



Shetland Islands Council

Report to the Audit Committee, Members of the Council and the Controller of Audit
on the 2020/21 audit

Issued on 24 September 2021 for the meeting on 29 September 2021

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Introduction

The key messages in this report

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the Annual Accounts.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

I have pleasure in presenting our final report to the Audit Committee (“the Committee”) of Shetland Islands Council (“the Council”) for the year ending 31 March 2021 audit. The scope of our audit was set out within our planning report presented to the Committee in March 2021.

This report summarises our findings and conclusions in relation to:

- The audit of the **Annual Accounts**; and
- Consideration of the **four audit dimensions** that frame the wider scope of public sector audit requirements as illustrated in the following diagram. This includes our consideration of the Council’s duty to secure best value.



Introduction (continued)

The key messages in this report (continued)

I would like to draw your attention to the key messages of this paper:

Conclusions from our testing

Based on our audit work completed to date we expect to issue an unmodified audit opinion.

The Management Commentary and Annual Governance Statement comply with the statutory guidance and proper practice and are consistent with the Annual Accounts and our knowledge of the Council.

The auditable parts of the Remuneration Report have been prepared in accordance with the relevant regulations.

A summary of our work on the significant risks is provided in the dashboard on page 10.

We have identified three misstatements and one disclosure deficiency above our reporting threshold, which have both been corrected by management. Two of the misstatements relate to events after the reporting period, rather than errors. These are detailed on pages 29 to 31.

Status of the Annual Accounts audit

Our audit is complete.

Conclusions on audit dimensions and best value

As set out on page 3, our audit work covered the four audit dimensions. Our separate detailed report presented to the Committee in June 2021 set out our findings and conclusions on each dimension. In accordance with the Code of Audit Practice, we have included our overall conclusions within this report on pages 25 and 26. Key highlights include:

Financial Management – In 2020/21 the Council drew £1.837m from its reserves (down from £21.72m drawn in 2019/20) continuing to place reliance on a draw on reserves to achieve a balanced budget.

The Council has strong financial management in place and the finance function continues to operate effectively to support the Council's financial management arrangements.

Financial sustainability - The Council achieved short-term financial balance in 2020/21 and has set a balanced budget for 2021/22. The current level of reserves held are at an acceptable level and are in line with policy.

The Council have revised their Medium Term Financial Plan ('MTFP') which is underpinned by realistic assumptions and financial projections. In addition, savings and efficiencies have been included as part of the 2021/22 budget.

Introduction (continued)

The key messages in this report (continued)

Conclusions on audit dimensions and best value (continued)

Governance and transparency - The Chief Executive has shown strong leadership during the pandemic, effectively communicating with staff on all levels.

The political leadership of the Council remains effective, however there are weaknesses in the Council's structure, evidenced by the ongoing difficulties with fully resourcing the Council's committees, referrals to the Commissioner for Ethical Standards in Public Life in Scotland, and the provision of confidential information from Council meetings to the local media in apparent contravention of the Member's Code of Conduct.

Value for money - The Council has a clear and robust Performance Management Framework in place which has been prepared in accordance with the Best Value Toolkit for performance management.

The performance of the Council is showing evidence of improvements in a number of areas in the Local Government Benchmarking Framework.

The Council has shown a commitment to reducing inequalities in Shetland through partnership working, which has been evidenced through outcomes achieved and individual projects undertaken.

Business cases are not implemented as initially agreed, resulting in additional costs and delays in the achievement of savings, undermining the effective of scrutiny within the Council.

Best value - As reported in our June 2021 report, the Council has a number of arrangements in place to secure Best Value. While the Council continues to demonstrate improvements in a number of areas and is committed to improvement, further improvements are needed in key areas and the Council needs to ensure the pace of change is appropriate.

Next steps

An agreed Action Plan was included in the separate wider scope report that was presented to the Committee in June 2021. Additional actions arising from the Annual Accounts audit are included in an agreed Action Plan included on page 32 of this report, including a follow-up of progress against prior year actions. We will consider progress with all agreed actions as part of our 2021/22 audit.

Introduction (continued)

The key messages in this report (continued)

Added value

Our aim is to add value to the Council by providing insight into, and offering foresight on, financial sustainability, risk and performance by identifying areas for improvement and recommending and encouraging good practice. In so doing, we aim to help the Council promote improved standards of governance, better management and decision making, and more effective use of resources.

In addition, we included our “sector developments” in the separate wider scope report that was presented to the Committee in June 2021 which covers our research, informed perspective and best practice from our work across the wider public sector that are specifically relevant to the Council.

As information emerges as a result of COVID-19, the withdrawal from the European Union, and evolving legislation we have shared guidance with management in relation to Annual reporting. We have also shared invites to relevant Deloitte-led webinars with the Council.

Pat Kenny
Audit Director








Annual Accounts audit



Quality indicators

Impact on the execution of our audit

Management and those charged with governance are in a position to influence the effectiveness of our audit, through timely formulation of judgements, provision of accurate information, and responsiveness to issues identified in the course of the audit. This slide summarises some key metrics related to your control environment which can significantly impact the execution of the audit. We consider these metrics important in assessing the reliability of your financial reporting and provide context for other messages in this report.

