Grant Thornton

The Annual Audit Letter for Essex Police, Fire and Crime Commissioner Fire and Rescue Authority

Year ended 31 March 2019

March 2020

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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 Essex Police, Fire and Crime Commissioner (PFCC) Fire and Rescue Authority (the Authority) for the year ended 31 March 2019.

This Letter is intended to provide a commentary on the results of our work to the Authority 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 Audit Committee in our Audit Findings Report on 26 July 2019 with a further updated report communicated to both the PFCC and the chair of the audit committee on the 09 December 2019.

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 Authority's financial statements (section two)
- assess the Authority'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 Authority'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 Authority's financial statements to be £1,302,000, which is 2**%** of the Authority's gross revenue expenditure.
Financial Statements opinion	We gave an unqualified opinion on the Authority's financial statements on 10 December 2019.
Whole of Government Accounts (WGA)	We completed work on the Authority's consolidation return following guidance issued by the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise our additional statutory powers.
Value for Money arrangements	We were satisfied that the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit report to the Authority on 10 December 2019.
Certificate	We certified that we completed the audit of the financial statements of the Essex Police, Fire and Crime Commissioner Fire and Rescue Authority in accordance with the requirements of the Code of Audit Practice on 10 December 2019.

Acknowledgements

We would like to take this opportunity to record our appreciation for the assistance provided by the Police, Fire and Crime Commissioner, the finance team, management, directors and other staff during our audit.

Audit of the Financial Statements

Our audit approach

Materiality

In our audit of the Authority'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 Authority’s financial statements to be £1,302,000, which is 2**%** of the Authority’s gross revenue expenditure. We used this benchmark as, in our view, users of the Authority’s financial statements are most interested in where the Authority has spent its revenue in the year.

We set a lower threshold of £65,000, above which we reported errors to those charged with governance 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 financial statements, the narrative report and the annual governance statement published alongside the financial statements to check it is consistent with our understanding of the Authority and with the financial statements included in the Annual Report 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 Authority’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
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. The Authority/Fund faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance. We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk of material misstatement.	As part of our work we: • evaluated the design effectiveness of management controls over journals • analysed the journals listing and determine 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 made by management and consider their reasonableness with regard to corroborative evidence • evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions	**Finding:** As part of our work on journals we identified that three super users also had finance processing duties. We performed additional work to assess whether suppliers had been inappropriately created by these super users on the Accounts Payable system. We also performed work to assess whether any journals during 2018/19 had been approved through this super user access. **Conclusion** From the results of our work we were satisfied that we had obtained sufficient appropriate evidence over the risk set out in the audit plan.
Incomplete or inaccurate financial information transferred to the new payroll system At the end of 2018, you implemented a new payroll system. When implementing a new significant accounting system, it is important to ensure that sufficient controls have been designed and operate to ensure the integrity of the data. There is also a risk over the completeness and accuracy of the data transfer from the previous system. We therefore identified the completeness and accuracy of the transfer of information to the new payroll system as a significant risk of material misstatement.	As part of our work we: • completed an information technology (IT) environment review to evaluate the design and implementation effectiveness of controls pertaining to the transfer of data from the old payroll system to the new. • performed substantive validity checks to obtain material assurance that balances, both at the individual and aggregate level, have been transferred completely and accurately.	**Conclusion** From the results of our work we were satisfied that we had obtained sufficient appropriate evidence over the risk set out in the audit plan.

Audit of the Financial Statements

Significant Audit Risks - continued

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	As part of our work we: • 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 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 • 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	Our work identified that revaluation movements disclosed in the Property, Plant and Equipment (PPE) note of the Authority's draft financial statement were incorrect. Whilst the net movement was correctly stated, management had disclosed the movement incorrectly in both the top and bottom half of the disclosure note. See appendix C for details of the disclosure adjustment. Our work on revaluations also discovered management used indices to revalue land and buildings since 2015. Management's valuer wrote to us to confirm that their work is not to be used for capital accounting purposes. A desktop indices revaluation is not a revaluation method compliant with the Code as set out in paragraph 4.1.2.4. As management had not complied with the Code in arriving at the accounting entries, we raised a control recommendation (appendix B). Notwithstanding the fact that the method of revaluation used by management did not comply with Code, our testing further identified that management had updated the accounts incorrectly based on the indices provided by the valuer. Given the number of issues identified, we concluded there was insufficient evidence to support the value of the Authority's PPE as at 31 March 2019. Management instructed their valuers to perform a full revaluation of their land and buildings. Management's expert concluded this work on the 26 November 2019 and we were provided with the full report on the 27 November. Management also provided an updated set of financial statements to reflect the revised revaluation values. The exercise by the valuer confirmed that the assets had previously been materially misstated in the original draft accounts by circa £18m. In relation to the revised valuation, in addition to reperforming the bullet-pointed procedures beside, we also performed the following (set out overleaf)

