The Annual Audit Letter for Sandwell MBC

Year ended 31 March 2020

March 2022

Contents

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Executive Summary

Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Sandwell Metropolitan Borough Council (the Council) and its subsidiaries (the group) for the year ended 31 March 2020.

This Letter is intended to provide a commentary on the results of our work to the group and external stakeholders, and to highlight issues that we wish to draw to the attention of the public. In preparing this Letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to the Council's Audit and Risk Assurance Committee as those charged with governance in our Audit Findings Report on 21 December 2021

Respective responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council and group's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council and group's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

Our work

Materiality	We determined materiality for the audit of the group’s financial statements to be £12m, which is 1.4% of the group's gross cost of services.
Financial Statements opinion	We gave an unqualified opinion on the group's financial statements on 4 January 2021. We identified significant issues with the financial statements. As a result our audit continued over an 18 month period. We have needed to deal with a number of financial reporting issues that have significantly delayed the audit and resulted in additional costs to the Council. A summary of our findings are set out overleaf. Action is needed by the Council to strengthen its financial reporting. We included an emphasis of matter paragraph in our report in respect of the uncertainty over valuations of the Council's land and buildings and investment properties given the Coronavirus pandemic. This does not affect our opinion that the statements give a true and fair view of the Council's financial position and its income and expenditure for the year.
Whole of Government Accounts (WGA)	Due to the late finalisation of the audit we were not required to make a submission to the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise our additional statutory powers in respect of the 2019-20 Audit year.

Executive Summary

Commentary on the Audit

On 4 January 2021 we issued an unqualified opinion on the accounts, the opinion included an emphasis of matter in relation to valuation uncertainty, due to the effects of Covid-19 and the Grenfell Tower fire on the valuation of land and buildings and property investments. This particular emphasis of matter was common for 2019/20 and reflects the view of the external valuers in a relatively uncertain property market as a consequence of the pandemic.

The external audit of the 2019/20 accounts was protracted. The audit commenced in September 2020 and draft audit findings reports (AFR) were presented to committee in March 2021, September 2021 with a final AFR in December 2021. The opinion was issued in early January 2022.

Remote working by both the council and audit teams as a consequence of COVID has contributed to delays, which is something that has been experienced in our audits up and down the country. However the protracted audit at Sandwell reflects underlying issues in the council's arrangements for producing the accounts and dealing with the audit process. In addition there were a number of specific issues that required management to consult more widely in order to resolve and reworking of a number of areas of the accounts. This process took some time and consequently we 'paused' the audit on a number of occasions to allow management to resolve matters, before restarting our work.

Some of the challenge and difficulties we experienced related to matters raised in the prior year where there has been insufficient time for management to address the matters, such as the underlying records and basis for the valuation of property plant and equipment.

More generally, management needs to produce a set of accounts which is supported by complete and reliable working papers, with entries that are understood and 'owned' by the finance team with clearly articulated assumptions and rationales, having appropriate regard and reference to accounting standards and the CIPFA code.

The accounts and supporting working papers should have a thorough and timely quality review and management signoff. Currently too much reliance is placed on the audit process for challenge and checks of the entries in the accounts. Management needs to improve both the quality of working papers as they were not adequate in a number of areas and also responses to audit queries and challenges, as all too often superficial responses were made resulting in follow up queries, adding to further delays.

In 2021 the Council has appointed a new S151 Officer and she has recognised that the finance team needs to be strengthened This was also highlighted by CIPFA in their report in January 2022.

As a consequence of the audit there were a number of adjustments to the accounts. CIES – the impact of the adjustments to the CIES has resulted in net decrease in deficit of £10.5m.

Key adjustments and issues are as follows:

- Property plant and equipment (PPE) has increased in value by £45m due to the changes in valuation of a number assets. As referenced later in the report, we have significant concerns around many aspects of the council's records and approach to valuation of property plant and equipment. Management has assured us that progress is being made to address our concerns including acquisition of appropriate software to improve record keeping. It will not be possible for management to address these matters for the 2020/21 audit as this has already commenced.
- Provisions – the accounts reflect a gross increase in short term provisions of £6.4m which relates specifically to unlodged business rates appeals for which there was no provision in the draft accounts. Management had originally determined that there was insufficient information on which to make a reasonable estimate. Following our challenge Analyse Local were able to provide some data that enabled management to make a reasonable estimate.