Area	Grading	Reason
Timing of key accounting judgements		Support for key accounting judgements, such as fishing quota, property plant and equipment ("PPE") valuations, defined benefit pensions support and investments were provided on time and were of a high quality.
Adherence to deliverables timetable		Management provided all evidence in a timely manner, in advance of agreed timelines and where there were anticipated delays in receiving information, we were informed early and worked with management to accommodate this. Any follow-up requests during the audit were quickly actioned.
Access to finance team and other key personnel		Deloitte and the Council have worked together to facilitate remote communication during the audit which has been successful. There have been no issues with access to the finance team or other key personnel.
Quality and accuracy of management accounting papers		Documentation provided has been of a high standard, which enabled an efficient audit. Working papers were clear and reconcilable to the Annual Accounts. This is borne out by the resubmission rate on requests for the audit being low.
Quality of draft Annual Accounts		A full draft of the Annual Accounts was received for audit on 6 July 2021. We identified 19 minor changes which were required, which is an improvement from the prior year.
Response to control deficiencies identified		We did not identify any control deficiencies during our audit.
Volume and magnitude of identified errors		We have identified four misstatements above our reporting threshold as part of our audit; three being financial misstatements and one being a disclosure misstatement, each of which have been corrected by management. These are detailed on pages 29 to 31. The adjustment for personal protective equipment and testing kits arose as a result of late guidance from the Scottish Government, while the adjustment in relation to cash and cash equivalents arose as a result of late information provided by the fund manager. These are therefore not indicative of the quality of the draft Annual Accounts.

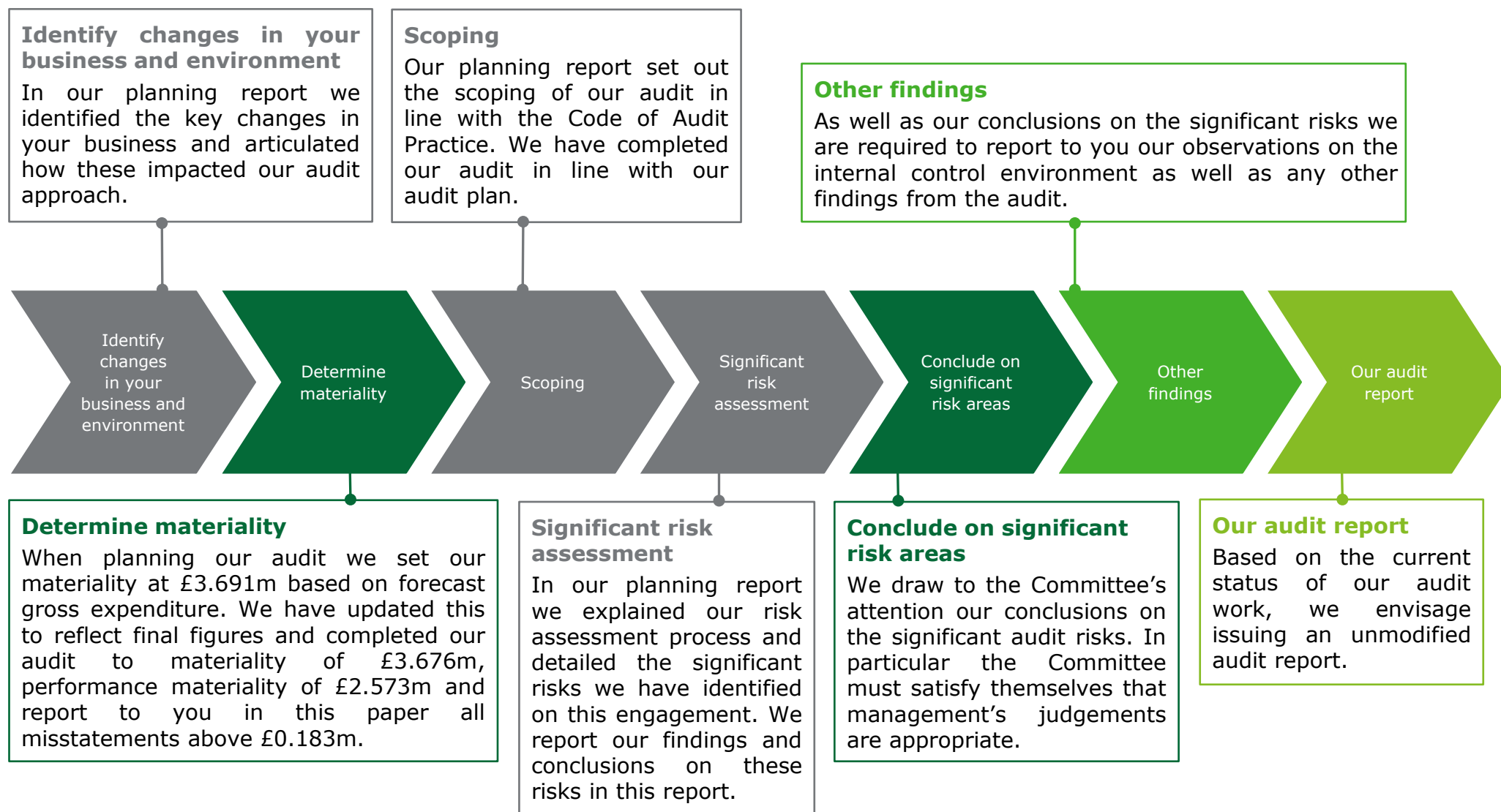
 Lagging

 Developing

 Mature







Our audit explained

We tailor our audit to your business and your strategy



Significant risks

Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Controls testing conclusion	Consistency of judgements with Deloitte's expectations	Comments	Page no.
Recognition of COVID-19 related income			D+I	Satisfactory		Satisfactory	11
Management override of controls			D+I	Satisfactory		Satisfactory	12

Overly prudent, likely to lead to future credit



Overly optimistic, likely to lead to future debit.

D+I: Testing of the design and implementation of key controls

Significant risks (continued)

Recognition of COVID-19 related income



Risk identified and key judgements

ISA 240 states that when identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.