Audit of the Financial Statements

Significant Audit Risks - continued

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 (continued)	In relation to the revised revaluation we performed the following: • 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 valuation expert • wrote 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 • 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 • independently tested the accuracy of information provided to the valuer • challenged management judgements pertaining to surplus assets • Undertook reconciliatory work to assess the completeness of information sent and received by the valuer • used an auditor's expert to assess the reasonableness of the valuation movement	**Findings from work performed on the revised revaluation:** From the results of this work we identified from the valuers report that 11 assets totalling (£2.9m) were classified as surplus and therefore valued at fair value. This contradicted the information presented in the statement of accounts as no surplus assets were disclosed. The issue was raised with management who provided us with a formal judgement as to why these 11 assets were not surplus and so should be included within operational land and building. Having considered this judgement, we are satisfied that it is reasonable. Nonetheless, the valuation method of 'Fair Value' is not appropriate for these assets because, in accordance with the Code, operational land and building are to be valued at Existing Use Value (EUV). Whilst we are satisfied that the difference in valuation methodology does not lead to a material misstatement, it does signal a control issue in the process of instructing the valuer to perform their work. As a result, a recommendation was made to improve this process – see appendix B for details. Conclusion From the results of our work and taking into account adjustments set out in appendix C, we were satisfied that we obtained sufficient appropriate evidence over the valuation of land and buildings in the final set of accounts.

Audit of the Financial Statements

Significant Audit Risks - continued

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 the pension fund net liability	As part of our work we: • identified 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 experts (actuaries) for this estimate and the scope of the actuary's work • assessed the competence, capabilities and objectivity of the actuaries who carried out the Authority's pension fund valuations • assessed the accuracy and completeness of the information provided by the Authority to the actuaries 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 reports from the actuaries • 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 • sought assurances from the auditor of Essex County Council 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.	**Impact of the McCloud transitional protection pensions ruling** The Court of Appeal ruled in December 2018 that there was age discrimination in the judges and firefighters pension schemes where transitional protections were given to scheme members. The Government applied to the Supreme Court for permission to appeal this ruling, but this permission to appeal was refused in late June 2019. The case will now be remitted back to employment tribunal for remedy. The legal ruling around age discrimination (McCloud - Court of Appeal) has implications not just for your pension funds, but also for other pension schemes where they have implemented transitional arrangements on changing benefits. For the Authority, this encompasses both the Firefighters Pension Scheme and the Local Government Pension Scheme. As a result of developments post period end in relation to the McCloud case, management requested estimates from their actuaries of the potential impact of the McCloud ruling. The actuary's estimate for the Firefighters Pension Scheme was of a likely increase in past service cost and overall pension liabilities of £29,888k. For the Local Government Pension Scheme, the Actuary has estimated the impact to be an increase in past service cost of £805k. We employed an auditor's experts to review the analysis performed by the actuaries for both the Firefighters Pension Scheme and Local Government Pension Scheme. Our expert considered whether the approach that has been taken to arrive at these estimates is reasonable. Based on our review and consideration of our expert's findings, we are satisfied that the assumptions and methodology used by management's expert is reasonable. There is sufficient evidence to indicate that a liability is probable, in particular in light of the Supreme Court refusal of the right to appeal the original judgement. As such, management updated their financial statements to reflect the revised liability and service cost figures provided by their actuaries. This has resulted in changes to the Comprehensive Income and Expenditure Statement, Balance Sheet and Movement in Reserves Statement, as well as a number of the Notes to the financial statements including the Expenditure and Funding Analysis and explanatory note, Adjustments between Accounting Basis and Funding Basis under Regulation, Unusable Reserves and Defined Benefit Pension Schemes. This impact is set out in Appendix C.

Audit of the Financial Statements

Significant Audit Risks - continued

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 the pension fund net liability (continued)		**Impact of Guaranteed Minimum Pension (GMP) equalisation ruling** The High Court has ruled that defined benefit pension schemes must remove any discriminatory effect that guaranteed minimum pension entitlements have had on members benefits. The Government has announced an "interim solution" for members in public service schemes, including the Firefighters Pension Scheme and the Local Government Pension Scheme. We performed specific work to ensure that the impact had been sufficiently included within the pension liability calculations. We are satisfied that all material liabilities arising from the GMP ruling have been included for both schemes in the balance sheet, having already been considered in the original actuarial valuations obtained for the draft financial statements, or otherwise having an immaterial impact. No amendment to the financial statements has been required as a result of this issue. **Conclusion** From the results of our work and taking into account adjustments set out in appendix C, we were satisfied that we had obtained sufficient appropriate evidence over the valuation of the pension fund net liability in the final set of accounts.

