such evidence should be retained (this does not have to be via a hardcopy working paper, but could be electronic).

### Potential effects

Risk of fraud and / or error.

### Recommendation

Retain evidence of the approval of the monthly Treasury Management system reconciliation to the general ledger.

### Management response

This has been actioned.



# 4. INTERNAL CONTROL RECOMMENDATIONS (CONTINUED)

## Other recommendations on internal control – Level 3

### Description of deficiency – completeness of bank account confirmations

Testing identified that the direct confirmation provided to us by the Council's bank had omitted one bank account in respect of a school. In this particular case, the letter we received listed all accounts (including schools) where there was a right of set-off in one section of the letter, but had then omitted one of the schools' actual bank balance in the earlier section of the letter in error. Whilst we were able to gain the assurance required, the completeness and accuracy of bank confirmations is an important source of assurance.

### Potential effects

Lack of assurance over bank accounts - a key area.

### Recommendation

The Council should liaise with its relationship manager at the bank to discuss the controls in place for ensuring bank confirmations provided are accurate and complete.

### Management response

This will be actioned.



# 4. INTERNAL CONTROL RECOMMENDATIONS (CONTINUED)

## Follow-up of previous internal control points

We set out below an update on internal control points raised in the prior year (both were level 2 – medium priority).

### Description of deficiency –recording IT assets

We tested an item of £13k within property, plant and equipment relating to IT hardware. We sought to verify the existence of this asset based on the serial number recorded on the invoice however were unable to trace the asset using either the serial number or the invoice details. This was because once the asset is received by the Council it is tagged and assigned an Asset number, which is not based on serial numbers or invoice numbers.

### Potential effects

Without a trail between asset records and invoices, an important element of asset verification is lost.

### Recommendation

The Council should consider recording serial numbers and invoice numbers in the register of IT assets.

### 2018/19 update

Following a more detailed review of the ICT inventory procedure in the wake of this recommendation, management has stated that this recommendation was already in place in that ICT do record the asset tag against serial/invoice numbers, and have done so since 2010.

It would appear in this particular case, the issue was either down to individual error or tracking of the asset though the capital scheme. The Council is looking to improve on the process to ensure it is easier to track individual assets in the future.

There were no similar issues arising from our 2018/19 testing.

### Description of deficiency – IT general controls

We reviewed a sample of starters and leavers to ensure that access controls to key financial systems were properly controlled. Two of the new starters checked in the SAP system were given additional access to that requested on their approval forms. Officers were unable to provide additional documentation to support the additional access rights.

### Potential effects

If access rights are not properly controlled, the integrity of key financial data could be compromised.

### Recommendation

The Council should ensure that all access rights to key systems are properly approved and relevant documentation retained to support this.

### 2018/19 update

Our 2018/19 IT general controls starters testing again identified one person who was not given the level of access requested, with no documented reason for this. In this instance the risk was mitigated as the person was given a lower level of access than requested.

Other than the above issue, there were no significant issues arising from our IT general controls testing.

# 5. SUMMARY OF MISSTATEMENTS

We set out below the misstatements identified for adjustment during the course of the audit, above the level of trivial threshold of £400k (Group trivial threshold of £416k).

The first table outlines the misstatements that were identified during the course of our audit which management has assessed as not being material either individually or in aggregate to the financial statements and does not currently plan to adjust.

The second table outlines the misstatements that have been adjusted by management during the course of the audit.

## Unadjusted misstatements 2018/19

		Comprehensive Income and Expenditure Statement		Balance Sheet	
		Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1	Dr: Property, Plant and Equipment Cr: Revaluation Reserve			2,181	2,181
Being the carried forward extrapolated error as a result of Property, Plant and Equipment testing in 2017/18. Whilst the Council has corrected the specific errors identified from our testing for the assets in question, the extrapolated error still has a carried forward impact in 2018/19.					
Total unadjusted misstatements		0	0	2,181	2,181

## Unadjusted misstatements 2017/18

		Comprehensive Income and Expenditure Statement		Balance Sheet	
		Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1	Dr: Group Property, Plant and Equipment Cr: Group Revaluation Reserve – joint ventures			5,161	5,161
Being an asset omitted from the Group consolidation adjustment for the leisure joint venture. This has been included in the 2018/19 revised financial statements, as shown overleaf.					
Total unadjusted misstatements		0	0	5,161	5,161