Executive Summary

- Impairment allowances: the debtors balance on the balance sheet is net of impairments allowances. These are for receivables, council tax, NNDR, Housing benefits and HRA. The basis of these allowances were not clearly understood by management and factors such as the impact of COVID on collectability had not been fully considered. For some 100% impairment allowance had been applied without a clearly articulated justification. Following audit challenge these balances were reassessed and a net adjustment of £4.7m made to these allowances. Overall we consider that the Council's arrangements for managing provisions and impairment allowances is poor. We also noted that a proportion of the debt and associated provision relating to housing benefit claims was omitted from the accounts in its entirety. Again we consider this to be poor practice.
- Cash/ Creditors - we identified a material error of £35m between cash and creditors on the balance sheet which arose due to an incorrect journal posting. There was no loss to the council from this adjustment. It is unusual in our experience to identify errors in cash or creditors of this magnitude. While this is a classification issue we would have expected the Council's quality control procedures to have identified this error either as part of the journal approval process or bank reconciliation sign off. This provides us with further concerns over controls surrounding management oversight and review.
- Group accounts – on consolidation of the SLP accounts the council needed to revalue the school land on the same basis as the council's assets. Following audit challenge and review by the internal valuer in consultation with the council's external valuer two significant changes in assumptions were made. The first in relation to the elements of the land that was valued as developed land (which has a significant impact on costs per square meter) and the treatment of academy land. These resulted in prior period adjustments to the accounts.
- Cashflow - there are material adjustments to the cashflow forecast due to the adjustments referenced above.
- Revenue grants credited to services increased by £13.4m (and charged to taxation reduced by the equivalent amount on the face of the CIES). This adjustment was because the council had not properly considered guidance on where the amounts should be reflected in the accounts. Further enhancements were made to the supporting note where there had been omissions in grants disclosed. This also resulted in a prior period adjustment.
- Opening/ Closing capital financing requirement (CFR) reduced by £56m (note 37). This adjustment arose because management was unable to fully justify the basis of the CFR, where the methodology had rolled forward and audit requested that the amount be recalculated from first principles using CIPFA guidance.   We were satisfied that the restated amounts were correctly calculated. This also resulted in the prior period balances being restated.
- Prior period adjustments (PPA): as a consequence of the PPAS a third balance sheet is reflected in the restated accounts in line with accounting requirements.

In addition to these matters there were numerous adjustments made to disclosures to provide improved description of assumptions and explanations and corrections for typographical errors.

Overall, we consider that significant improvements are needed in the Council's financial reporting procedures.

Executive Summary

Value for Money arrangements	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources except for the arrangements around children's services. We qualified our value for money conclusion in our audit report to the Council on 4 January 2022 due to this matter. We noted in the Audit Findings Report that a number of governance issues have come to our attention during 2021. We consider that there is insufficient evidence to confirm that these matters impacted on 2019/20 and as such they are being dealt with as part of the 2020/21 audit.
Certificate	We certified that we have completed the audit of the financial statements of Sandwell MBC in accordance with the requirements of the Code of Audit Practice on 25 January 2022.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council's staff .

Grant Thornton UK LLP
March 2022

Audit of the Financial Statements

Our audit approach

Materiality

In our audit of the Council's financial statements, we use the concept of materiality to determine the nature, timing and extent of our work, and in evaluating the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for the audit of the council and group's financial statements to be £12m, which is 1.4% of the group's gross cost of services. We used this benchmark as, in our view, users of the financial statements are most interested in where the Council has spent its revenue in the year.

We also set a lower level of specific materiality for senior officer remuneration of £0.1m.

We set a lower threshold of £600,000, above which we reported errors to the Audit and Risk Assurance Committee in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining sufficient evidence about the amounts and disclosures in the financial statements to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error. This includes assessing whether:

- the accounting policies are appropriate, have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the remainder of the Statement of Accounts to check it is consistent with our understanding of the Council and with the financial statements included in the Statement of Accounts on which we gave our opinion.

We carry out our audit in accordance with ISAs (UK) and the NAO Code of Audit Practice. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of the Council and group's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the Financial Statements

Significant Audit Risks

These are the significant risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of land and buildings The group revalue its land and buildings on a rolling five-yearly basis. Some assets are likely to be valued annually, such as some school buildings. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£2 billion) and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Authority and group financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used. We therefore identified valuation of land and buildings, particularly revaluations, as a significant risk, which was one of the most significant assessed risks of material misstatement.	We have: • Evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work • Evaluated the competence, capabilities and objectivity of the Council's valuation expert • Written to the valuer to confirm the basis on which the valuation was carried out to ensure that the requirements of the Code are met • Challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding • Engaged our own valuer to assess the instructions to the Authority's valuer, the Authority's valuer's report and the assumptions that underpin the valuation • Tested revaluations made during the year to see if they had been input correctly into the Authority's asset register • Evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value at year end.	In line with RICS guidance, the external valuers included reference to a material uncertainty in the final valuation report for both land and buildings and council housing and in relation to high rise buildings. The pension fund accounts also make reference to a material uncertainty in relation to property assets. There were a number of adjustments to the valuations during the audit, particularly relating to leisure centres and this resulted in adjustments to both the 2019/20 accounts and prior years. We have discussed with management and made recommendations this year and last for improvements in both the asset management system and the fixed asset registers. Significant amendments were made in the group accounts due to a change in valuation approach to land in the subsidiary company Sandwell Land and Property Ltd. Again this resulted in a prior period adjustment.