Audit of the Financial Statements

Audit opinion
We gave an unqualified opinion on the Authority's financial statements on 10 December 2019.

Preparation of the financial statements
The Authority presented us with draft financial statements in accordance with the national deadline, and a set of working papers to support them.

Issues arising from the audit of the financial statements
We reported the key issues from our audit to the Authority's Audit Committee on 26 July 2019 with a further update being shared with the Police, Fire and Crime Commissioner and the chair of the Audit Committee on the 9 December 2019.

In addition to the key audit risks reported above, we identified a number of issues throughout our audit that we have asked the Authority's management to address for the next financial year: Refer to appendix B for details.

Annual Governance Statement and Narrative Report
We are required to review the Authority's Annual Governance Statement and Narrative Report. It published them on its website within its unaudited financial statements in line with the national deadlines. Following the completion of our audit work and the publication of our audit report, the Authority has since uploaded its audited financial statements which also contains the Annual Governance Statement and Narrative Report.

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 Authority and with our knowledge of the Authority.

Whole of Government Accounts (WGA)
We carried out work on the Authority's Data Collection Tool in line with instructions provided by the NAO . We issued an assurance statement which confirmed the Authority was below the audit threshold.

Certificate of closure of the audit
We certified that we have completed the audit of the financial statements of Essex Police, Fire and Crime Commissioner Fire and Rescue Authority in accordance with the requirements of the Code of Audit Practice on 10 December 2019.

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 November 2017 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.

Overall Value for Money conclusion

We are satisfied that in all significant respects the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2019.

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Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Fire and Rescue Plan *The risk associated with having ineffective arrangements for the development of the new Fire and Rescue Plan*	• We assessed the arrangements in place for the development of this plan, with a focus on the effectiveness of the arrangements in ensuring that appropriate priorities are selected. • We reviewed arrangements in place to identify measures against which progress against the plan will be assessed.	**Findings/Recommendation:** None **Conclusion:** We were satisfied from the work performed that sufficient arrangements are in place to mitigate the risk identified.
Culture change programme *The risk associated with having ineffective arrangements to plan and implement the Cultural change programme*	• We assessed the effectiveness of governance arrangements in place to plan and implement the next phase of the cultural change programme and drive transformation in behaviours, culture and ways of working. • We reviewed how you have incorporated the findings from Essex County Council's review in early 2018 of progress made by the Authority since the publication of the Lucas Review Report.	**Findings/Recommendation:** Whilst we have seen evidence of good work in relation to culture change, there is scope to add further structure in respect of mapping the journey and identifying key metrics upon which you will assess progress. This includes 'soft' metrics focused on the 'how' as well as 'hard metrics' focused on the what. **Conclusion:** Notwithstanding the above, we were satisfied from the work performed that sufficient arrangements are in place to mitigate the risk identified.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Collaboration with the Police under the PFCC structure *The risk associated with ineffective governance arrangements for partnership working with the Police under the PFCC structure*	• We reviewed the arrangements in place for collaboration with the Police under this new governance structure and assess the extent to which the benefits articulated in the business case for change have been realised..	**Findings/Recommendation:** The arrangements to identify and quantify cashable benefits in relation to collaboration programmes continue to progress. Where cashable benefits are identified from collaboration, these need to be embedded within the medium term financial plans of Essex Police and Essex Fire. There is currently some disconnect between the work of the collaboration team within the PFCC and the arrangements for strategic financial planning within both organisations. **Conclusion:** Notwithstanding the above, we were satisfied from the work performed that sufficient arrangements are in place to mitigate the risk identified.
Financial strategy and long term sustainability *The risk associated with ineffective arrangements to secure medium and long term financial sustainability, including the reserves strategy*	• We reviewed updates to your medium term financial strategy, assess the gaps in savings requirements, and assess the long term sustainability of your reserves strategy, as well as how well your planned use of reserves is articulated in your strategies.	**Findings/Recommendation:** Once the Authority has developed its new target operating model and IRMP, these business planning arrangements need to be aligned and factored into the Authority's medium term financial plan. As management begins to transform the Fire and Rescue service, they will need to strengthen arrangements to monitor and report delivery against savings. Currently, the monthly budget monitoring report does not disaggregate achievement against savings plans from performance against the budget. This runs the risk of not being able to differentiate the achievement – or otherwise – of true base line savings from fortuitous underspends. Management should review budgeting and forecasting arrangements to understand the reason for the significant variance in 2018-19 to outturn, considering whether there are issues in the baseline budget for 2019-20 as this impacts the reliability of the MTFP forecast and therefore the VFM of any strategic decisions taken based on the information. **Conclusion:** Notwithstanding the above, we were satisfied from the work performed that sufficient arrangements are in place to mitigate the risk identified.