## 5. SUMMARY OF MISSTATEMENTS

### Adjusted misstatements 2018/19

		Comprehensive Income and Expenditure Statement		Balance Sheet	
		Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1	Dr: IAS 19 pensions (McCloud)	17,210			
	Dr: Cabinet Secretary	30			
	Dr: Other comprehensive I & E	10,320			
	Cr: Pensions reserve				27,560
Being the omission of employer pension contributions following the McCloud judgement. Being £17.21m in respect of McCloud, plus updated asset return values resulting in an increase of £10.27m. No net impact on the Council's General Fund, with pension costs under IAS 19 being reversed out in the Movement in Reserves Statement and replaced by actual employer pension contributions.					
2	Dr: Group CIES: Children, Learning and Skills (TfC)	2,847			
	Dr: Group CIES: Health & Social Care (SCAS)	2,580			
	Dr: Group CIES: Other comprehensive I & E	1,195			
	Cr: Group Balance Sheet: Pensions liability				6,622
Being amendment to the Group statements for McCloud.					
3	Dr: Other comprehensive I & E	2,328			
	Dr: Financial Instruments Revaluation Reserve			2,759	
	Cr: Long-term investments				5,087
Being the valuation of the Council's long-term investment in Siglion at cost instead of fair value, as permitted by the Code. Impacting on the Movement in Reserves Statement for both the single entity and Group, as well as a number of disclosures.					
4	Dr: Group net cost of services – Health & Social Care	38,980			
	Cr: Group net cost of services – Community & Culture		28,796		
	Cr: Group net cost of services – Environment & Transport		10,184		
Being transposition of Group gross income and expenditure for the three lines shown above. No impact on Group total net cost of services.					
5	Dr: Cash and Cash Equivalents (overdrawn)			9,272	
	Cr: Cash and Cash Equivalents (in hand & bank)				9,272
Being amendment to the presentation of cash and cash equivalents, due to right of 'set-off' existing.					
6	Dr: Group Balance Sheet – Property, Plant and Equipment			5,800	
	Cr: Group Balance Sheet – Revaluation Reserve: joint ventures				5,800
Being omitted asset from the Group consolidation adjustment for the leisure joint venture.					
7	Dr: Financial Instruments Revaluation Reserve			7,892	
	Cr: Long-term investments				7,892
Being amendment to the valuation of the Airport shares.					



# 5. SUMMARY OF MISSTATEMENTS (CONTINUED)

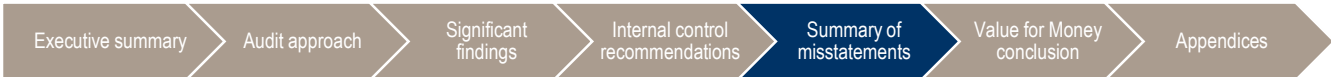
## Disclosure amendments

The Council has amended the disclosures for various minor points and presentational issues. The most significant disclosure amendments are summarised below.

- **Note 3 critical judgements:** amendment to include the judgement in respect of pensions liabilities (McCloud judgement).
- **Note 4 assumptions:** various amendments to clarify assumptions.
- **Note 8 Expenditure and Funding analysis** (consisting of three tables): amendment to the first table to ensure it reconciles with the second table.
- **Note 15 financial instruments:** various amendments, including narrative to clarify the changes as a result of implementing IFRS 9.  
Amendment to the valuation basis of the Council's investment in Siglion from fair value to cost.  
Amendment to the income, expense, gains and losses table to reflect new Code requirements.  
Amendment to the fair value disclosures for PWLB debt due to a transposition error (no impact on the balance sheet).
- **Note 33 related party transactions:** various amendments to update disclosures.
- **Note 40 pensions:** various amendments, including for the impact of the additional liabilities accrued in respect of the McCloud judgement, as shown on preceding page.  
Amendment to correct a transposition error in respect of the past service cost lines (no net impact).  
Amendment to presentation of employer deficiency payments (no net impact).
- **Note 43 nature and extent of risks of financial instruments:** minor amendments.

## Group disclosure amendments

- **Group reconciliation:** amendments to line descriptors to clarify they represent 'total comprehensive income and expenditure' and not 'profit and loss'.
- **Group disclosures:** various amendments to clarify group disclosures and also deletion of non-material notes.



# 6. VALUE FOR MONEY CONCLUSION

## Our approach to Value for Money

We are required to form a conclusion as to whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider.

The overall criterion is that, ‘in all significant respects, the Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.’ To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- informed decision-making;
- sustainable resource deployment; and
- working with partners and other third parties.

Commentary against each of the sub-criteria, and an indication of whether arrangements are in place, is provided below, followed by:

- consideration of significant risks identified to our Value for Money conclusion;
- our ‘reality check’;
- and our overall conclusion (as set out in Appendix B).

Sub-criteria	Commentary	Arrangements in place?
Informed decision-making	<p><i>City Plan</i></p> <p>Alongside changes in senior management over the last year, the Council has refreshed its strategic approach, as encapsulated in its new City Plan. The City Plan ‘Sunderland 2019-2030’ will replace the existing Corporate Plan which covers up to and including 2019/20 and will be the Council’s overarching strategic plan for the period 2019/2020 to 2029/2030 as well as for the city’s Strategic Partnership arrangements.</p> <p>The detail behind the new City Plan is currently being developed; it is important that appropriate measures and targets are in place to help the Council measure progress and inform its decision-making.</p> <p><i>Medium-term financial strategy</i></p> <p>The Council has a robust medium-term financial strategy in place, supported by regular financial reporting in the year. We comment further on the financial resilience of the Council overleaf.</p> <p><i>Risk assurance and mapping</i></p> <p>The Council’s system of internal control is subject to Internal Audit using an in-house function, and for 2018/19, the Council’s internal auditors have given an opinion that there continues to be an adequate system of internal control.</p> <p>The Council continues to develop its risk assurance and mapping, which provides a useful oversight of the activities of the Council, as well as encompassing its interests in other entities.</p> <p>An Audit and Governance Committee is in place to oversee the governance framework, including risk management and internal audit, and approval of the Council’s financial statements.</p>	Yes

