

Annual Audit Letter

Cleveland Fire Authority

Year ending 31 March 2019





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Our reports are prepared in the context of the 'Statement of responsibilities of auditors and audited bodies' issued by Public Sector Audit Appointments Ltd. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the Authority and we take no responsibility to any member or officer in their individual capacity or to any third party.

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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 Cleveland Fire Authority for the year ended 31 March 2019. 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 auditor's report issued on 26 July 2019 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 2019 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 2018/19.
Other information published alongside the audited financial statements	<p>Our auditor's report issued on 26 July 2019 included our opinion that:</p> <ul style="list-style-type: none">• The other information in the Statement of Accounts is consistent with the audited financial statements.
Value for Money conclusion	<p>Our auditor's 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 2019.</p>
Reporting to the group auditor	<p>In line with group audit instructions issued by the NAO, on 26 July 2019 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 auditor's 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 2019 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 auditor's report, issued to the Authority on 26 July 2019, stated that, in our view, the financial statements give a true and fair view of the Authority's financial position as at 31 March 2019 and of its financial performance for the year then ended.

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 the concept of 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 Authority. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2019:

Financial statement materiality	Our financial statement materiality is based on 2% of Gross Revenue Expenditure at Surplus/deficit on Provision of Services level	£962,000 (£1,054,000 for the Group)
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£29,000 (£32,000 for the Group)
Specific materiality	We applied a lower level of materiality to the following areas of the accounts: <ul style="list-style-type: none">• Members allowances• Senior Officer Remuneration	£1,000 £43,000

2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant risks

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 identified at the planning stage to the Audit and Governance Committee within the 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, 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 In all entities, 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. Due to the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.</p>	<p>How we addressed this risk We addressed this risk through performing audit work over:</p> <ul style="list-style-type: none"> Accounting estimates impacting on amounts included in the financial statements; Consideration of identified 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 audit work has provided the assurance we sought and has not identified any material issues to bring to your attention. There is no indication of management override of controls.</p>
<p>Revenue Recognition In accordance with ISA 240 we presume there is a risk of fraud in respect of the recognition of revenue because of the potential for inappropriate recording of transactions in the wrong period. ISA 240 allows the presumption to be rebutted but, given the Authority's range of revenue sources and their volatility we have concluded that there are insufficient grounds for rebuttal in 2018/19. This does not imply that we suspect actual or intended manipulation but that we continue to deliver our audit work with appropriate professional scepticism.</p>	<p>We addressed this risk by performing work in the following areas: We addressed this risk by evaluating the design and implementation of controls to mitigate the risk of income being recognised in the wrong period. In addition, we undertook a range of substantive procedures including:</p> <ul style="list-style-type: none"> testing receipts in March, April and May 2019 to ensure they have been recognised in the right year; testing any material reductions in income categories against budget and the previous year; and testing adjustment journals as above for management override with particular focus on journals moving revenue between years. 	<p>Our audit work has provided the assurance we sought and has not identified any material issues to bring to your attention. There is no indication of revenue being recognised in the wrong year.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS (CONT.)

Identified significant risk	Our response	Our findings and conclusions
<p>Property, Plant and Equipment Valuation</p> <p>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 uses a valuation expert to provide information on valuations, there remains a high degree of estimation uncertainty associated with the revaluation of PPE due to the significant judgements and number of variables involved in providing revaluations. In 2018/19 six fire stations were revalued for the first time since 2013/14. We have therefore identified the valuation of PPE to be an area of significant risk.</p>	<p>We addressed this risk by performing work in the following areas:</p> <p>We addressed this risk by considering 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 external valuer. We also assessed the competence, skills and experience of the valuer.</p> <p>We discussed methods used with the valuer and examined test valuations. We used indices provided by our own expert to confirm the assets not revalued are unlikely to have materially changed in value. We tested all revaluations in year to valuation reports and supporting calculation sheets and ensured the calculations were correct and source data agreed with floor plans.</p>	<p>Our audit work has provided the assurance we sought and have not identified any material issues to bring to your attention. An immaterial error by the valuer was identified and was disclosed as an adjusted error in our audit completion report.</p>
<p>Defined benefit liability valuation</p> <p>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 addressed this risk by performing work in the following areas:</p> <p>We discussed with key contacts any significant changes to the pension estimates. 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.</p> <p>We reviewed the appropriateness of the key assumptions included within the valuations, compared them to expected ranges and reviewed the methodology applied in the valuation. We also considered the adequacy of disclosures in the financial statements.</p>	<p>Our work has provided the assurance sought. The adjusted errors relating to pension assets and liabilities are national issues relating to legal cases and the timing of information obtained from the actuary. These were described in our audit completion report.</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. We did not identify any deficiencies in internal control as part of our audit.

