



The Annual Audit Letter for Hereford & Worcester Fire Authority

Year ended 31 March 2020

01 December 2020



Contents



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Section

	Page
1. Executive Summary	3
2. Audit of the Financial Statements	5
3. Value for Money conclusion	11

Appendices

A Reports issued and fees	13
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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 Hereford & Worcester Fire Authority (the Authority) for the year ended 31 March 2020.

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 Authority's Audit & Governance Committee as those charged with governance in our Audit Findings Report on 8 October 2020.

Our work

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.

Materiality	We determined materiality for the audit of the Authority's financial statements to be £688,000, which equates to 2% of the Authority's forecast gross expenditure for the year.
Financial Statements opinion	<p>We gave an unqualified opinion on the Authority's financial statements on 10 November 2020.</p> <p>We included an emphasis of matter paragraph in our report in respect of the uncertainty over valuations of the Authority's land and buildings given the Coronavirus pandemic. This does not affect our opinion that the statements give a true and fair view of the Authority's financial position and its income and expenditure for the year.</p>
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.

Executive Summary

Value for Money arrangements	We were satisfied that the Authority put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit report to the Authority on 10 November 2020.
Certificate	We certified that we have completed the audit of the financial statements of Hereford & Worcester Fire Authority in accordance with the requirements of the Code of Audit Practice on 10 November 2020.

Working with the Authority

Working remotely presented a number of challenges, for auditors and officers, including remotely accessing financial systems, video calling, and additional procedures to verify the completeness and accuracy of information produced by the Authority. This resulted in considerably more audit time than initially planned.

However, we were able to give our audit opinion on 10 November, nearly three weeks before the publication deadline.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Authority's staff .

Grant Thornton UK LLP
December 2020

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 £688,000, which was 2% of the Authority's forecast gross cost of services for the year at the planning stage. 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 also set a lower level of specific materiality for the disclosure note on remuneration of individual senior managers. In view of the sensitivity of this note to the reader of the accounts, we set a materiality level of £50,000.

We set a lower threshold of £34,000, above which we reported errors to the Audit & Standards Committee 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 Statement of Accounts to check it is consistent with our understanding of the Authority and with the financial statements included in the Statement of Accounts 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
<p>Covid-19</p> <p>The global outbreak of the Covid-19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented. We expect current circumstances will have an impact on the production and audit of the financial statements for the year ended 31 March 2020, including and not limited to;</p> <ul style="list-style-type: none"> - Remote working arrangements and redeployment of staff to critical front line duties may impact on the quality and timing of the production of the financial statements, and the evidence we can obtain through physical observation - Volatility of financial and property markets will increase the uncertainty of assumptions applied by management to asset valuation and receivable recovery estimates, and the reliability of evidence we can obtain to corroborate management estimates - Financial uncertainty will require management to reconsider financial forecasts supporting their going concern assessment and whether material uncertainties for a period of at least 12 months from the anticipated date of approval of the audited financial statements have arisen; and - Disclosures within the financial statements will require significant revision to reflect the unprecedented situation and its impact on the preparation of the financial statements as at 31 March 2020 in accordance with IAS1, particularly in relation to material uncertainties. <p>We therefore identified the global outbreak of the Covid-19 virus as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>To address this risk we:</p> <ul style="list-style-type: none"> • worked with management to understand the implications the response to the Covid-19 pandemic has had on the organisation's ability to prepare the financial statements and update financial forecasts and assessed the implications on our audit approach • liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross sector responses to issues as and when they arose • evaluated the adequacy of the disclosures in the financial statements in light of the Covid-19 pandemic. • evaluated whether sufficient audit evidence using alternative approaches could be obtained for the purposes of our audit whilst working remotely • evaluated whether sufficient audit evidence could be obtained to corroborate significant management estimates such as asset valuations • evaluated management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment • discussed with management any potential implications for our audit report if we had been unable to obtain sufficient audit evidence. 	<p>We were able to obtain sufficient appropriate audit evidence to undertake our audit as we planned. However, aspects of our work were more challenging as being able to sit with colleagues and officers makes discussing issues and resolving questions much easier.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