# 6. VALUE FOR MONEY CONCLUSION (CONTINUED)

Sub-criteria	Commentary	Arrangements in place?
Sustainable resource deployment	<p>The Council has continued to make good progress in addressing the financial challenges from public sector austerity and has a proven track record of strong budget management and delivering planned budget reductions.</p> <p><i>Financial resilience</i></p> <p>The final revenue outturn for 2018/19 was an underspend of £0.682 million (prior year £0.788 million). This was after making an additional contributions to Together for Children Sunderland Limited to address financial pressures, in particular, demand pressures around the costs of looked after children. It was also after providing additional support for Sunderland Care and Support Limited to support workforce transformation costs.</p> <p>The Council has maintained comparatively healthy levels of usable reserves; these have decreased slightly to £154.022 million as at 31 March 2019 (£159.1 million at 31 March 2018). Although these are earmarked for specific purposes, they do provide flexibility to manage the medium-term financial position.</p> <p>The Council continues to face a funding gap to address in coming years, therefore further savings and / or sources of additional income continue to be required. We comment on this further in the next section on our VfM significant risks.</p> <p><i>Capital programme</i></p> <p>The Council has maintained a substantial capital programme of investment projects. The final outturn for 2018/19 was a capital spend of £80.9 million (prior year £94.1 million), and the capital programme for 2019/20 amounts to £168.9 million. Similar to other local government bodies, there is a degree of slippage in capital projects, resulting in significant changes between the original and revised budgets; this should be kept under review.</p> <p>A major part of the Council's asset management strategy involved transferring its commercial property portfolio to its joint venture local asset-backed vehicle, Siglion LLP, with the aim of accelerating regeneration schemes. Earlier this year, the Council bought out it's partner in Siglion and therefore now wholly owns the company.</p> <p><i>Workforce development</i></p> <p>Going forward, the Council faces the challenge of supporting the cultural change that will be needed, as resources continue to reduce and new ways of working are sought – including the move to the new civic centre when it is built.</p>	Yes

# 6. VALUE FOR MONEY CONCLUSION (CONTINUED)

Sub-criteria	Commentary	Arrangements in place?
Working with partners and other third parties	<p>As set out earlier, the Council's new City Plan sets out its strategic direction, as well as for its strategic partnership arrangements. The City Plan sets out the key challenges facing the Council and is clear that it requires the input of all partners in the city if it is to be delivered.</p> <p>The Council already has well developed partnership arrangements in place, however, a new focus will be needed to deliver the ambitions of the City Plan, with, as set out in the peer review feedback report, alignment of performance and risk management frameworks.</p> <p>Continuing to build upon working arrangements with the local health economy is important, with April 2019 seeing the start of the new 'All Together Better' alliance in Sunderland, which brings together health and social care professionals together in commissioning services in the most effective manner to support individuals.</p> <p>The Council continues to work closely with its various interests, namely:</p> <ul style="list-style-type: none"><li>• Together for Children;</li><li>• Sunderland Care and Support;</li><li>• Sunderland Homes;</li><li>• Siglion;</li><li>• Sunderland Lifestyle Partnership; and</li><li>• International Advanced Manufacturing Park.</li></ul> <p>The use of separate entities and joint ventures by the Council to achieve its aims presents both opportunities and challenges. It is important that good governance arrangements continue to be maintained in respect of these various interests, as well as wider partnership working arrangements.</p> <p>We note the deterioration in arrangements at Together for Children, as highlighted by Ofsted in its recent monitoring letter of June 2019. However, some sub-areas of Children's Services such as fostering, adoption and Children's homes were rated as good or outstanding. We consider this further in our significant risks section overleaf.</p> <p>Sunderland Care and Support, after adjusting for pension liabilities, reported a small profit for 2018/19 and is refreshing its business plan and actively seeking other income streams.</p>	<p>Yes – other than in respect of those aspects of Children's Services rated as inadequate by Ofsted (see significant risks section overleaf)</p>

# 6. VALUE FOR MONEY CONCLUSION (CONTINUED)

## Significant Value for Money risks

The NAO’s guidance requires us to carry out work to identify whether or not a significant risk to the Value for Money conclusion exists. Risk, in the context of our Value for Money work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Council being inadequate. In our Audit Strategy Memorandum, we reported that we had identified two significant Value for Money risks:

- responding to financial pressures; and
- Ofsted’s inspection of Children’s Services.

The work we carried out in relation to significant risks is outlined below.