A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit and confirm there were no fees for the provision of non audit services.

Reports issued

Report	Date issued
Audit Plan	February 2019
Audit Findings Report	26 July 2019 with an updated version being communicated on 9 December 2019
Annual Audit Letter	February 2020

Fees for non-audit services

Service	Fees £
Audit related services - None	Nil
Non-Audit related services - None	Nil

Non- audit services

- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Authority. 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 Authority's auditor and have ensured that appropriate safeguards are put in place.

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

Appendix B

B. Financial statement audit action plan

We identified 4 recommendations for the Authority as a result of issues identified during the course of our financial statement audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2019/20 audit. The matters reported here are limited to those deficiencies that we identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

	Assessment	Issue and risk	Recommendations
1	●	Your revaluation process is not compliant with the requirements of the Local Government CIPFA Code of Practice.	Following a full revaluation exercise in 2019/2020, you will need to implement a revaluation policy which ensure your assets are revalued sufficiently regularly but also ensures the carrying value of your assets is not materially different from the current value as at the 31 March.
2	●	As part of our work on the journal I.T. control environment we identified three people who had both super user access and financial processing duties. These two roles are incompatible and flag as a segregation of duties issue. We have performed additional work to assurance ourselves that this incompatibility has not resulted in a material issue in your statement of accounts.	Review systems access to your financial systems and ensure super user access is restricted to appropriate persons.
3	●	Given the difficulties we faced obtaining evidence to support previous decisions made in relation to the historical use of capital receipts, we recommend you strengthen the documentation of judgements and decision making in these areas, and ensure your MRP policy is updated to fully reflect the decisions intended to be taken and approved by the Authority.	Strengthen the documentation of judgements and decision making in relation to capital financing, and ensure your MRP policy is updated to fully reflect the decisions intended to be taken and approved by the Authority.

Controls

- ● High – Significant effect on control system
- ● Medium – Effect on control system
- ● Low – Best practice

B. Financial statement audit action plan- continued

	Assessment	Issue and risk	Recommendations
4	● Medium	As part of our work on your full revaluation exercise, we identified 11 assets (£2.9m) which were classified as surplus in the valuers report but were not classified as surplus in your statement of accounts. In response to our challenge, management provided us with a formal judgement setting out a rationale as to why the assets were not surplus and therefore correctly included within operational land and building. Whilst we are satisfied that the judgement is reasonable, these assets were nevertheless incorrectly valued at Fair Value, instead of Existing Use Value (EUV) as required by the Code. Whilst we are satisfied that the difference in valuation methodology does not lead to a material misstatement, it does indicate a weakness in the controls put in place by management pertaining to the valuation exercise.	Ensure the valuer is instructed to value assets on the right basis. In order to do so, management will need to have a formal process to make judgments, in accordance with the accounting framework, as to the correct classification of assets as at 31 March 2019.

Controls

- High – Significant effect on control system
- Medium – Effect on control system
- Low – Best practice

C. Audit Adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2019.

	Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000
1	**Impact of the McCloud pensions ruling** Management requested estimates from their actuaries of the potential impact of the McCloud ruling. The actuary's estimate for the Firefighters Scheme was of a possible increase in past service cost and overall pension liabilities of £29,888k The actuary's estimate for the Local Government Pension Scheme was of a possible increase in past service cost and overall pension liabilities of £805k. This will result in changes to the draft Comprehensive Income and Expenditure Statement, Balance Sheet and Movement in Reserves Statement, as well as a number of the Notes to the financial statements including the Expenditure and Funding Analysis and explanatory note, Adjustments between Accounting Basis and Funding Basis under Regulation, Unusable Reserves and Defined Benefit Pension Schemes.	30,693	(30,693)	30,693
2	**Impact of the full PPE revaluation** Following a full revaluation of your Land and Buildings the valuer has estimated the net increase to be £17,706k. The increase in your asset value has lead to a gain in your revaluation reserve (unusable reserve) of £11,656k. The rest (£6,050k) has been reversed through your CIES. Note, any gain through the CIES is then reversed out through the MIRS into the Capital Adjustment Account (unusable reserve).	CIES = (6,050)	PPE = 17,706	**Net impact on CIES:** (6,050) **Gain in Other Comprehensive income:** Gain to revaluation reserve = (11,656) **MIRS:** Gain to CIES reversed out of the general fund to the CAA. Increase to CAA (6,050)
	Overall impact	**24,643**	**(12,987)**	**24,643**