We have assessed the income streams of the Council, the complexity of the recognition principles and the extent of any estimates used, and concluded that, with the exception of the funding received in 2020/21 in response to the COVID-19 pandemic, there is no significant risk of fraud.

During 2020/21, the Council has received additional funding in relation to COVID-19 mobilisation costs. In addition, there are a number of business support schemes designed to help eligible businesses during the COVID-19 pandemic that are being administered by Councils on behalf of the Scottish Government.

We have pinpointed the significant risk to the completeness and occurrence of the funding for COVID-19 mobilisation costs and the completeness and accuracy of the agency arrangement disclosures.

The key judgements for management are assessing:

- Any conditions associated with the mobilisation cost funding; and
- Whether the Council is acting as a principal or agent in administering the business support schemes.



Deloitte response and challenge

We have performed the following:

- Assessed the design and implementation of the controls in relation to the accounting treatment of all COVID-19 related funding;
- Tested a sample of funding for COVID-19 mobilisation costs and confirm these have been recognised in accordance with any conditions applicable; and
- Tested the agency arrangement disclosures to confirm, where it is concluded that the Council is acting as an agent, that:
 - Transactions have been excluded from the Comprehensive Income and Expenditure Statement;
 - The Balance Sheet reflects the debtor or creditor position at 31 March 2021 in respect of cash collected or expenditure incurred on behalf of the principal; and
 - The net cash position at 31 March 2021 is included in the financing activities in the Cash Flow Statement.

Deloitte view

We have concluded that income has been correctly recognised in accordance with the requirements of the Code of Practice on Local Authority Accounting and the "Guidance on Accounting for Coronavirus (COVID-19) Grants/ Funding Streams" issued by LASSAC. Given the significance and change in the year, the funding has also been appropriately explained within the Management Commentary and the notes to the accounts.

Significant risks (continued)

Management override of controls



Risk identified

Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent Annual Accounts by overriding controls that otherwise appear to be operating effectively.

Although management is responsible for safeguarding the assets of the entity, we planned our audit so that we had a reasonable expectation of detecting material misstatements to the Annual Accounts and accounting records.



Deloitte response and challenge

In considering the risk of management override, we have performed the following audit procedures that directly address this risk:

Journals

We have tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the Annual Accounts. In designing and performing audit procedures for such tests, we have:

- Tested the design and implementation of controls over journal entry processing;
- Made inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments;
- Selected journal entries and other adjustments made at the end of a reporting period; and
- Considered the need to test journal entries and other adjustments throughout the period.

Accounting estimates and judgements

We have reviewed accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. In performing this review, we have:

- Evaluated whether the judgments and decisions made by management in making the accounting estimates included in the Annual Accounts, even if they are individually reasonable, indicate a possible bias on the part of the entity's management that may represent a risk of material misstatement due to fraud. From our testing we did not identify any indications of bias. A summary of the key estimates considered is provided on the following page; and
- Performed a retrospective review of management judgements and assumptions related to significant accounting estimates reflected in the Annual Accounts of the prior year.

Significant and unusual transactions

We did not identify any significant transactions outside the normal course of business or any transactions where the business rationale was not clear.

Deloitte view

We have not identified any significant bias in the key judgements made by management.

We have not identified any instances of management override of controls in relation to the specific transactions tested.

Significant risks (continued)

Management override of controls (continued)

Key judgements The key judgement in the Annual Accounts is that which we have selected to be the significant audit risk around the recognition of COVID-19 related income (page 11). While not considered to be significant audit risks, we have also considered the assumptions used to calculate the pension liability (page 16) and the recognition of expenditure (page 17). In the table below, we set out our challenge of the assumptions used in the determination of property valuations, PFI projects, provisions, investments and fishing quota.

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Property valuations	<p>The Council is required to hold property assets within Property, Plant and Equipment at a modern equivalent use valuation. The valuations are, by nature, significant estimates based on specialist and management assumptions and which can be subject to material changes in value.</p> <p>The Council has had an independent valuation carried out at 31 March 2021 by its internal valuers to include valuation of the Council's land and property in accordance with the schedule detailed within its 5-year rolling programme.</p> <p>The valuation method has not changed from the prior year and is in line with International Financial Reporting Standards. The Council's revaluation has resulted in a downward revaluation of £2.021m.</p>	<p>We did not identify this as a significant risk in our Audit Plan as our property specialists, Deloitte Real Estate, reviewed the methodology applied by the Council's valuer in previous years and concluded it was robust. We have confirmed that the valuer and the methodology applied has not changed in the year.</p> <p>We have challenged management's assessment and consulted with our internal property experts. For those valued on Existing Use Value on a market comparable basis, our property experts have confirmed that minimal market value would be expected in 2020/21. For those valued on a Depreciated Replacement Cost basis, which would be impacted by changes in build costs during the year, we have performed an analysis of changes in the Build Costs Information Service index and concluded that no material movement would be expected. We are therefore satisfied that there is no indication of a material movement in assets not formally revalued during the year.</p> <p>We have reviewed the valuers report, specifically in relation to the impact of COVID-19. The valuer has confirmed that the valuation is not reported as being subject to 'material valuation uncertainty'. This is in line with our expectation and in line with the RICS guidance at 31 March 2021.</p>

Significant risks (continued)

Management override of controls (continued)