Risk	Work undertaken	Conclusion
<b>Responding to financial pressures</b>	We reviewed budget monitoring and reporting. We note the refreshed format of budget monitoring and reporting going forward.	We obtained the assurance sought, with no significant issues arising.
The Council faces financial pressures from reduced funding and continues to identify plans to deliver future savings and improvements, including alternative models of service delivery.	We also considered the adequacy of plans that are developed to deliver savings and improvements.  The Council set out it needed to deliver savings of approximately £25 million for 2018/19. This target has been met overall by virtue of the net underspend of £0.682 million.	We highlighted one best practice recommendation, as set out to the left.
Without robust budgetary control and delivery of its action plans, the Council’s financial resilience and service performance could deteriorate.	We note there is regular monitoring of the delivery of savings during the year, but there is no formal year-end position statement on whether planned savings have been delivered as it is considered to be covered via the overall budget monitoring outturn. We would recommend the actual versus planned savings position is formally reported, to aid good decision-making.  The Council has plans to meet the funding gap identified for future years and recognises this remains very challenging, in particular given the scale of savings already delivered to date.  See also our commentary in the previous section.	

# 6. VALUE FOR MONEY CONCLUSION (CONTINUED)

## Significant risks (continued)

Risk	Work undertaken	Conclusion
<b>Ofsted inspection: Children's Services</b>	We considered the progress made by the Council in relation to Children's Services.	Children's Services has been rated as 'inadequate' by Ofsted.
There is a risk Council does not make the required improvements to Children's Services, or does not make the improvements rapidly enough.	<p>This requires an expert judgement, therefore, we have relied on the updated assessment of Ofsted made in July 2018. This concluded that whilst some improvement had been made, their overall assessment remained that Children's Services was 'inadequate'.</p> <p>We note the most recent Ofsted monitoring visit in 2019 which highlighted a deterioration in some areas of performance. However, some sub-areas of Children's Services such as fostering, adoption and Children's homes were rated as good or outstanding</p> <p>The table below shows the results of Ofsted's inspection results from 2015 and 2018.</p>	This will result in a qualification of our VFM conclusion, on an 'except for' basis (i.e. that adequate arrangements are in place, except for those aspects assessed as inadequate by Ofsted).

The table below summarises the outcome from the 2015 and 2018 Ofsted inspection results in respect of Children's Services.

Area		2015 Ofsted inspection results	2018 Ofsted inspection results
1.	Children who need help and protection	Inadequate	Inadequate
2.	Children looked after and achieving permanence	Inadequate	Requires improvement
2.1	Children looked after and achieving permanence - adoption performance	Inadequate	Good
2.2	Children looked after and achieving permanence - experiences and progress of care leavers	Inadequate	Requires improvement
3.	Leadership, management and governance	Inadequate	Inadequate

# 6. VALUE FOR MONEY CONCLUSION (CONTINUED)

## Reality check

Having completed our VfM conclusion work, we carried out a final ‘reality check’, which included consideration of our cumulative knowledge of the Council and, in particular:

- reports by statutory inspectorates, other regulators and external advisors;
- achievement of performance and other targets; and
- performance against budgets and other financial targets.

We do this to identify anything that would make us reconsider our conclusion. We did not identify any such matters.

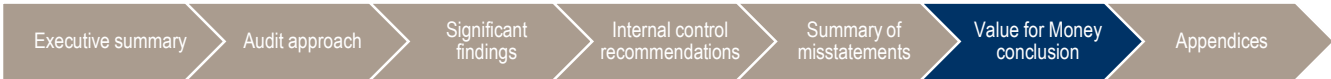
Area	Auditor assessment
Outputs by statutory inspectorates or other regulators	<p><u>Ofsted – Children’s Services</u></p> <p>We note Ofsted’s monitoring visit, reported in June 2019, which highlighted a deterioration in the quality of some services.</p> <p><u>Ofsted – Further Education and Skills</u></p> <p>Ofsted issued a reinspection report in respect of Further Education and Skills at the Council in May 2019, which rated the service as ‘good’ overall, being an improvement from the previous inspection rating of ‘inadequate’.</p> <p><u>Peer review</u></p> <p>The Council’s feedback report following on from its Local Government Association peer review earlier in the year was issued in June 2019. This set out areas of strength as well as recommendations for the Council to consider, linked to the delivery of the new ambitious City Plan.</p>
Achievement of performance and other targets	Nothing arising from our consideration of the Council’s performance, other than where already highlighted, which would impact on our VfM conclusion responsibilities.
Performance against budgets and other financial targets	The Council achieved a small underspend for the year of £0.682m and has maintained comparatively healthy earmarked reserves.

## Our overall Value for Money conclusion

On the basis of our work, with the exception of the matter reported below, we are satisfied that in all significant respects Sunderland City Council put in place proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

The exception to this are the areas of Children’s Services that were identified as ‘inadequate’ in Ofsted’s report to the Council in July 2018, as set out above.

The wording of the Value for Money conclusion is set out in our draft audit report in Appendix B.





# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER

To be provided to us on client headed note paper

[Client address]

[Date]

Dear Cameron

**Sunderland City Council - audit for year ended 31 March 2019**

This representation letter is provided in connection with your audit of the financial statements of Sunderland City Council ('the Council') and its Group for the year ended 31 March 2019 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the Code) and applicable law.

I confirm that the following representations are made on the basis of enquiries of management and staff with relevant knowledge and experience (and, where appropriate, inspection of supporting documentation) sufficient to satisfy myself that I can properly make each of the following representations to you.

**My responsibility for the financial statements and accounting information**

I believe that I have fulfilled my responsibilities for the true and fair presentation and preparation of the financial statements in accordance with the Code and applicable law.