3. VALUE FOR MONEY CONCLUSION

Value for Money conclusion

Unqualified

Our approach to Value for Money

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
- Working with partners and other third parties

Our auditor's report, issued to the Authority on 26 July 2019, stated that 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 31st March 2019.

Sub-criteria	Commentary	Arrangements in place?
Informed decision making	<p>We reviewed financial, performance and risk management reports throughout the year and attended meetings of the Audit and Governance Committee. We did not identify any concerns regarding data quality or the decision-making process.</p> <p>We considered the following aspects of proper arrangements specified by the National Audit Office as part of our risk assessment, and, based on our risk-based approach, we did not identify any significant issues or exceptions in the Authority's arrangements:</p> <p>a) Acting in the public interest, through demonstrating and applying the principles and values of sound governance;</p> <p>b) Understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management;</p> <p>c) Reliable and timely financial reporting that supports the delivery of strategic priorities; and</p> <p>d) Managing risks effectively and maintaining a sound system of internal control.</p>	Yes

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3. VALUE FOR MONEY CONCLUSION (CONTINUED)

Sub-criteria	Commentary	Arrangements in place?
Sustainable resource deployment	<p>Financial and performance reports demonstrate a history of achieving cost reductions without adversely affecting services to date and the Authority has balanced the 2019/20 budget through identified savings of £671K, which have already been secured by deleting posts on 1 April. General reserves of £1.5m are maintained and the £4.1M budget support fund is available to allow time for further savings to be implemented once the scale of funding reduction from 2020/21 is known. The Medium Term Financial Strategy 2018/19 to 2022/23 models two alternative scenarios that forecast a deficit of between £2.3M and £3.8M built up between 2020/21 and 2023/23. The Strategy shows that each deficit will be funded from the budget support fund until savings from ongoing projects are identified and delivered; the call on this reserve varying depending on the scenario.</p> <p>We considered the following aspects of proper arrangements specified by the National Audit Office as part of our risk assessment, and, based on our risk-based approach, we did not identify any significant issues or exceptions in the Authority's arrangements:</p> <ul style="list-style-type: none"> a) Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions; b) Managing and utilising assets effectively to support the delivery of strategic priorities; and c) Planning, organising and developing the workforce effectively to deliver strategic priorities. 	Yes



3. VALUE FOR MONEY CONCLUSION (CONTINUED)

Sub-criteria	Commentary	Arrangements in place?
Working with partners and other third parties	<p>Memoranda of understanding with other emergency services illustrate the Authority’s commitment to increase collaboration and build on long-established partnership arrangements to improve community safety. The Community Integrated Risk Management Plan (CIRMP) includes proposals for further collaboration that are currently subject to due diligence.</p> <p>We considered the following aspects of proper arrangements specified by the National Audit Office as part of our risk assessment, and, based on our risk-based approach, we did not identify any significant issues or exceptions in the Authority’s arrangements:</p> <ul style="list-style-type: none"> a) Working with third parties effectively to deliver strategic priorities; b) Commissioning services effectively to support the delivery of strategic priorities; and c) Procuring supplies and services effectively to support the delivery of strategic priorities. 	Yes

3. VALUE FOR MONEY CONCLUSION

Significant Value for Money 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 Value for Money 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 Value for Money risk. The work we carried out in relation to significant risks is outlined below.

Risk	Work undertaken	Conclusion
<p>Sustainable resource deployment beyond 2020/21</p> <p>The Government is reviewing the approach it will take to funding fire and rescue from 2020/21, but has indicated that it will not release the results of the review until late 2019. There is also considerable uncertainty about pay and pension pressures.</p> <p>The Authority has prudently built up £4.1m reserves to bridge the time between the extent of the funding gap being known and the implementation date for additional savings schemes required. The Medium Term Financial Strategy shows the savings required from 2020/21 to 2022/23 after utilising these reserves for a range of possible income and cost scenarios.</p> <p>However, there is a risk that the Authority will be unable to sustain delivery of strategic priorities in the Community Integrated Risk Management Plan (CIRMP), and maintain statutory functions beyond 31 March 2020 unless the arrangements to identify and implement additional savings are strong.</p>	<p>We reviewed the 2018/19 financial and performance outturn and the updated VFM Profile produced by the National Audit Office to identify any emerging risks to the VFM Conclusion. This review considered the latest forecasts for the level of reserves available at 31 March 2020.</p> <p>We also reviewed the Authority’s arrangements to ensure that it delivers its CIRMP, focusing especially on progress identifying additional savings from 2020/21 onwards.</p>	<p>The Authority increased its usable reserves more than budgeted in 2018/19 whilst improving performance in priority areas. The Authority reduced the number of accidental dwelling fires per head by 20% to a record low, significantly lower than all other fire authorities. This has been achieved largely through delivering the highest number of home fires safety checks per head in the country. The Authority has maintained the fastest response times to primary fires in the country.</p> <p>Year 1 projects set out in the 2018-2022 CIRMP were delivered on track and progress with year 2 projects is good, with the required 2019/20 savings already secured. Plans to implement the remaining proposals are developing in line with project milestones. These include developing a plan to offset the planning scenarios in the Medium Term Financial Plan of a £2.3M to £3.8M deficit by 2022/23. The £4.1M budget support fund provides a longer lead time to deliver the savings once the uncertainty over funding, pay and pensions is resolved.</p>



