

Annual Audit Letter

Tyne and Wear Fire and Rescue Authority
Year ending 31 March 2018





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1. EXECUTIVE SUMMARY

Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for Tyne and Wear Fire and Rescue Authority (the Authority) for the year ended 31 March 2018. Although this letter is addressed to the Authority, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the Local Audit and Accountability Act 2014 (the 2014 Act) and the Code of Audit Practice issued by the National Audit Office (the NAO). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of responsibility	Summary
Audit of the financial statements	<p>Our report issued on 31 July 2018 included our opinion that the financial statements:</p> <ul style="list-style-type: none">• give a true and fair view of the Authority's financial position as at 31 March 2018 and of its expenditure and income for the year then ended; and• have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18.
Other information published alongside the audited financial statements	<p>Our report included our opinion that the other information in the Statement of Accounts is consistent with the audited financial statements.</p>
Value for money conclusion	<p>Our report concluded that 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 ended 31 March 2018.</p>
Reporting to the group auditor	<p>On 31 July 2018 we reported that your activity was below the threshold set by the NAO, meaning we were not required to review the Whole of Government Accounts return.</p>
Statutory reporting	<p>Our report confirmed that we did not use our powers under s24 of the 2014 Act to issue a report in the public interest or to make written recommendations to the Authority.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS

Opinion on the financial statements

Unqualified

The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the Authority and whether they give a true and fair view of the Authority's financial position as at 31 March 2018 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the Authority's circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Governance Committee. We call this our trivial threshold.

The table below provides details of the overall materiality levels applied in the audit of the Authority's financial statements for the year ended 31 March 2018.

Financial statement materiality	Our financial statement materiality is based on 2% of gross operating expenditure.	£758k
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£21k

2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant risks and key areas of management judgement

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the Authority's financial statements that required special audit consideration. We reported significant risks and key areas of management judgement identified at the planning stage to the Governance Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks and judgements, the work we carried out on those risks and our conclusions.

Identified significant risk	Our response	Our findings and conclusions
<p>Management override of controls Management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur, we consider there to be a significant risk on all audits.</p>	<p>We addressed this risk by performing audit work in respect of:</p> <ul style="list-style-type: none"> accounting estimates impacting on amounts included in the financial statements; significant transactions outside the normal course of business; and journals recorded in the general ledger and other adjustments made in preparation of the financial statements. 	<p>Our work has provided the assurance we sought and has not highlighted any material issues to bring to your attention. We found no indication of management override of controls.</p>
<p>Defined benefit liability valuation The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.</p>	<p>We obtained explanations to support any significant changes to the pension estimates.</p> <p>In addition to our standard programme of work in this area, we evaluated the management controls you have in place to assess the reasonableness of the figures provided by the Actuary and considered the reasonableness of the Actuary's output, referring to an expert's report on all actuaries nationally which is commissioned annually by PSAA Ltd.</p>	<p>Our work has provided the assurance we sought and has not highlighted any material issues to bring to your attention. We found no indication of material estimation error in respect of pensions.</p>
<p>Property, plant and equipment (PPE) valuation(s) The financial statements contain material entries on the Balance Sheet as well as material disclosure notes in relation to the Authority's holding of PPE. Although the Authority employs an internal valuation expert to provide information on valuations, there remains a high degree of estimation uncertainty associated with PPE valuations because of the significant judgements and number of variables involved. We have therefore identified the valuation of PPE to be an area of risk.</p>	<p>We considered the Authority's arrangements for ensuring that PPE values are reasonable and engaged our own expert to provide data to enable us to assess the reasonableness of the valuations provided by the Authority's valuer. We also assessed the competence, skills and experience of the valuer.</p> <p>We also performed further audit procedures on individual assets to ensure that the basis and level of revaluation was appropriate.</p>	<p>Our work provided the assurance we sought. Our audit work identified that fire stations were materially understated and therefore required amendment. This was due to a significant increase in the underlying indices used to value them.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS

Internal control recommendations

As part of our audit we considered the internal controls in place that are relevant to the preparation of the financial statements. We did this to design audit procedures that allow us to express our opinion on the financial statements, but this did not extend to us expressing an opinion on the effectiveness of internal controls.

One deficiency was identified in internal control during the audit.

Error identified in the calculation of a widow's pension

Description of deficiency

We reviewed the calculation of a new widow's pension as part of our work testing pension payments in the Firefighters' Pension Fund Account. We identified an error in the calculation, and this was confirmed when it was checked and recalculated by Sunderland City Council which had administered the firefighters' pension scheme in 2017/18. The widow had been underpaid pension of approximately £2.5k in a six month period. As a consequence of this we received assurances that this was a one-off error, and to test this assertion we extended our sample. We did not find any errors in the additional new widows pensions we tested in the year.