**My responsibility to provide and disclose relevant information**

I have provided you with:

- access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other material;
- additional information that you have requested from us for the purpose of the audit; and
- unrestricted access to individuals within the Council and Group you determined it was necessary to contact in order to obtain audit evidence.

I confirm as Executive Director of Corporate Resources that I have taken all the necessary steps to make me aware of any relevant audit information and to establish that you, as auditors, are aware of this information.

As far as I am aware there is no relevant audit information of which you, as auditors, are unaware.

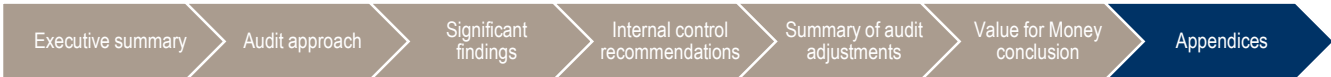
**Accounting records**

I confirm that all transactions that have a material effect on the financial statements have been recorded in the accounting records and are reflected in the financial statements. All other records and related information, including minutes of all Council, Cabinet and committee meetings, have been made available to you.

**Accounting policies**

I confirm that I have reviewed the accounting policies applied during the year in accordance with Code and International Accounting Standard 8 and consider these policies to faithfully represent the effects of transactions, other events or conditions on the Council and Group's financial position, financial performance and cash flows.

[continued]



# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER

### (CONTINUED)

**Accounting estimates, including those measured at fair value**

I confirm that any significant assumptions used by the Council and Group in making accounting estimates, including those measured at current or fair value, are reasonable.

**Contingencies**

There are no material contingent losses including pending or potential litigation that should be accrued where:

- information presently available indicates that it is probable that an asset has been impaired or a liability has been incurred at the balance sheet date; and
- the amount of the loss can be reasonably estimated.

There are no material contingent losses that should be disclosed where, although either or both the conditions specified above are not met, there is a reasonable possibility that a loss, or a loss greater than that accrued, may have been incurred at the balance sheet date.

There are no undisclosed contingent gains which should be disclosed.

All material matters, including unasserted claims, that may result in litigation against the Council and Group have been brought to your attention. All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to you and accounted for and disclosed in accordance with the Code and applicable law.

**Laws and regulations**

I confirm that I have disclosed to you all those events of which I am aware which involve known or suspected non-compliance with laws and regulations, together with the actual or contingent consequences which may arise therefrom.

The Council and Group have complied with all aspects of contractual agreements that would have a material effect on the accounts in the event of non-compliance.

**Fraud and error**

I acknowledge my responsibility as Executive Director of Corporate Resources for the design, implementation and maintenance of internal controls to prevent and detect fraud and error.

I have disclosed to you:

- all the results of my assessment of the risk that the financial statements may be materially misstated as a result of fraud;
- all knowledge of fraud or suspected fraud affecting the Council and Group involving:
  - management and those charged with governance;
  - employees who have significant roles in internal control; and
  - others where fraud could have a material effect on the financial statements.

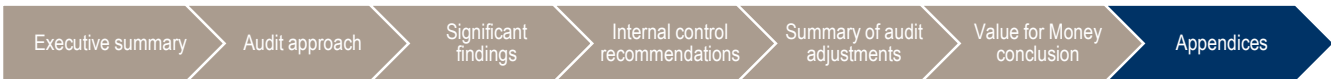
I have disclosed to you all information in relation to any allegations of fraud, or suspected fraud, affecting the Council's and Group's financial statements communicated by employees, former employees, analysts, regulators or others.

**Related party transactions**

I confirm that all related party relationships, transactions and balances, have been appropriately accounted for and disclosed in accordance with the requirements of the Code and applicable law.

I have disclosed to you the identity of the Council and Group's related parties and all related party relationships and transactions of which I am aware.

[continued]



# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER

### (CONTINUED)

**Future commitments**

I am not aware of any plans, intentions or commitments that may materially affect the carrying value or classification of assets and liabilities or give rise to additional liabilities.

**Service concession arrangements**

I am not aware of any material contract variations, payment deductions or additional service charges in 2018/19 in relation to the Council's PFI schemes that you have not been made aware of.

**Subsequent events**

I confirm all events subsequent to the date of the financial statements and for which the Code and applicable law, require adjustment or disclosure have been adjusted or disclosed.

Should further material events occur after the date of this letter which may necessitate revision of the figures included in the financial statements or inclusion of a note thereto, I will advise you accordingly.

**Going concern**

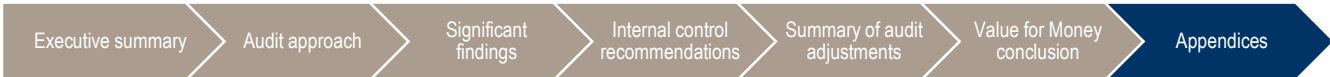
To the best of my knowledge there is nothing to indicate that the Council and Group will not continue as a going concern in the foreseeable future. The period to which I have paid particular attention in assessing the appropriateness of the going concern basis is not less than twelve months from the date of approval of the accounts.