4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	No matters to report
Completion of group audit reporting requirements	Below testing 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 on 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 publicly.

We have not exercised any of these statutory reporting powers.

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

The NAO, as group auditor, requires us to complete the WGA Assurance Statement in respect of its consolidation data. We submitted this information to the NAO on 26 July 2019.

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 Audit and Governance Committee in February 2019.

We have completed our work for the 2018/19 financial year, but at the time of producing this report, we have not yet finalised our audit fees for the year. If the final fee varies from that in the table below, we will write to the Chief Financial Officer setting out the proposed variation and any reasons for the variation, and seeking agreement to it. Any variations to the final fee will also require the approval of Public Sector Audit Appointments Limited, which manages the contracts for our work.

Area of work	2018/19 proposed fee £	2018/19 final fee £ ***
Delivery of audit work under the NAO Code of Audit Practice	22,243	22,243
Group Accounts	2,926	2,926
Total Audit Fees	25,169	25,169

*** Please note that at the time of producing this report, the audit fee has not yet been finalised.

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's total income for 2019/20 is 22% (£7.3M) lower than it was in 2010/11. The Authority has done well to maintain or improve services over this period whilst keeping within budget every year and it is also on course to deliver the 2019/20 budgeted savings of £671,000.

In the Value for Money Conclusion section of this letter we indicated that the greatest financial challenge may lie further ahead because the Government is reviewing the approach it will take to funding fire and rescue from 2020/21, but has indicated that it will not release the results of the review until late 2019. The Authority currently receives £5.7M of funding in revenue support grant, which the Government has indicated it wishes to phase out as part of the review and although it is expected much of this will be compensated through other funding the Authority's reliance on grant funding increases the risk of a further reduction in overall resources following the review.

Work to develop further savings options to bridge the funding shortfall expected in 2020/21 is progressing well and using earmarked reserves to protect services in 2020/21 and 2021/22 would defer a budget shortfall to 2022/23. However, a permanent solution would then be required in 2022/23.

In addition to the reduction in government funding the Authority has several other financial pressures including:

- a risk that actual pay awards for firefighters exceed the provision included in the base budgets as although there has been recent progress, settlement has not yet been reached;
- rising employer contributions to the pension schemes with uncertainty as to the extent to which the Government will fund the increased costs; and
- the continuation of a cap on the percentage to which fire authorities can increase council tax without a costly referendum.

Operational challenges

The Authority has just been inspected by HMICFRS and expects to receive its report and grading in late 2019. Irrespective of the grading, the Authority will need to draw up an action plan to respond to opportunities for improvement identified by HMICFRS and delivering further improvement at a time of significantly diminishing resources will be challenging.

Legislative / environmental changes

The Police and Crime Act (2017) establishes a new duty on fire authorities to collaborate with other emergency services and the Authority is currently undertaking due diligence on proposals to increase collaboration with Cleveland Police.

How we will work with the Authority

We are grateful to the Authority, its Members and officers for the cooperation and open dialogue during the year and look forward to continuing to work closely with them in delivering our Code of Audit Practice responsibilities.

We are also keen to help the Authority face its many challenges through the delivery of added value work. In 2018/19 the Engagement Lead provided free member training in fire financial statements. The Engagement Manager is a former National and Regional Fire Service Lead with the Audit Commission and has substantial experience of added value work in the fire and rescue sector. We would be happy to discuss the potential for added value work as the scale of the financial challenge referred to above becomes clearer.