Audit of the Financial Statements

Significant Audit Risks - continued

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of net pension liability The Authority's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements and group accounts. The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£759.7 million in the Authority's balance sheet) and the sensitivity of the estimate to changes in key assumptions. We therefore identified valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement.	We have: • updated our understanding of the processes and controls put in place by management to ensure that the Authority's pension fund net liability is not materially misstated and evaluated the design of the associated controls • evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work • assessed the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation • assessed the accuracy and completeness of the information provided by the Authority to the actuary to estimate the liability • tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary • undertaken procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report; and • obtained assurances from the auditor of West Midlands Pension Fund as to the controls surrounding the validity and accuracy of membership data; contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements.	Our audit work has not identified any issues in respect of valuation of the net liability.
Management override of internal controls Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.	We have: • Evaluated the design effectiveness of management controls over journals, • Analysed the journals listing and determined the criteria for selecting high risk unusual journals, • Tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration, • Gained an understanding of the accounting estimates and critical judgements applied by management and considered their reasonableness with regard to corroborative evidence, and • Evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.	Our audit work has not identified any issues in respect of management override of controls.

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Council and group's financial statements on 4 January 2022.

Preparation of the financial statements

The audit was more protracted than expected. There were a large number of amendments made to the accounts which included prior period adjustments. In order to address concerns, management are seeking to strengthen the finance team and improve underlying records, including the systems to support management and recording of the Council’s property plant and equipment. We will follow up our recommendations for improvement as part of the 2020/21 audit.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Council's Audit and Risk Assurance Committee in July 21 and again in December 2021. Our detailed recommendations are made in these Audit Findings Reports but the key matters and recommendations are summarised below.

Property plant and equipment

We reported a number of matters on the approach to valuation and underling record keeping of the Council’s property assets. Our key recommendations included the following:

- Improve property asset management through implementation of more modern IT systems for both storing and updating information on the Council’s property asset holdings. Records should be verified to primary information as part of this exercise to ensure underlying data is complete and accurate.
- Improve the asset registers, (which are used to inform the statement of accounts) by moving from an excel based system, to a more appropriate specialised system that is commensurate with the relative size and value of the council property stock.
- Better document the instructions, correspondence, challenge and checking of output of the external valuer.

Arrears

Our review of impairments of receivables indicated that management had not recently properly reviewed the basis of provisions, having appropriate regard to their collectability, as expected under the code and IFRS9.

- We noted some HB arrears had been excluded from the accounts, and recommended management ensure they be included in the 20/21 accounts.
- Additional work was undertaken by management, at audit request, on the impairment of debt and the accounts were adjusted as a consequence.
- The provision for business rates appeals was also judged to be inadequate and was increased.

We recommended management build on this work in the 20/21 accounts and properly consider the impact of COVID 19 on the collectability of debt.

Bank Reconciliation

A material error was identified on the bank reconciliation which was as a result of a journal error. We recommended that management should:

- simplify the reconciliation as the complexity is likely to have contributed to the error not being identified on management review.
- Consider the adequacy of controls over journals to ensure that journals are appropriately reviewed and approved.
- Review the controls and safeguards around payments to prevent postings being made that are outside set parameters.

Grants

We noted that several of the council’s grants had not been correctly classified within income in the accounts. We recommend that management considered this as part of the preparation of the 20/21 accounts.

Capital financing requirement (CFR)

The council recalculated the CFR and concluded that it was materially misstated.

Audit of the Financial Statements

Annual Governance Statement and Narrative Report

We are also required to review the Council’s Annual Governance Statement and Narrative Report. It published them along with the accounts in January 2022.

Both documents were prepared in line with the CIPFA Code and relevant supporting guidance. We confirmed that both documents were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

Whole of Government Accounts (WGA)

Due to the late completion of the audit, the WGA return was not required to be submitted.

Other statutory powers

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts. No powers have been exercised in relation to the 2019/20 financial year.

Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of [name of Council] in accordance with the requirements of the Code of Audit Practice on 25 January 2022.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in April 2020 which specified the criterion for auditors to evaluate:
In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the risks where we concentrated our work.

The risks we identified and the work we performed are set out overleaf.

As part of our Audit Findings report we agreed recommendations to address our findings.