**Unadjusted misstatements**

I confirm that the effects of the uncorrected misstatements are immaterial, both individually and in aggregate, to the financial statements as a whole. All uncorrected misstatements are included as an appendix to this letter.

Yours faithfully

Jon Ritchie  
Executive Director of Corporate Resources



Independent auditor's report to the Members of Sunderland City Council

Report on the financial statements

Opinion

We have audited the financial statements of Sunderland City Council ('the Council') and its subsidiaries and joint ventures ('the Group') for the year ended 31 March 2019, which comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Collection Fund Statement, the Group Movement in Reserves Statement, the Group Comprehensive Income and Expenditure Statement, the Group Balance Sheet, the Group Cash Flow Statement and notes to the Council and Group financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

In our opinion, the financial statements:

- give a true and fair view of the financial position of the Council and the Group as at 31 March 2019 and of the Council's and the Group's expenditure and income for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities section of our report. We are independent of the Council in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applicable to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

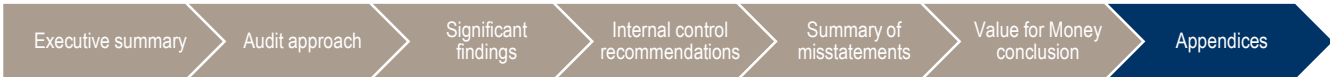
We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Executive Director of Corporate Resources' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Executive Director of Corporate Resources has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Council's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

These key matters were relevant to our audit of the Group financial statements, insofar as the Group consolidates the Council's statements.



# APPENDIX B

## DRAFT AUDITOR’S REPORT (CONTINUED)

Key audit matter	Our response and key observations
<p><b>Valuation of Property, Plant &amp; Equipment and Investment Properties</b></p> <p>The financial statements contain material entries on the balance sheet as well as material disclosure notes in relation to the Council’s holding of Property, Plant and Equipment (PPE) and Investment Properties. Due to the volatility of valuations, we consider this area to be a ‘key audit matter’.</p> <p>The Council employs a valuation expert to provide information on valuations, however there remains a high degree of estimation uncertainty associated with the (re)valuations of PPE and Investment Properties due to the significant judgements and number of variables involved.</p>	<p>How we addressed this key audit matter:</p> <ul style="list-style-type: none"> <li>• we critically assessed the Council’s arrangements for ensuring that PPE and Investment Property valuations are reasonable;</li> <li>• we critically assessed the data provided by Gerald Eve (an expert commissioned by the NAO), as part of our challenge of the reasonableness of the valuations provided by the Council’s Valuer;</li> <li>• we considered the competence, skills and experience of the Valuer and the instructions issued to the Valuer, including checking whether planned revaluations had taken place;</li> <li>• substantively tested capital expenditure additions and disposals during the year;</li> <li>• substantively tested the Council’s PPE and investment properties to gain assurance that they existed and were owned by the Council;</li> <li>• substantively tested revaluations, including critically reviewing the Council’s own consideration of assets not revalued in the year and why they were not materially misstated; and</li> <li>• where necessary, performed further audit procedures on individual assets to ensure the basis of valuations was appropriate.</li> </ul> <p>We have not identified any significant matters from our testing, and we have concluded that the Council’s Property, Plant &amp; Equipment and Investment Properties are materially fairly stated.</p>
<p><b>Valuation of Defined Benefit Pension liability</b></p> <p>The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.</p> <p>Due to the high estimation uncertainty of pension calculations, we consider this to be a ‘key audit matter’.</p>	<p>How we addressed this key audit matter:</p> <ul style="list-style-type: none"> <li>• we critically assessed the competency, objectivity and independence of the Actuary;</li> <li>• we liaised with the auditors of the Pension Fund to gain assurance that the controls in place at the Pension Fund were operating effectively;</li> <li>• we gained assurance over the processes and controls put in place by management to ensure data provided to the Actuary by the Pension Fund for the purposes of the pension valuation was complete and accurate;</li> <li>• reviewed the appropriateness of the pension asset and liability valuation methodologies applied by the Pension Fund Actuary and the key assumptions included within the valuation;</li> <li>• we compared assumptions to expected ranges, using information provided by the consulting actuary engaged by the National Audit Office;</li> <li>• we agreed the data in the Actuary’s valuation report for accounting purposes to the pension accounting entries and disclosures in the Council’s financial statements; and</li> <li>• we challenged the Council on the completeness of pension liabilities in relation to the McCloud judgement and guaranteed minimum pension equalisation.</li> </ul> <p>The Council has amended its financial statements for additional pension liabilities arising from the McCloud judgement and other disclosure points. We have gained the assurance sought with no other significant issues arising.</p>

# APPENDIX B

## DRAFT AUDITOR’S REPORT (CONTINUED)

### Our application of materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures, and in evaluating the effect of misstatements, both individually and on the financial statements as a whole. Based on our professional judgement, we determined materiality for the financial statements of the Council and the Group as a whole as follows:

