

Essex Fire Authority

Annual Audit Letter for the year ended 31 March 2015

October 2015

Ernst & Young LLP





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12 October 2015

Dear Members

Annual Audit Letter 2014/15

The purpose of this annual audit letter is to communicate the key issues arising from our work to the Members and external stakeholders, including members of the public.

We have already reported the detailed findings from our audit work in our 2014/15 Audit Results Report presented to the 23 September 2015 Policy and Strategy Committee, representing those charged with governance. We do not repeat those findings here.

The matters reported here are those we consider most significant for Essex Fire Authority.

We would like to take this opportunity to thank officers for their assistance during the course of our work.

Yours sincerely

Debbie Hanson
Director
For and on behalf of Ernst & Young LLP
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Relevant parts of the Audit Commission Act 1998 are transitionally saved by the Local Audit and Accountability Act 2014 (Commencement No. 7, Transitional Provisions and Savings) Order 2015 for 2014/15 audits.

The Audit Commission's 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the accountable officer of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

1. Executive summary

Our 2014/15 audit work was undertaken in accordance with our Audit Plan issued in March 2015 and was conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The Authority is responsible for preparing and publishing its Statement of Accounts, accompanied by an Annual Governance Statement (AGS). In the AGS, the Authority reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Authority is also responsible for having proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- forming an opinion on the financial statements, and on the consistency of other information published with them
- reviewing and reporting by exception on the Authority's AGS
- forming a conclusion on the arrangements the Authority has to secure economy, efficiency and effectiveness in its use of resources
- undertaking any other work specified by the Audit Commission and the Code of Audit Practice.

Summarised below are the results of our work across all these areas:

Area of work	Result
Audit of the financial statement of Essex Fire Authority for the financial year ended 31 March 2015 in accordance with International Standards on Auditing (UK & Ireland)	On 25 September 2015 we issued an unqualified audit opinion on the Authority's financial statements
Form a conclusion on the arrangements the Authority has made for securing economy, efficiency and effectiveness in its use of resources	On 25 September 2015 we issued a qualified value for money conclusion. In assessing the Authority's arrangements for securing economy, efficiency and effectiveness, we considered the findings from the cultural review commissioned by the Authority which was published on 2 September. As a result of the findings in the report, we were unable to conclude that the Authority's arrangements for promoting and demonstrating the principles and values of good governance during 2014/15 were adequate.
Report to the National Audit Office on the accuracy of the consolidation pack the Authority needs to prepare for the Whole of Government Accounts	The Authority is below the specified audit threshold of £350 million. Therefore we did not perform any audit procedures on the consolidation pack.
Consider the completeness of disclosures on the Authority's AGS, identify any inconsistencies with other information which we know about from our work and consider whether it complies with CIPFA/ SOLACE guidance	No issues to report

Consider whether we should make a report in the public interest on any matter coming to our notice in the course of the audit

No issues to report

Determine whether we need to take any other action in relation to our responsibilities under the Audit Commission Act

No issues to report

As a result of the above we have also:

Issued a report to those charged with governance of the Authority communicating the significant findings from our audit.

Our Audit Results Report was presented to the Policy and Strategy committee on 23 September 2015.

Issued a certificate that we have completed the audit in accordance with the requirements of the Audit Commission Act 1998 and the Code of Practice issued by the Audit Commission.

We issued our certificate on 25 September 2015.

2. Key findings

2.1 Financial statement audit

The Authority's Statement of Accounts is an important tool to show both how the Authority has used public money and how it can demonstrate its financial management and financial health.

We audited the Authority's Statement of Accounts in line with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission and issued an unqualified audit report on 25 September 2015.

Our detailed findings were reported to the 23 September Policy and Strategy Committee.

In our view, the quality of the process for producing the accounts, including the supporting working papers was good and the Authority had prepared its financial statements well.

We identified a number of amendments, which were corrected in the audited accounts. There were no items that were material individually or in total to the accounts.

The main issues identified as part of our audit were:

Significant risk 1: Risk of management override

As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

For fire authorities the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.

We designed and performed appropriate audit procedures to obtain reasonable assurance that the financial statements as a whole are free of material misstatement.