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Private Finance initiatives ('PFI')	<p>The Council currently has one PFI project: the Anderson High School contract. The PFI liability is valued based on the value of the remaining lease payments under the relevant accounting standards. The minimum lease rental is split between interest and principal using the actuarial method.</p> <p>In 2020/21, the Council made payments of £3.851m on PFI projects.</p>	<p>We obtained and assessed the initial PFI agreements in place and reconciled to the payment schedules for each model. We have conducted a retrospective review of the prior year liability to assess accuracy, and have challenged any changes made to the model. We have assessed the value of the underlying buildings through our Valuations work.</p> <p>We are satisfied that the PFI liability recognised in the Annual Accounts is in line with the models and there is no indication of management bias.</p>
Fishing Quota	<p>The Council holds a substantial amount of fishing quota, leased to third parties for use in the year. The value of fishing quota at the year end was £32.9m, which is an upward revaluation of £2.7m from the prior year.</p> <p>The valuation of fishing quota is performed by an independent expert. The price that quota attract is affected by the quantity of Fixed Quota Allocation Units (FQAs) in the market.</p>	<p>All valuations are informed by an external expert. Deloitte are satisfied that the independent valuer is suitably competent and has the capabilities to carry out a valuation of the fishing quotas held by the Council.</p> <p>We have assessed the objectivity and competence of management's expert and developed an independent estimate of the value based on information obtained from the active market in the year. We have also assessed the Council's valuation against fishing quota held by similar local authorities and assessed the movement against the movement in the market in the year.</p> <p>We have concluded that fishing quota are held at a reasonable value.</p>

Significant risks (continued)

Management override of controls (continued)

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Investments	<p>The Council holds investments at fair value, with valuations provided to the Council by independent fund managers. The value of investments at the year end was £429.627m, a significant increase of £98.280m from the prior year.</p> <p>When the fair value of financial assets and liabilities cannot be measured based on quoted prices in active markets (i.e. Level 1 inputs), their fair value is measured using valuation techniques. Where possible, the inputs to these valuation techniques are based on observable data, but where this is not possible judgement is required in establishing fair values. These judgements typically include considerations such as uncertainty and risk.</p>	<p>Investments are managed by external fund managers, with the valuation of investments provided by them independently.</p> <p>While the balance sheet value is material, the Council only records what they are advised by the independent fund managers in terms of valuations and gain/losses on disposals. The Council have little scope to manipulate the balances as the fund managers provide monthly reports with a comprehensive breakdown of additions, disposals and revaluations.</p> <p>We have consulted with financial instrument experts to review the assumptions and valuations performed by the fund managers, as well as agreeing the valuation of investments to third party evidence or developing a point estimate based on adjusted net asset values.</p> <p>We have not identified any issues through our work.</p>

Significant risks (continued)

Management override of controls (continued)

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Provisions	<p>The total provisions held within the Council's balance sheet is £3.414m. The balance is primarily comprised of the pension cessation costs as a result of the Shetland College, Train Shetland and North Atlantic Fisheries College ('NAFC') merger, accounting for £2.447m (decreased from £5.080m in 2019/20). The calculation of this amount has been determined by the Council's independent actuary.</p>	<p>We examined the rationale for the provision discussed across and consulted with the Council's legal experts to confirm completeness of the provision.</p> <p>For the pension cessation costs, we confirmed that the calculation was provided by the same actuaries we assessed for the pension liability. We have confirmed that the amount recorded by the Council is in line with the amount provided by the actuary. Post year-end, the Council reached agreement with the Trust that ran the NAFC and Shetland College to manage the significant cessation costs associated with the ending of NAFC's membership in the Local Government Pension Scheme. As a result the provision will be reversed in the 2021/22 financial year.</p> <p>We have engaged with our internal experts and have concluded that the provisions made were reasonable.</p>

Other areas of audit focus

Defined benefits pension scheme



Background

The Council participates in two defined benefits schemes:

- Scottish Teachers' Superannuation Scheme, administered by the Scottish Government; and
- The Shetland Islands Council Pension Fund, administered by the Council.

The net pension liability has increased from £171.912m in 2019/20 to £243.841m in 2020/21. The increase is a combination of an increase of £105.153m in the fair value of the assets and an increase of £177.082m in the liabilities as a result of demographic changes and financial assumptions.

The Council's pension liability continues to be affected by the following legal cases:

- **McCloud** – this case is in respect of possible discrimination in the implementation of transitional protections following the introduction of the reformed public services pension schemes from 1 April 2014 and 2015. The actuary has advised that an estimated allowance for McCloud has been included within the current service cost, consistent with the prior year. There is still uncertainty about the form of compensation that will be provided to members and therefore the final actual cost of complying with the ruling may be different to the estimate.
- **Goodwin** – this is a legal challenge made against the Government in respect of unequitable benefits for male dependants of female members (based on service after 1988) following the earlier Walker ruling. The 31 March 2020 triennial funding valuation did not allow for the impact of Goodwin, therefore the Council's actuary has used the same percentage allowance that was used last year (0.1% of the liability).

Deloitte response

- We assessed the independence and expertise of the actuary supporting the basis of reliance upon their work;
- We reviewed and challenged the assumptions made by Hymans Robertson, including benchmarking as shown the table below;
- We have requested assurance from the auditor of the pension fund over the controls for providing accurate data to the actuary;
- We assessed the reasonableness of the Council's share of the total assets of the scheme with the Pension Fund Annual Accounts;
- We have reviewed and challenged the calculation of the impact of the McCloud and Goodwin cases on pension liabilities and concluded the approach as appropriate and reasonable; and
- We reviewed the disclosures within the accounts against the Code.