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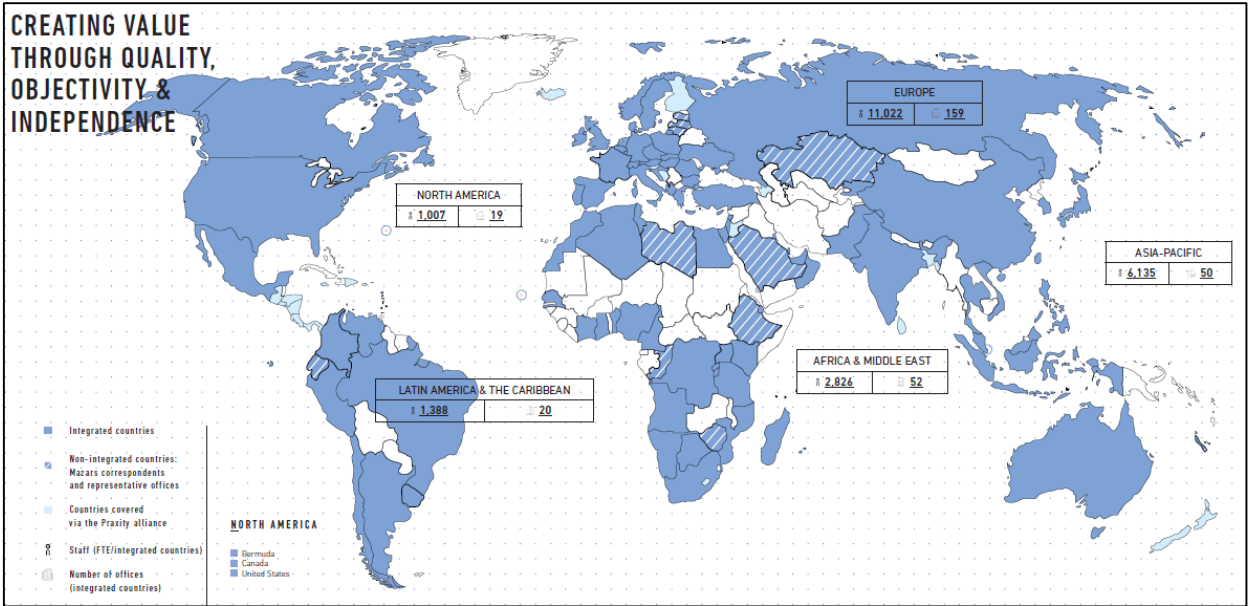
6. Forward look

MAZARS AT A GLANCE

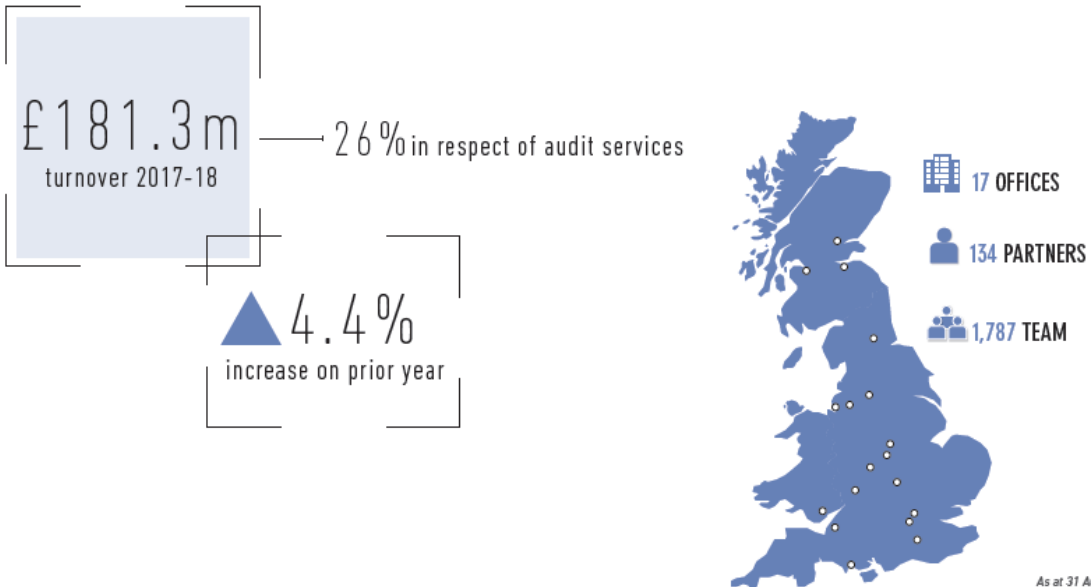
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Mazars Internationally



Mazars in the UK



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