	Group	Council
Overall materiality	£13.861m	£13.320m
Basis for determining materiality	Materiality has been determined as 2% of gross expenditure at the surplus/deficit on provision of services level.	
Rationale for benchmark applied	Gross expenditure at the surplus/deficit on provision of services level was chosen as the appropriate benchmark as this is a key measure of financial performance for the Council and for users of the financial statements.	
Performance materiality (Note 1)	£10.811m	£10.389m
Reporting threshold – triviality (Note 2)	£0.416m	£0.400m
Specific materiality: officers’ remuneration (25% of total)	n/a	£0.221m
Specific materiality: officers’ remuneration (bandings table)	Correct banding (£5,000 banding)	Correct banding (£5,000 banding)
Specific materiality: Exit Packages (25% of total)	£0.874m	£0.564m

*Note 1: performance materiality is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole.*

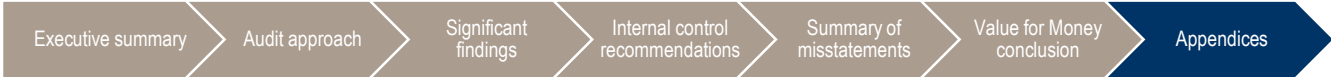
*Note 2: the triviality threshold is the level under which individual errors (unless cumulatively material) are not communicated to the Audit and Governance Committee and is based on 3% of overall materiality.*

### An overview of the scope of our audit

As part of designing our audit, we determined materiality and assessed the risk of material misstatement in the financial statements. In particular, we looked at where the Executive Director of Corporate Resources made subjective judgements such as making assumptions on significant accounting estimates.

We gained an understanding of the legal and regulatory framework applicable to the Council and the sector in which it operates. We considered the risk of acts by the Council which were contrary to the applicable laws and regulations including fraud. We designed our audit procedures to respond to those identified risks, including non-compliance with laws and regulations (irregularities) that are material to the financial statements. We focused on laws and regulations that could give rise to a material misstatement in the financial statements.

We tailored the scope of our audit to ensure that we performed sufficient work to be able to give an opinion on the financial statements as a whole. We used the outputs of our risk assessment, our understanding of the Council’s accounting processes and controls and its environment, and considered qualitative factors in order to ensure that we obtained sufficient coverage across all financial statement line items.



# APPENDIX B

## DRAFT AUDITOR’S REPORT (CONTINUED)

Our tests included, but were not limited to:

- obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by irregularities including fraud or error;
- review of minutes of Council meetings in the year; and
- enquiries of management.

As a result of our procedures, we did not identify any key audit matters relating to irregularities, including fraud.

The primary responsibility for the prevention and detection of irregularities including fraud rests with both those charged with governance and management. As with any audit, there remained a risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal controls.

The Group consists of the Council and six other entities, four of which are 100% Council-owned subsidiaries as at 31 March 2019, other than the two joint ventures, Sunderland Lifestyle Partnership Limited and International Advanced Manufacturing Park LLP. Our approach to auditing the Group was based on our understanding of the Group structure and an assessment of the significance of individual components to the Group financial statements and is summarised in the following table:

Component	% of Group total assets	% of Group total liabilities	% of Group income	% of Group expenditure
The Council	93.60%	92.19%	77.67%	77.14%
Together for Children Limited	1.04%	2.48%	13.92%	14.64%
Sunderland Lifestyle Partnership Limited	0.26%	0.23%	0.20%	0.20%
Other subsidiaries and joint ventures	5.10%	5.10%	8.22%	8.02%
Total	100%	100%	100%	100%

- **The Council:** full scope audit procedures were carried out on the Council.
- **Together for Children Limited (TfC):** Group audit instructions were issued to the auditor of TfC in respect of their full scope audit of the financial statements for the year ended 31 March 2019. Component materiality used is that as set by the component auditor which is below our maximum threshold.
- **Sunderland Lifestyle Partnership Limited (SLP):** the Council’s interest in this joint venture was assessed as a material but not significant component. This is due to the consolidation adjustment for the leisure assets carried out by the Council in producing the Group financial statements being material in terms of Group materiality. We carried out specific procedures on the consolidation adjustment made by the Council in preparing the Group statements as well as group analytical procedures.
- **Other Council interests:** analytical procedures were performed for the other Council interests consolidated in the Group financial statements and assessed as non-significant components, namely:
  - Sunderland Care and Support Limited;
  - Sunderland Homes Limited;
  - Siglion Limited; and
  - International Advanced Manufacturing Park LLP (joint venture).



# APPENDIX B

## DRAFT AUDITOR’S REPORT (CONTINUED)

We also tested the consolidation process and carried out analytical procedures to confirm our conclusion that there were no significant risks of material misstatement arising from the aggregated financial information.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are discussed under ‘Key Audit Matters’ within this report.

### Other information

The Executive Director of Corporate Resources is responsible for the other information. The other information comprises the information included in the Statement of Accounts, other than the financial statements and our auditor’s report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

### Responsibilities of the Executive Director of Corporate Resources for the financial statements

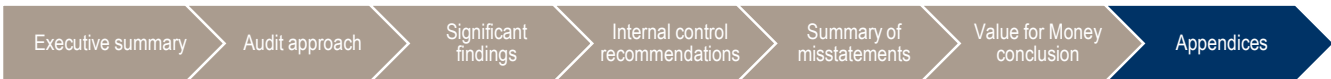
As explained more fully in the Executive Director of Corporate Services’ Responsibilities, the Executive Director of Corporate Resources is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19, and for being satisfied that they give a true and fair view. The Executive Director of Corporate Resources is also responsible for such internal control as the Executive Director of Corporate Resources determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Executive Director of Corporate Resources is required to comply with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and prepare the financial statements on a going concern basis, unless the Council is informed of the intention for dissolution without transfer of services or function to another entity. The Executive Director of Corporate Resources is responsible for assessing each year whether or not it is appropriate for the Council to prepare its accounts on the going concern basis and disclosing, as applicable, matters related to going concern.