	Council	Comments
Discount rate (% p.a.)	2.0	Prudent end of reasonable range
Consumer Price Index (CPI) Inflation rate (% p.a.)	2.85	Reasonable
Salary increase (% p.a.)	2.85	This has been set in line with CPI inflation
Pension increase in payment (% p.a.)	2.85	Reasonable
Pension increase in deferment (% p.a.)	2.85	Reasonable
Mortality - Life expectancy of a male/ female pensioner from age 65 (currently aged 65)	22.3 / 25.3	Prudent end of reasonable range

Deloitte view

Following receipt of the updated Annual Accounts to reflect the required changes to the note 'transactions relating to post employment benefits' (page 31), we are satisfied that the net pension liability disclosed within the Annual Accounts is materially correct.

Other areas of audit focus (continued)

Expenditure recognition

Risk identified

In accordance with Practice Note 10 (*Audit of financial statements of public sector bodies in the United Kingdom*), in addition to the presumed risk of fraud in revenue recognition set out in ISA (UK) 240, as discussed further on page 12, auditors of public sector bodies should also consider the risk of fraud and error on expenditure. This is on the basis that most public bodies are net spending bodies, therefore the risk of material misstatement due to fraud related to expenditure may be greater than the risk of material misstatement due to fraud related to revenue recognition.

We have considered this risk for the Council and concluded that we are satisfied that the control environment is strong and there is no history of errors or audit adjustments. This has therefore not been assessed as a significant risk area, but continued to be an area of audit focus.



Deloitte response

We performed the following procedures to address the above risk:

- A review of the number and median value of invoices processed in the year. As illustrated in table opposite, based on the medium amount, the Council would need to omit over 25,759 invoices at year-end to result in a material error. We noted that in the month following the year-end, a total of 3,293 invoices were processed. We therefore concluded that a risk of material misstatement was remote.
- An analytical review to test the completeness and accuracy of year-end creditor balances was carried out. We are satisfied that the amount recorded is reasonable.

	Invoice Analysis
Median invoice amount	£143.29
Average number of invoices processed per month	4,295
Number of invoices that would need to be unrecorded to cause a material misstatement	25,759
Total invoices processed in April 2021 (one month after year-end)	3,293 (total value £9.098m)

Deloitte view

We have concluded that expenditure has been correctly recognised in accordance with the requirements of the Code of Practice on Local Authority Accounting.

Other areas of audit focus (continued)

Charitable trusts

Risk identified

From 2013/14, all Scottish Councils who act as sole trustees for any registered charities have to fully comply with the Charities Accounts Regulations. This requires Charities SORP-compliant accounts to be prepared for each charity, and a separate audit of each. Shetland Islands Council administers one such registered charity, disclosed in a single set of Annual Accounts.

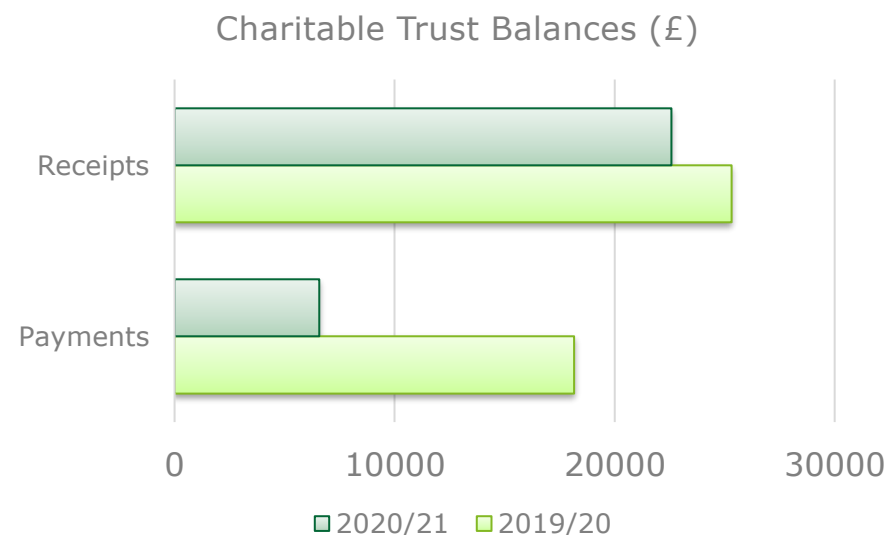
As the gross income of the Trust is less than £100,000, the Council has opted to prepare the charitable trust accounts on a receipts and payments basis in accordance with The Charities Accounts (Scotland) Regulation 2006. Fully compliant Charities SORP accounts are therefore not required and disclosure is limited to that specified in the Regulations.



Deloitte response

We have assessed that the Statement of Receipts and Payments and the Statement of Balances to ensure these have been prepared in accordance with the Charities Accounts (Scotland) Regulations 2006.

A summary is provided in the table adjacent. From an initial review of draft Annual Accounts we note that there has been a large movement in payments which have dropped from £18.148k in 2019/20 to £6.577k in 2020/21. This is largely due to the impact of the COVID-19 pandemic.



Deloitte view

Our testing of the charitable trusts is complete and no issues noted. We anticipate issuing an unmodified opinion.

Other significant findings (continued)

Financial reporting findings

Below, we set out the findings from our audit surrounding your financial reporting process.

Qualitative aspects of your accounting practices:

The Council has prepared its Annual Accounts in line with the Code of Practice on Local Authority Accounting. We are satisfied that the Council's accounting practices are appropriate.

The Council could improve its disclosures on critical judgements and sources of estimation uncertainty to include more information for the users of the Annual Accounts, and to be appropriately tailored to the specific conditions facing the Council.

Significant matters discussed with management:

Significant matters discussed with management related primarily to the impact of COVID-19 on the organisation. In particular, the Local Authority (Scotland) Accounts Advisory Committee ("LASAAC") guidance on accounting for Personal Protective Equipment COVID-19 suggests that the Council is acting as principal regarding the PPE transactions and therefore should recognise any income, expenditure, or stocks of PPE. This was discussed with management and confirmed that this guidance has been followed.