Potential effects

Ensuring correct pension payments is essential to support those who have worked for the Authority and their dependents.

Recommendation

The Authority must ensure that all widows pensions are calculated accurately.

Management response

The Authority has recently changed its administrator for firefighters' pensions, and the Finance Manager has asked the new provider to review the calculations of all widows pensions.

3. VALUE FOR MONEY CONCLUSION

Value for money conclusion

Unqualified

Our audit approach

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

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

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

Our auditor's report (supplemented by our follow-up letter), issued to the Authority on 31 July 2018, stated that, in all significant respects, the Authority put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2018.

Sub-criteria	Commentary	Arrangements in place?
Informed decision-making	<p>The Authority is governed by a Constitution including all of the normal features of an effective governance framework in local government and related bodies.</p> <p>The Authority uses its Integrated Risk Management Plan (IRMP) to deliver significant changes to the service. In recent years, this has helped the Authority manage the challenges of public sector austerity, where significant savings have had to be delivered in light of reduced government funding.</p> <p>In January 2018 the Authority considered an IRMP Action Plan Update for 2017/20. This reported on progress against the current priorities including the actions agreed to review response relative to risk, collaborative measures with emergency services and other partners, and opportunities for further efficiency and effectiveness.</p> <p>There is evidence of financial reporting being used effectively to deliver strategic objectives, for example, through the Medium Term Financial Strategy and in allocating resources to priority areas and addressing issues such as those identified in the IRMP.</p> <p>The Authority's Annual Governance Statement includes a balanced assessment of the effectiveness of the Authority's governance arrangements and identifies appropriate areas for further improvement. The 2017/18 Annual Governance Statement provides an update on the issue reported last year in relation to overpaid fire injury pensions from 2006/07 to 2011/12 of £10.5m. The Authority has now agreed to repay this amount over a period of 17 years to the Home Office., with £1.8m being paid in 2017/18.</p>	Yes

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3. VALUE FOR MONEY CONCLUSION

Sub-criteria	Commentary	Arrangements in place?
Sustainable resource deployment	<p>The Authority has made good progress in addressing the financial challenges from public sector austerity and has a proven track record of strong budget management and delivering planned budget reductions.</p> <p>In the 2017/18 outturn, the Authority delivered a £1.273m underspend against budget. This reflected a range of predominantly one-off savings and reflects an increased focus on financial management and effective budgetary control.</p> <p>In the 2018/19 budget, the Authority identified that over the medium-term of 2018/19 to 2021/22 it faced a cumulative budget gap of £3.6m. The Authority has prudently established an earmarked reserve to match the budget gap of £3.6m so that it can be funded over this period. In the meantime, various work streams linked to the IRMP are in place seeking to deliver further savings and improvement. It is important to identify measures that deliver an annual reduction in the base budget and this is the focus of the efforts that are being undertaken.</p> <p>Subsequent to the setting of the 2018/19 budget, the Authority also concluded its negotiations with the Home Office over the repayment of the £10.5m historic overpayment of fire injury pensions. £1.8m was paid in 2017/18 utilising the reserve that had been established for this purpose. The remaining £8.7m is to be repaid over a period of 17 years at the rate of £500k per annum. Whilst this settlement has enabled the Authority to replenish its reserves which were initially utilised to provide for repayment in full, the settlement creates an additional annual budget pressure of £500k against which further annual savings will need to be delivered.</p>	Yes
Working with partners and other third parties	<p>The Authority works with a range of partners and third parties. The Government's Policing and Crime Act includes a statutory duty on all three emergency services to collaborate with each other to improve efficiency and effectiveness. It also seeks to enable Police and Crime Commissioners to take on fire and rescue responsibilities in their area where a local case is made.</p> <p>There are already good examples of the Authority working with the other emergency services, seeking to make best use of its assets, for example, through co-location with Northumbria Police and the North East Ambulance Service.</p> <p>The Authority has entered into a formal non-binding Statement of Intent with Northumbria Police which signals the intent to work together in a range of areas including sharing information, service delivery, estate and asset integration, control room, back office functions, training and development, risk assessment, public engagement and accountability and finance and procurement. The Police and Crime Commissioner is also now a member of the Fire Authority.</p> <p>The Authority is developing a more commercial approach to income generation. One area which the Authority is reviewing is its partnership arrangements with Impeller Services. This is an area which needs to be closely monitored by the Authority.</p>	Yes

3. VALUE FOR MONEY CONCLUSION

Significant audit risks

The NAO's guidance requires us to carry out work to identify whether or not a risk to the value for money conclusion exists. Risk, in the context of our work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Authority being inadequate. In our Audit Strategy Memorandum, we reported that we had identified one significant audit risk- responding to financial pressures

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

Significant risk: Responding to financial pressures

Risk: our audit work in previous years has concluded that the Authority has arrangements in place for managing its financial position. The Authority, however, continues to face financial pressure in the coming years. In addition, £10.5m of overpaid fire injury pensions are being recovered from the Authority by the Home Office.