### Auditor’s responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council’s website at [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditor’s report.



# APPENDIX B

## DRAFT AUDITOR'S REPORT (CONTINUED)

### Matters on which we are required to report by exception under the Code of Audit Practice

- We are required by the Code of Audit Practice to report to you if:
- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014;
  - we make a recommendation under section 24 of the Local Audit and Accountability Act 2014; or
  - we exercise any other special powers of the auditor under sections 28, 29 or 31 of the Local Audit and Accountability Act 2014.

We have nothing to report in these respects.

### Conclusion on Sunderland City Council's arrangements for securing economy, efficiency and effectiveness in the use of resources

#### Qualified conclusion – except for

On the basis of our work, having regard to the guidance on the specified criterion issued by the Comptroller and Auditor General in November 2017, with the exception of the matter reported in the basis for qualified conclusion below, we are satisfied that, in all significant respects, Sunderland City Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

#### Basis for qualified conclusion

In seeking to satisfy ourselves the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources, we have considered reports issued by other regulators. In July 2018, Ofsted reported its second inspection of services for children in need of help and protection, looked after children, care leavers and adoption performance. Ofsted concluded that the categories of 'children who need help and protection' and 'leadership, management and governance' remained inadequate. Therefore our conclusion is qualified in respect of those categories assessed as inadequate by Ofsted.

We have undertaken our review in accordance with the Code of Audit Practice issued by the Comptroller and Auditor General, having regard to the guidance on the specified criterion issued in November 2017, as to whether the Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The Comptroller and Auditor General determined this criterion as that necessary for us to consider in satisfying ourselves whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

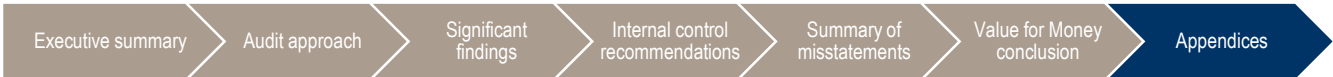
We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, the Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

#### Responsibilities of the Council

The Council is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

### Auditor's responsibilities for the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We are required under section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice requires us to report to you our conclusion relating to proper arrangements. We are not required to consider, nor have we considered, whether all aspects of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.



# APPENDIX B

## DRAFT AUDITOR’S REPORT (CONTINUED)

**Other matters which we are required to address**

We were appointed as the Council’s auditor by Public Sector Audit Appointments Ltd, in its role as appointing person under the Local Audit (Appointing Person) Regulations 2015, on 14 December 2017. The period of total uninterrupted engagement, including previous renewals and reappointments of the firm, is 7 years covering the audit of the financial year ending 31 March 2019.

The non-audit services prohibited by the FRC’s Ethical Standard were not provided to the Council or its Group and we remain independent of the Council and its Group in conducting our audit.

In addition to the audit, we provided the following services to the Council and Group during the period 1 April 2018 to 31 March 2019, that have not been disclosed separately in the Statement of Accounts:

- Sunderland Care and Support Limited: provision of external audit services for 2018/19.

Our audit opinion is consistent with the Audit Completion Report presented to the Audit and Governance Committee.

**Use of the audit report**

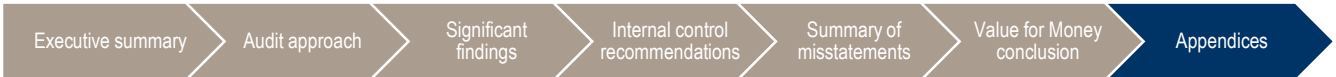
This report is made solely to the members of Sunderland City Council, as a body, in accordance with part 5 of the Local Audit and Accountability Act 2014 and as set out in paragraph 44 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the members of the Council those matters we are required to state to them in an auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the members of the Council, as a body, for our audit work, for this report, or for the opinions we have formed.

**Delay in certification of completion of the audit**

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 Whole of Government Accounts consolidation pack. We are satisfied that these matters do not have a material effect on the financial statements or on our conclusion on the Council’s arrangements for securing economy, efficiency and effectiveness in its use of resources.

Cameron Waddell  
For and on behalf of Mazars LLP  
Salvus House  
Aykley Heads  
Durham  
DH1 5TS

Date:



# APPENDIX C

## INDEPENDENCE

As part of our ongoing risk assessment we monitor our relationships with you to identify any new actual or perceived threats to our independence within the regulatory or professional requirements governing us as your auditors.

We can confirm that no new threats to independence have been identified since issuing the Audit Strategy Memorandum and therefore we remain independent.

We also confirm we have received confirmation from auditor’s external experts regarding their independence.