Other matters relevant to financial reporting:

We have not identified other matters arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process.

We will obtain written representations from the Council on matters material to the Annual Accounts when other sufficient appropriate audit evidence cannot reasonably be expected to exist. A copy of the draft representations letter has been circulated separately.

Our audit report

Other matters relating to the form and content of our report

Here we discuss how the results of the audit impact on other significant sections of our audit report.



Our opinion on the Annual Accounts

Based on our audit work completed to date, we expect to issue an unmodified audit opinion.



Material uncertainty related to going concern

We have not identified a material uncertainty related to going concern and will report by exception regarding the appropriateness of the use of the going concern basis of accounting.

Practice Note 10 provides guidance on applying ISA (UK) 570 Going Concern to the audit of public sector bodies. The anticipated continued provision of the service is relevant to the assessment of the continued existence of a particular body.



Emphasis of matter and other matter paragraphs

There are no matters we judge to be of fundamental importance in the Annual Accounts that we consider it necessary to draw attention to in an emphasis of matter paragraph.

There are no matters relevant to users' understanding of the audit that we consider necessary to communicate in an other matter paragraph.



Other reporting responsibilities

The narrative parts of the Annual Accounts is reviewed in its entirety for material consistency with the Annual Accounts and the audit work performance and to ensure that they are fair, balanced and reasonable.

Our opinion on matters prescribed by the Controller of Audit as discussed further on page 22.

Your Annual Report

We are required to provide an opinion on the auditable parts of the Remuneration Report, the Annual Governance Statement and whether the Management Commentary is consistent with the disclosures in the accounts.

	Requirement	Deloitte response
Management Commentary	The Management Commentary comments on financial performance, strategy and performance review and targets. The commentary included both financial and non financial KPIs and made good use of graphs and diagrams. The Council also focuses on the strategic planning context.	<p>We have assessed whether the Management Commentary has been prepared in accordance with the statutory guidance.</p> <p>We have also read the Management Commentary and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>We are satisfied that the Management Commentary has been prepared in accordance with guidance, is consistent with our knowledge and is not otherwise misleading.</p>
Remuneration Report	The Remuneration Report has been prepared in accordance with the 2014 Regulations, disclosing the remuneration and pension benefits of Senior councillors and Senior Employees of the Council.	We have audited the disclosures of remuneration and pension benefits, pay bands, and exit packages, and we can confirm that they have been properly prepared in accordance with the regulations.
Annual Governance Statement	The Annual Governance Statement reports that the Council's governance arrangements provide assurance, are adequate and are operating effectively.	We have assessed whether the information given in the Annual Governance Statement is consistent with the Annual Accounts and has been prepared in accordance with the Delivering Good Governance in Local Government Framework.

Audit dimensions and best value



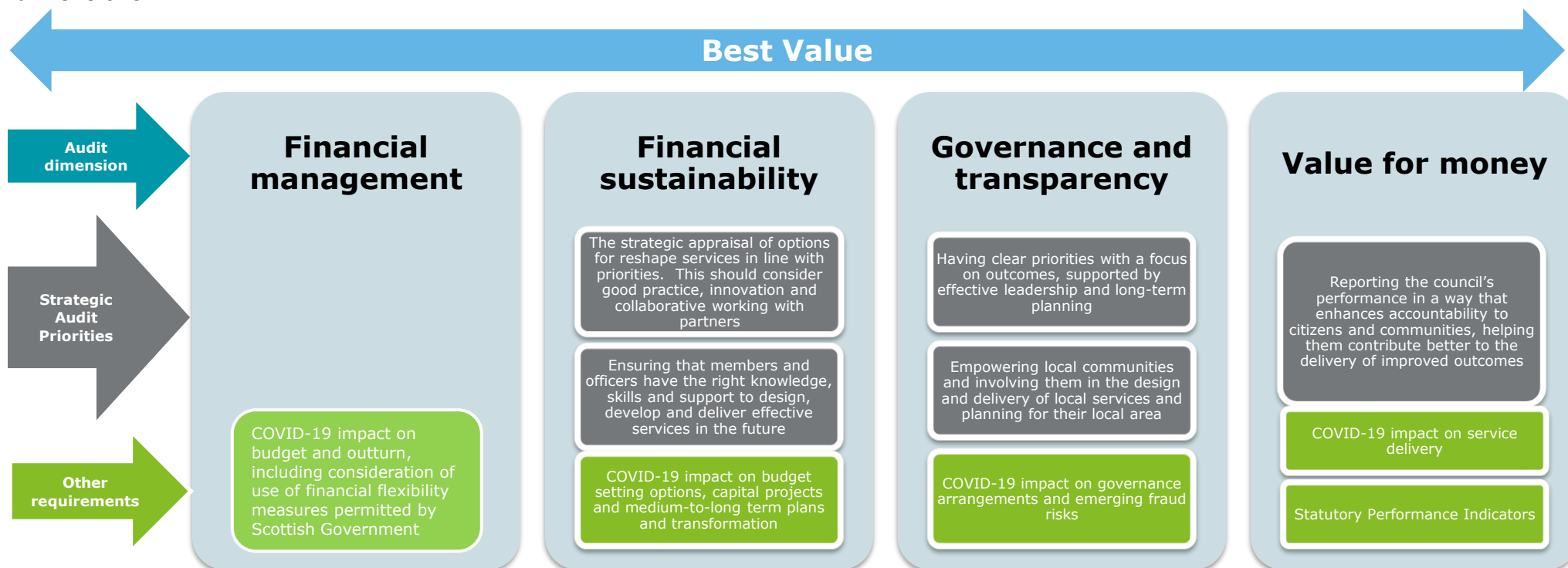
Audit dimensions and best value

Overview and conclusions

As set out in our audit plan and separate report on the “Audit Dimensions and Best Value” presented to the Committee in June 2021, public audit in Scotland is wider in scope than financial audits. Our separate report sets out our findings and conclusions on our audit work covering the areas set out below. Our report is structured in accordance with the four **audit dimensions**, but also covers our specific audit requirements on Best Value, the Accounts Commission’s **Strategic Audit Priorities (SAPs)** and the **Statutory Performance Information (SPI)** Direction.