We need to ensure our knowledge of the Authority's medium-term financial strategy (MTFS) arrangements and its monitoring of the planned delivery of savings, remains up to date in order to ensure we give the correct conclusion.

Work undertaken

Building on our work in previous years, we have reviewed the Authority's updated MTFS to ensure it reflects the latest funding position and reviewed and updated our knowledge of the arrangements the Authority has in place to monitor progress against its savings plans and income projections that underpin the MTFS.

In addition, we have assessed the impact of the final position for repayment of fire injury pensions on financial sustainability.

Conclusion

In the 2018/19 budget, the Authority identified that over the medium-term of 2018/19 to 2021/22 it faced a cumulative budget gap of £3.6m. The Authority has prudently established an earmarked reserve to match the budget gap of £3.6m so that it can be funded over this period. In the meantime, various work streams linked to the IRMP are in place seeking to deliver further savings and improvement.

It is important to identify measures that deliver an annual reduction in the base budget and this is the focus of the efforts that are being undertaken.

Subsequent to the setting of the 2018/19 budget, the Authority also concluded its negotiations with the Home Office over the repayment of the £10.5m historic overpayment of fire injury pensions. £1.8m was paid in 2017/18 utilising the reserve that had been established for this purpose. The remaining £8.7m is to be repaid over a period of 17 years at the rate of £500k per annum.

Whilst this settlement has enabled the Authority to replenish its reserves which were initially utilised to provide for repayment in full, the settlement creates an additional annual budget pressure of £500k against which further annual savings will need to be delivered.

The Authority has managed a difficult financial position well, but now needs to deliver further savings in the base budget to balance the budget over the medium to long term and secure the financial sustainability of the service. It is clear that this is an important priority for the Authority.

Overall we obtained sufficient assurance to mitigate the audit risk.

4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	No matters to report
Completion of NAO group audit reporting requirements	Below reporting threshold
Other information published alongside the audited financial statements	Consistent

The NAO's Code of Audit Practice and the 2014 Act place wider reporting responsibilities on us, as the Authority's external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

Matters which we report by exception

The 2014 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- issue a report in the public interest;
- make a referral to the Secretary of State where we believe that a decision has led to, or would lead to, unlawful expenditure, or an action has been, or would be unlawful and likely to cause a loss or deficiency; and
- make written recommendations to the Authority which must be responded to publically.

We have not exercised any of these statutory reporting powers.

Reporting to the NAO in respect of Whole of Government Accounts (WGA) consolidation data

On 31 July 2018 we reported that your activity was below the threshold set by the NAO, meaning we were not required to review the Whole of Government Accounts return.

Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the Authority. In our opinion, the other information in the Statement of Accounts is consistent with the audited financial statements.

5. OUR FEES

Fees for work as the Authority's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to the Governance Committee in March 2018.

Having completed our work for the 2017/18 financial year, we can confirm that our final fees are as follows:

Area of work	2017/18 proposed fee	2017/18 final fee
Delivery of audit work under the NAO Code of Audit Practice	£30,636	£30,636

Fees for other work

We confirm that we have not undertaken any non-audit services for the Authority in the year.

6. FORWARD LOOK

Financial outlook

The Authority has continued to make good progress in addressing the financial challenges from public sector austerity and has a proven track record of strong budget management and delivering planned budget reductions.

In the 2018/19 budget, the Authority identified that over the medium-term of 2018/19 to 2021/22 it faced a cumulative budget gap of £3.6m. The Authority has prudently established an earmarked reserve to match the budget gap of £3.6m so that it can be funded over this period. In the meantime, various work streams linked to the IRMP are in place seeking to deliver further savings and improvement.

Subsequent to the setting of the 2018/19 budget, the Authority also concluded its negotiations with the Home Office over the repayment of the £10.5m historic overpayment of fire injury pensions. £1.8m was paid in 2017/18 utilising the reserve that had been established for this purpose. The remaining £8.7m is to be repaid over a period of 17 years at the rate of £500k per annum. Whilst this settlement has enabled the Authority to replenish its reserves which were initially utilised to provide for repayment in full, the settlement creates an additional annual budget pressure of £500k against which further annual savings will need to be delivered.

To bridge the savings gap, Members will once again face the need for difficult decisions to balance the budget over the medium term.

Looking forward to 2020/21, the Authority is facing major uncertainties in relation to business rates retention and the fair funding review.

Operational and strategic challenges

As set out above, the key areas of focus for the Authority will be continued strong budget management given the continued financial pressures, as well as the challenge of maintaining and improving service delivery in the face of delivering further savings.