Overall Value for Money conclusion

We are satisfied that, in all significant respects, except for the matter we identified overleaf, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2020.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Sustainable resource deployment: budget planning The sector faces continuing financial pressures due to the reductions in central government grants. The Council medium term financial plan (MTFP) highlights considerable uncertainties in funding beyond 2020/21 due to the new formula for funding settlement. Significant cuts in funding for older people are anticipated. The MTFP is currently assuming that the Council will have a broadly balanced position over the life of the plan. The latest budget report for 2019/20 is anticipating an overspend of £0.058m. £10.681 of earmarked reserves are anticipated to be utilised during the year, resulting in an overall overspend of £10.739m. Any overspend by the Children's Trust may provide a further budget pressure. Due to the continuing pressures and uncertainties in the sector we consider that this is a significant risk. We will consider your arrangements for managing and reporting your financial resources and the Council's arrangements for achieving savings.	As part of our work we have considered: • Budget reporting • Medium term financial plan • Children's and Adult social care budgets reserves • Capital • Impact of COVID-19	Our detailed findings are contained in the AFR. We have seen that the Council, even before COVID-19 is facing increasing cost pressures and is likely to require further focus on delivering savings, particularly in Adult social care and children's services. As with most councils COVID- 19 has impacted significantly operationally and financially. However management are currently forecasting that the impact is manageable, particularly as the central government grant is offsetting much of the additional cost and income pressures in 2020/21. The Council currently has good levels of balances relative to many other councils. **Overall we are satisfied that the VFM risk identified in our 2019/20 plan has been mitigated.**

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Informed decision making: children's services The Council's Children's services were assessed as 'inadequate' in January 2018 and Children's Trust was subsequently established. The most recent monitoring report in December 2019 highlighted that improvements had been made but the pace of change needed to accelerate. As the service continues to be assessed as 'inadequate' this presents a significant value for money risk. .	As part of our work we have considered progress since our previous audit findings report in 2018/19.	The Ofsted inspection report of children's services, published in January 2018, concluded that Children's services in Sandwell were inadequate. There have been six monitoring visits since the last inspection. Ofsted have recognised that improvements in the service are being made but have noted that further progress is needed if the issues raised in their last inspection report are to be fully addressed. Having considered the findings and conclusions of Ofsted's inspections and monitoring visits, together with the results of our audit work, we have concluded that there are weaknesses in the Authority's arrangements for delivering services for children in need of help and protection, children looked after and care leavers. These matters are evidence of weaknesses in proper arrangements for understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management. **We are unable to conclude that the risk has been mitigated in relation to children's services**
Informed decision making : providence place In June 2019, the Department for Education approved the provision of a new, 750 place secondary free school in West Bromwich, to be delivered in partnership with Shireland Academy and the City of Birmingham Symphony Orchestra (CBSO). It is proposed that the Council sell the freehold interest of 1 Providence Place, West Bromwich, with vacant possession, along with a development plot to the DfE for £8.46m	We obtained the history of the Providence Place asset from the initial acquisition of the asset up to the decision to dispose. The council will incur a significant loss on disposal of the asset.	As Provident Place is being sold at its current market value and the decision to purchase it was made in 2014 **we do not consider that the sale impacts on our 2019/20 VfM conclusion.** However, due to the significance of the loss we have raised this matter with the Chief Executive to ensure that future purchases or sales of land and property are clearly aligned with a long term estate strategy. We have also made reference to this matter in our Governance review as part of the 20/21 audit.

A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit and provision of non-audit services.

Reports issued

Report	Date issued
Audit Plan	March 2021
Audit Findings Report	December 2021
Annual Audit Letter	January 2022

Fees

	Planned £	Actual fees £
Statutory audit	153,136	253,300
Total fees	**153,136**	**253,300**

Audit fee variation

As outlined in our audit plan, the 2019-20 scale fee published by PSAA of £153,000 assumes that the scope of the audit does not significantly change. There are a number of areas where the scope of the audit has changed, which has led to additional work. These are set out in the following table.

Fee variations are subject to PSAA approval.

Area	Reason	Fee proposed
Variation agreed February 2021	Issues as set out in the audit plan	32,350
Additional uplift	Issues as reflected in the September AFR	57,814
Further overrun	Issues as reflected in the AFR addendum	10,000
Total		100,164

A. Reports issued and fees continued

Fees for non-audit services

Service	Fees £
Audit of subsidiary	
Sandwell Children's Trust	27,250
Sandwell Land and Property Ltd	25,000
Audit related services	
- Housing Subsidy	28,000
- Teachers pension	6,000
Non-Audit related services	
- CFO highlights	12,500
- Agreed upon procedures Sandwell Children's Trust (annual certification of the expenditure in respect of the Trust's Improvement Grant for DfE)*	5,000

Non- audit services

- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to group. The table above summarises all non-audit services which were identified.
- We have considered whether non-audit services might be perceived as a threat to our independence as the group's auditor and have ensured that appropriate safeguards are put in place.

The above non-audit services are consistent with group's policy on the allotment of non-audit work to your auditor.