The risk profile of public bodies for the 2020/21 audits is significantly affected by the COVID-19 pandemic. Our audit work across each dimension has therefore been specifically focussed on how the Council has responded to these risks.

In recognition of the demands on auditors’ time and the challenges of remote auditing, the Commission agreed that auditors are not required to specifically consider and report on the SAPs as part of the 2020/21 audit. The SAPs continue to be important but the work on the audit dimensions will be used to inform progress. We have therefore set out below how each SAP inter-relates to the audit dimensions.



In accordance with the Code of Audit Practice, our overall conclusions on each audit dimension and best value are summarised on the following page.

Audit dimensions and best value (continued)

Overview and conclusions (continued)

Financial management

In 2020/21, the Council's drew £1.837m on reserves (down from £21.72m drawn in 2019/20) continuing to place reliance on a draw on reserves to achieve a balanced budget.

The Council has strong financial management in place, with detailed financial management reports presented on a quarterly basis, clearly reporting on variance against budget. Management have agreed reporting could be enhanced by improving detail and clarity on revisions made to the budget.

The Council's finance team has remained consistent during the year and continues to operate effectively to support the Council's financial management arrangements.

The arrangements for prevention and detection of fraud are robust, however, the Council should ensure Internal Audit is appropriately resourced to increase the rate of audit completion.

Financial sustainability

The Council achieved short-term financial balance in 2020/21 and has set a balanced budget for 2021/22. The current level of reserves held are at an acceptable level and are in line with policy.

We are pleased to note the inclusion of savings and efficiencies are part of the 2021/22 budget and that the Council has continually reported on the financial impact of COVID-19 throughout the year.

The Council have revised their MTFP which is underpinned by realistic assumptions and the financial projections convey an accurate reflection of the financial challenge faced by the Council. We welcome the Council's commitment to revise the plan on an annual basis.

It is positive to note that the Council have revised their workforce strategy in the year, however we continued to encourage the Council to develop an action plan to underpin this strategy.

Several projects have been delayed in 2020/21 and given the ongoing impact of the pandemic, the delayed projects in 2020/21, and the Council's history of slippage for capital projects, there is a risk that the capital plan for 2021/22 and the AIP to 2025/26, is unachievable.

Governance and transparency

The Chief Executive has shown strong leadership during the pandemic, effectively communicating with staff on all levels. We are satisfied that the governance arrangements have continued to work effectively.

The political leadership of the Council remains effective, however there are weaknesses in the Council's structure, evidenced by the ongoing difficulties with fully resourcing the Council's committees, referrals to the Commissioner for Ethical Standards in Public Life in Scotland, and the providing of confidential information from Council meetings to the local media in apparent contravention of the Member's Code of Conduct. These weaknesses demonstrate that relationships and adherence to roles and responsibilities require improvement.

Audit dimensions and best value (continued)

Overview and conclusions (continued)

Governance and transparency (continued)

The Council carried out a comprehensive review of the Openness and Transparency of the organisation. This review demonstrated good practice in a number of areas and also identified areas for improvement and actions to be delivered in 2021/22. This demonstrates the Council's commitment to continuous improvement and to ensure the appropriate arrangements are in place to remain open and transparent.

We welcomed the review performed of the Integration Scheme ensuring that the Council is compliant with the IJB's governing legislation and the improved partnership working throughout the pandemic.

Value for money

The Council has a clear and robust Performance Management Framework in place which has been prepared in accordance with the Best Value Toolkit for performance management. It also has robust and long-standing arrangements in place to comply with the new SPI direction including its public performance reporting requirements.

The performance of the Council is showing evidence of improvements in a number of areas in the Local Government Benchmarking Framework. It is important that the Council reports on actual performance against target, and take any lessons learned as it moves into the recovery phase to consider alternative approaches to service delivery.

Value for money (continued)

The Council has shown a commitment to reducing inequalities in Shetland through partnership working, which has been evidenced through outcomes achieved and individual projects undertaken. We encourage the Council to incorporate addressing inequalities within strategic documents and that addressing inequalities becomes more explicit in reporting to Members.

Business cases have not been implemented as initially agreed resulting in additional costs and delays in the achievement of savings. This undermines the effectiveness and scrutiny within the Council as there is a possibility that Members would have reached alternative decisions had they been aware of the issues which eventually came to pass.

Best value

It is the duty of the Council to secure Best Value as prescribed in Part 1 of the Local Government in Scotland Act 2003. We have a statutory duty to be satisfied that the local government bodies have made proper arrangements for securing BV.

Based on our audit work performed on the four audit dimensions, we are satisfied that the Council has robust arrangements in place to secure best value and has a clear understanding of areas which require further development.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to help the Committee discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA (UK) 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Annual Report;
- Our internal control observations; and
- Other insights we have identified from our audit.

The scope of our work

Our observations are developed in the context of our audit of the Annual Accounts.

We described the scope of our work in our audit plan.