Against a backdrop of continued reductions in funding and future uncertainty, the Authority will require organisational capacity, continued good governance and strong risk and project management arrangements. The Authority will need to ensure operational and financial plans deliver statutory duties within available resources.

How we will work with the Authority

In terms of the technical challenges that officers face around the production of the statement of accounts, we will continue to work with them to share our knowledge of new accounting developments and we will be on hand to discuss any issues as and when they arise. A key focus in the coming year will be the adoption of IFRS 9 Financial Instruments, a new standard for 2018/19, which changes the approach to financial assets and accounting for impairment.

Looking further ahead, IFRS 16 Leases is a new standard to be adopted from 2019/20, which establishes a new model for lessees and removes existing classifications of operating and finance leases. It is anticipated that the impact on the accounts of this could be material.

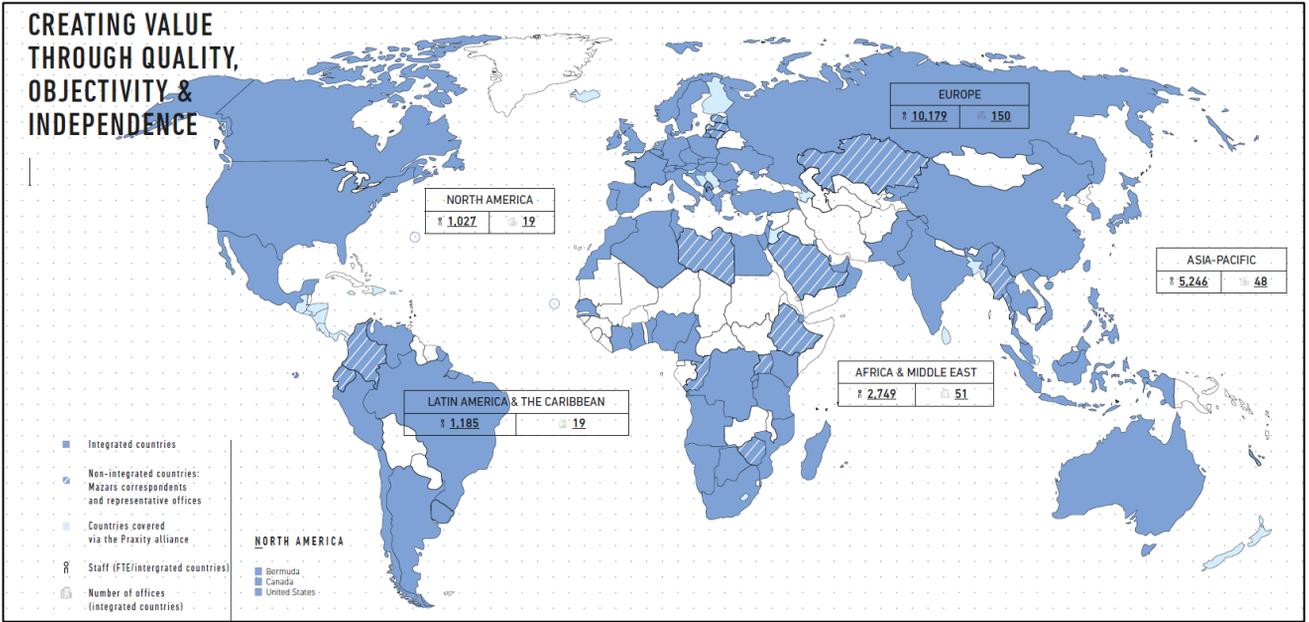
We will continue to offer accounting workshops to finance officers and the audit team will continue to work with them to share our knowledge of new accounting developments and we will be on hand to discuss any issues as and when they arise.

MAZARS AT A GLANCE

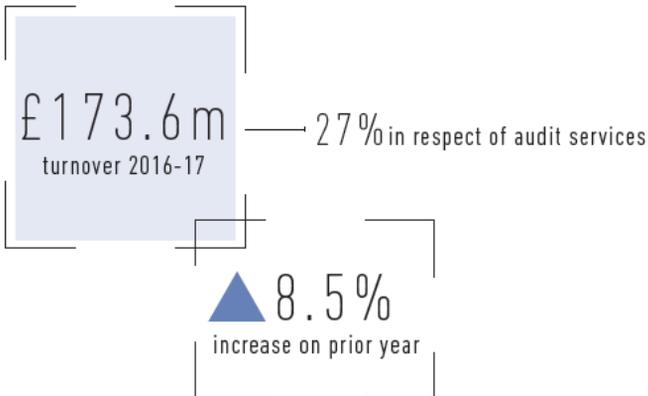
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Mazars Internationally



Mazars in the UK



As at 31 August 2017

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