Findings:

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- ▶ We did not identify any material errors in our sample testing of journal entries or management bias in accounting estimates.
 - ▶ We did not identify any significant unusual transactions.
 - ▶ We did not identify any material errors in our sample testing of additions on property, plant and equipment.
-

Significant risk 2: Valuation of fixed assets

The Authority appointed an external valuer to carry out a full valuation of all its land and building assets as at 31 March 2015.

This work required a revaluation of the assets to the relevant basis and adjustments to be made to the asset register and financial statements to reflect the new values. The resulting entries in the Authority's accounts were likely to be material.

Findings:

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- ▶ We did not identify any material errors in our sample testing of the revaluation of land and building assets.
 - ▶ We did not identify any material errors in our sample testing of the accounting transactions for the adjustments in the financial statements.
-

Other financial statement risk: Firefighters' pension injury payments

In 2013/14, the Authority identified that payments in respect of firefighters' pension injury benefits had been incorrectly paid from the firefighters' pension fund instead of the general fund.

The Authority corrected this error in the 2013/14 financial statements. However, there remained a risk regarding the correct classification of current year payments.

Findings:

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- ▶ We did not identify any material errors in our sample testing of firefighters' pension injury payments.
-

We have no other matters to report.

2.2 Value for money conclusion

As part of our work we must also conclude whether the Authority has proper arrangements to secure economy, efficiency and effectiveness in the use of resources. This is known as our value for money conclusion.

In accordance with guidance issued by the Audit Commission, our 2014/15 value for money conclusion was based on two criteria. We consider whether the Authority had proper arrangements in place for:

- ▶ securing financial resilience, and
- ▶ challenging how it secures economy, efficiency and effectiveness.

We issued a qualified value for money conclusion on 25 September 2015.

We noted the following as part of our audit:

Arrangements to secure financial resilience: significant risk

We identified a significant risk in relation to the Authority's arrangements to secure financial resilience, as a result of the level of future budget gap in the Authority's medium term financial strategy (MTFS). The September 2014 MTFS, identifies a budget gap totalling £8.4 million over the two years from 2016/17 to 2017/18 (£3.2 million in 2016/17 and £5.2 million in 2017/18).

To address the specific risk identified we undertook a more detailed review of the Authority's MTFS and the key assumptions within this. We also looked at the level and planned use of reserves and the Authority's track record in delivering previous budgets and savings plans.

Findings:

The Authority has a strong track record of delivering its budget and planned savings, reporting underspends in previous years. In 2014/15, the Authority spent in line with its budget, and was also able to reduce the planned use of reserves of £1.8 million by approximately £1 million.

At 31 March 2015, the Authority had general fund balances of £3.7 million and earmarked reserves of £7.8 million. The general reserve represents 3.6% of planned expenditure in 2015/16 and is above the minimum level of £2.2 million recommended by the Finance Director and Treasurer. Around £3.5 million of the Authority's earmarked reserves is required for specific purposes. The remainder of around £4.3 million have been set aside to support future projects such as spend to save initiatives and is therefore available to help the implement any necessary changes to the service resulting from the 2020 Programme and the Integrated Risk Management Plan Consultation.

The MTFS includes an assumed reduction in Government funding of around £2 million per year in both 2016/17 and 2017/18. This represents around a 7% per year reduction. The MTFS is however clear regarding the uncertainty of the scale and timing of the anticipated reductions in this funding.

The Authority is also clear that plans to manage the expected reductions in funding need to be developed and that many of the changes that will be required to achieve the necessary savings will take time to develop and implement. With this in mind, the Authority has put in place its 2020 programme with the aim of transforming the Service to meet the demands of a modern Fire and Rescue Service.

As part of the 2020 Programme, the Authority is undertaking wide ranging engagement and consultation with stakeholders with the aim of designing a Fire and Rescue Service that can improve community safety, meet future strategic challenges, provide value for money and remain fit for purpose in 2020 and beyond. The Integrated Risk Management Plan is a key element of the 2020 Programme and the Fire and Rescue Service has been consulting on this widely over the 2015 Summer. The Authority aims to agree a Service Plan arising from these streams of work in early 2016.

As a result of this ongoing consultation on the future design of the service, detailed plans have not currently been developed to address the budget gaps that have been identified for 2016/17 and future years. The Authority has however already identified and earmarked reserves that will support the delivery of any agreed transformation and change programme. It is now crucial that the Authority and Service work together to agree the future Vision for the Service which enables the financial and cultural challenges that are facing Essex Fire and Rescue Service to be addressed on a timely basis.