Use of this report

This report has been prepared for the Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the Committee.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the procedures performed in fulfilling our audit plan.

We welcome the opportunity to discuss our report with you and receive your feedback.



Pat Kenny, CPFA

For and on behalf of Deloitte LLP

Glasgow | 24 September 2021

Appendices



Audit adjustments

Corrected misstatements

The following misstatements have been identified up to the date of this report which have been corrected by management. We nonetheless communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

	Debit/(Credit) Comprehensive Income and Expenditure Statement (CIES) £k	Debit/(Credit) in Net Assets £k	Debit/(Credit) prior year Reserves £k	Debit/(Credit) in Income £k	If applicable, control deficiency identified
Misstatements identified in current year					
Cash and Cash Equivalents / Investments Adjustment [1]					N/A
Increase "Long-term Investments (including investments in subsidiary)"		7,954			
Decrease "Cash and Cash Equivalents"		(7,954)			
Debtors and Creditors Adjustment [2]					N/A
Decrease "Short-term Debtors"		(3,723)			
Decrease "Short-term Creditors"		3,723			
PPE and Testing Kit Adjustments [3]					
Increase in Community Care Services Expenditure	808				N/A
Increase in Community Care Services Income	(808)				
Total	-	-	-	-	

Audit adjustments (continued)

Corrected adjustments (continued)

[1] This adjustment was required following the late reporting from one external fund manager, which confirmed a series of investments had been made on 1 January 2021. The balance sheet, cash flow statements and notes 17 Financial Instruments and 19 Cash and Cash Equivalents have all been adjusted to reflect the increase in long-term investments and corresponding reduction in the balance of Cash and Cash Equivalents held by the Council as at 31 March 2021. The adjustment has also been reflected within note 35 Events after the Balance Sheet Date.

[2] During our audit work it was noted that debtors and creditors for a group entity had not been offset on a net basis, unlike in previous years. Accounting standards require consistency in treatment to enable comparability between years. An adjustment has been raised to offset the same debtors and creditors in 2020/21 to ensure comparability with 2019/20.

[3] During the audit, and after the draft Annual Accounts were completed, the Scottish Government and Audit Scotland finalised the guidance in relation to the accounting for Personal Protective Equipment and COVID-19 testing kit usage by Councils and Health and Social Care Partnerships, including the determination of principal and agency transactions. As a result, an adjustment was required to recognise donated PPE of £808k with the full amount having been utilised in year. The adjustment arose as a result of late guidance from the Scottish Government and is therefore not indicative of the quality of the draft Annual Accounts. This has an overall nil impact on the Comprehensive Income and Expenditure Statement nor was there any change to the Balance Sheet as there was no residual stock remaining at year-end.

Audit adjustments (continued)

Corrected disclosure misstatements

The following disclosure misstatements have been identified up to the date of this report which have been corrected by management. We nonetheless communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

Disclosure	Summary of disclosure requirement	Quantitative or qualitative consideration
<p><i>Note 28 Transactions relating to post-employment benefits</i></p> <p>In Note 28 there is a line for "reversal of net charges made to the surplus or deficit for the provision of services for pension benefits in accordance with the Code" which was incorrectly calculated by the Council. An adjustment of £14.924m was made to correct the calculation.</p>	<p>Code of Practice on Local Authority Accounting in the United Kingdom 2020/21 (6.4.3.45)</p>	<p>Quantitatively material</p>

Action plan (continued)

Follow-up 2019/20 action plan

We have followed up the recommendation made in our 2019/20 annual report and have noted that the recommendation made in the prior year has been partially implemented. We will continue to monitor this as part of our audit work.

Area	Recommendation	Responsible person	Target Date	Priority	2020/21 Update	Revised Target Date
<i>IT controls</i>	Given the substantial number of control deficiencies identified in the six IT systems examined, management should review existing controls and policies, making appropriate adjustments to satisfy themselves that the control environment is appropriate and that controls are designed effectively and appropriately implemented.	Executive Manager ICT	31/03/2021	Medium	<i>Partially Implemented:</i> We have addressed a number of specific issues identified during the last audit, including the implementation of a new change control process and the delivery of awareness training. The Council also approved an updated ICT Security Policy in April 2021 which outlines the roles and responsibilities of employees, line managers and teams. We will be seeking to address any of the remaining weaknesses identified in a small number of systems through 2020/21.	31/03/2022

Our other responsibilities explained

Fraud responsibilities and representations



Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

As auditor, we obtain reasonable, but not absolute, assurance that the Annual Accounts as a whole are free from material misstatement, whether caused by fraud or error.



Required representations:

We have asked the Council to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the Annual Accounts may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity or group.

We have also asked the Council to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.



Audit work performed:

In our planning we identified the risk of fraud in relation to recognition of grant income and management override of controls as a key audit risk for your organisation.

During course of our audit, we have had discussions with management and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the Annual Accounts.

Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation

We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and our objectivity is not compromised.

Fees

The audit fee for 2020/21, which is 5% below the expected fee range proposed by Audit Scotland, is £212,553 as analysed below:

	£
Auditor remuneration	139,973
Audit Scotland fixed charges:	
Pooled costs	14,010
Contribution to PABV	50,070
Audit support costs	8,100
Total fee	212,153

In addition to the above, the audit fee for the charitable trusts audit is £400.

We have still to assess any impact on additional testing performed as a result of COVID-19. Once completed, we will discuss any impact on the fee with management.

No non-audit services fees have been charged for the period.

Non-audit services

In our opinion there are no inconsistencies between the FRC's Ethical Standard and the company's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

Relationships

We are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

We are not aware of any relationships which are required to be disclosed.



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