These are the 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
<p>The revenue cycle includes fraudulent transactions (rebutted)</p> <p>Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p>Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Authority, we have determined that the risk of fraud arising from revenue recognition can be rebutted because:</p> <ul style="list-style-type: none"> • there is little incentive to manipulate revenue recognition • opportunities to manipulate revenue recognition are very limited • the culture and ethical frameworks of local authorities, including Hereford & Worcester Fire Authority, mean that all forms of fraud are seen as unacceptable. <p>Therefore we do not consider this to be a significant risk for Hereford & Worcester Fire Authority.</p>	<p>Our audit work did not identified any issues that caused us to revisit our initial assessment.</p>
<p>Management override of controls</p> <p>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.</p> <p>We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>To address this risk we:</p> <ul style="list-style-type: none"> • evaluated the design effectiveness of management controls over journals • analysed the journals listing and determined 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 by management and considered their reasonableness with regard to corroborative evidence • evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions. 	<p>Our audit work did not identified any issues in respect of management override of controls.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

These are the 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
<p>Valuation of land and buildings</p> <p>The Authority revalues its land and buildings on an annual basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Authority and group financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used</p> <p>We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>To address this risk we:</p> <ul style="list-style-type: none"> 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 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 at year end. 	<p>We noted in our Audit Plan dated 22 April 2020 that the FRC has determined that auditors need to improve the quality of audit challenge on property valuations across the sector. We therefore increased the volume and scope of our audit work to ensure an adequate level of audit scrutiny and challenge over the assumptions that underpin property valuations. This resulted in significantly more work than previous years, including review and challenge of the source data used by the valuer to prepare valuations. This work was particularly challenging as we were not able to meet in person with the valuer or officers to go through this work.</p> <p>The financial statements presented for audit did not include a material uncertainty in relation to the valuation of property and investment property as at 31 March 2020. Having questioned the valuer they confirmed that this was an omission from their valuation report and provided the Authority with further letters clarifying the situation, and officers have updated the financial statements to ensure this was properly disclosed in Note 34, page 42.</p> <p>Our work did not identify any further issues.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

These are the 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
<p>Valuation of pension fund net liability</p> <p>The Authority's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements.</p> <p>The pension fund net liability is considered a significant estimate due to the size of the numbers involved and the sensitivity of the estimate to changes in key assumptions.</p> <p>We therefore identified valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>To address this risk we:</p> <ul style="list-style-type: none"> • updated our understanding of 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 expert (an actuary) for this estimate and the scope of the actuary's work • assessed the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation • assessed the accuracy and completeness of the information provided by the Authority to the actuary 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 report from the actuary • undertook procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performed any additional procedures suggested within the report • obtained assurances from the auditor of Worcestershire 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. 	<p>Our audit work did not identified any issues in respect of the valuation of the pension fund net liability.</p> <p>In respect of the McCloud case, the draft financial statements, Note 130 – Critical Judgements in Applying Accounting Policies, noted that “The exact remedy has not been agreed by the employment tribunal but it is possible to estimate what position individuals would have been in had the transition arrangements (which are now deemed discriminatory) not applied. This recalculation undertaken by the Pension Actuaries has provided a funding figure based on one possible solution to the back funding position of the pension. However, a different solution would result in a different funding figure. At this time it is not possible to quantify this position.”</p> <p>However, after the draft financial statements were published, further guidance was provided and the pension liability was remeasured, as normal, via an actuarial report, taking account of best estimates in relation to the impact of McCloud/Sargeant judgements.</p> <p>Our work did not identify any further issues.</p>

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Authority's financial statements on 10 November 2020.

Preparation of the financial statements

The Authority's draft financial statements were signed by the Treasurer on 29 May, which was within the normal deadline, and well before the revised 31 August deadline. Officers also provided a good set of working papers to support them. However, working remotely presented a number of challenges, for auditors and officers, including remotely accessing financial systems, video calling, and additional procedures to verify the completeness and accuracy of information produced by the Authority.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Authority's Audit & Standards Committee on 8 October 2020. There were no adjustments to the financial statements that resulted in adjustments to the Authority's Comprehensive Income and Expenditure Statement (CIES) as a result of our audit work. However, during our audit HM Treasury issued updated guidance on the McCloud pension case. Officers asked the actuary (GAD) to provide an updated report incorporating the latest guidance. The affect was to reduce the Firefighters' Pension Fund net deficit by £2.35m from £363.246m to £360.896m. The impact on the CIES was to reduce current service in respect of firefighters by £0.65m from £8.76m to £8.11m and to reduce past service cost by £1.65m from £1.25m to a "gain" of £0.4m. A total of £2.3m. Officers amended the financial statements appropriately.