Arrangements for securing economy, efficiency and effectiveness

We did not identify any significant risks in relation to this criterion in our Audit Plan.

However, since we issued our Plan in March 2015, the Authority commissioned a wide-ranging review to look at how the culture of the Fire and Rescue Service in Essex is having a detrimental impact on the organisation, its employees and the communities it serves. The review was initiated by the Authority in response to widely recognised and publically reported issues, which include serious incidents, allegations of bullying and intimidation, and ongoing and protracted industrial disputes.

The outcome from this review, which was undertaken by Irene Lucas CBE, was reported in an 'Independent Cultural Review of Essex County Fire and Rescue Service' which was issued to the Fire Authority in September 2015. The report was issued publically at the same time it was released to the Fire Authority.

We have considered the conclusions of this review, along with the actions the Authority has taken to address the issues it faces, as part of our value for money assessment.

Findings:

The Authority considered the report and its recommendation at a full Authority meeting in September and fully accepted its findings and recommendations. The issues outlined in the report are difficult and wide ranging, and the Authority and Fire Service will need to work together to address them. The report makes a number of recommendations which the Authority now needs to consider carefully in order to develop its detailed response and action plan to address the issues identified.

As a result of the issues identified in the report commissioned by the Authority, we have concluded that the Authority's arrangements for promoting and demonstrating the principles and values of good governance are inadequate. We therefore qualified our value for money conclusion regarding the Authority's arrangements for securing economy, efficiency and effectiveness in this respect. We do however recognise the challenging nature of the issues being faced by the Fire and Rescue Service, and the action that has been taken to try to address these in commissioning the publically reported independent review.

We will consider the Authority's response to the report and recommendations as part of our 2015/16 value for money conclusion.

2.3 Whole of Government Accounts

We performed the procedures required by the National Audit Office. The Authority is below the specified audit threshold of £350 million and therefore we were not required to audit the accuracy of the consolidation pack prepared by the Authority for Whole of Government Accounts purposes.

2.4 Annual Governance Statement

We are required to consider the completeness of disclosures in the Authority's AGS, identify any inconsistencies with the other information which we know about from our work, and consider whether it complies with relevant guidance.

We completed this work and did not identify any areas of concern.

2.5 Objections received

We did not receive any objections to the 2014/15 financial statements from members of the public.

2.6 Other powers and duties

We did not identify any issues during our audit that required us to use powers under the Audit Commission Act 1998, including reporting in the public interest.

2.7 Independence

We communicated our assessment of independence to the Policy and Strategy committee on 23 September. In our professional judgement the firm is independent and the objectivity of the audit engagement director and audit staff has not been compromised within the meaning of regulatory and professional requirements.

3. Control themes and observations

As part of our work, we obtained enough understanding of internal control to plan our audit and determine the nature, timing and extent of testing performed. We have tested the controls of the Authority only to the extent necessary for us to complete our audit. We sample tested the key controls within the payroll and pensions systems. We are not expressing an opinion on the overall effectiveness of internal control.

Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to tell the Authority about any significant deficiencies in internal control we find during our audit.

We did not identify any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in the Authority's financial statements.

4 Looking ahead

There are a number of changes in accounting and auditing requirements that could have a significant impact on the Authority's arrangements for the production of its financial statements. We have outlined what we think is the main challenge below.

Description	Impact
<p>Earlier deadline for production and audit of the financial statements from 2017/18</p> <p>The Accounts and Audit Regulations 2015 were laid before Parliament in February 2015. A key change in the regulations is that from the 2017/18 financial year the timetable for the preparation and approval of accounts will be brought forward.</p> <p>As a result, the Authority will need to produce draft accounts by 31 May and these accounts will need to be audited by 31 July.</p>	<p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p> <p>The Authority is aware of this challenge and the need to start planning for the impact of these changes. This will necessarily include review of the processes for the production and audit of the accounts, including areas such as the production of estimates, particularly in relation to pensions and the valuation of assets, and the year end closure processes.</p> <p>As the auditors, we are also reviewing our processes, including identifying areas of work that can be completed during our interim work, carrying out "dry-runs" of auditing the financial statements and issuing audit opinions earlier, and having ongoing discussions with fire authorities and local government bodies to support the earlier closedown process.</p>

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