The financial statements were also updated to include a "material uncertainty" in respect of the valuations of property and investment property. This is now consistent with the RICS guidance and the public sector in general.

The Annual Governance Statement (AGS) was not published on the Authority website until 8 September, which was after the public inspection period had begun. We took the view that the AGS was available should

anyone have wished to review it; the accounts themselves were available and on the Authority website from the end of May; and no one had inspected them; the likelihood of anyone wishing to inspect the AGS is small; we confirmed with the Treasurer that, should anyone have wished to inspect the AGS outside of the inspection period, they would have been allowed to do so. We therefore agreed with the Treasurer to leave the inspection period unchanged.

Annual Governance Statement and Narrative Report

We are also required to review the Authority's 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 in line with instructions provided by the NAO . We issued an assurance statement which confirmed the Authority was below the audit threshold on 10 November 2020.

Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of Hereford & Worcester Fire Authority in accordance with the requirements of the Code of Audit Practice on 10 November 2020.

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 April 2020 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 put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2020.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Medium Term Financial Plan (MTFP)</p> <p>The MTFP approved in February 2020 set out the financial challenge and proposed use of reserves to bridge the short term deficit. Even with the use of £2.4m of reserves, there remains an ongoing deficit of around £0.4m from 2024/25.</p> <p>To address this risk we:</p> <ul style="list-style-type: none"> • reviewed the Authority's arrangements for updating, agreeing and monitoring its financial plans and MTFP. • reviewed progress made to address the forecast underlying and ongoing deficit. • considered any significant new savings schemes brought forward in the February 2020 MTFP to obtain assurance that they are robust and realistic. 	<p>The Budget, Precept 2020/21 and MTFP were presented in a paper to Full Authority on 12 February 2020. The report sets out the background and challenges, particularly the uncertainties in many areas. The report is clear and comprehensive, and sets out the key assumptions and risks.</p> <p>The Authority is forecasting an underlying long term deficit of around £400k per year. This has been clearly reported to Members. The underlying deficit has decreased over the years. For example, the October 2019 MTFP update reported that the Authority would need to be spending £1.2m less from 2023/24. The latest position is essentially back to where we reported in our Audit Findings Report last year, meaning that the financial challenges caused by changes to the pension contributions have been allayed through government funding.</p> <p>We selected three of the larger savings schemes for detailed testing - Crewing Changes (£250k a year), Fire Control Collaboration (£300k a year) and Wyre Forest Hub (£100k a year). While noting that none of these schemes are new, we are satisfied that the forecast savings are reasonable. The Fire Control collaboration with Shropshire Fire Authority (and/or other potential partners) requires all authorities to agree a way forward, and will need to reflect latest guidance in relation to joint working and call handling capacity, and the recommendations of the Kerslake and Grenfell enquiries.</p>	<p>Finance reports are regularly updated and reported to Members. Finances are monitored very closely - both the MTFP and quarterly reports highlight issues and amounts that are of immaterial value, but without providing too much detail. This is because the majority of the budget is pay.</p> <p>The Authority has a number of longer term transformational projects in progress which will reduce the ongoing deficit to around £400k a year. Once the long term funding from government is clearer the Authority will need to consider how best to bridge the residual gap to ensure that use of reserves to balance the budget is not required on an ongoing basis.</p>

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	April 2020
Audit Findings Report	October 2020
Annual Audit Letter	December 2020

Fees

	Planned £	Actual fees £	2018/19 fees £
Statutory audit	30,561	35,145	27,311
Total fees	30,561	35,145	27,311

Audit fee variation

As outlined in our audit plan, the 2019-20 scale fee published by PSAA of £25,311 assumes that the scope of the audit does not significantly change. There are a number of areas where the scope of the audit has changed, which has led to additional work. These are set out in the following table.

Fee variations are subject to PSAA approval.

Area	Reason	Fee proposed
Pensions – IAS 19	The Financial Reporting Council (FRC) has highlighted that the quality of work by audit firms in respect of IAS 19 needs to improve across local government audits. Accordingly, we have increased the level of scope and coverage in respect of IAS 19 this year to reflect this.	1,750
PPE Valuation – work of experts	As above, the Financial Reporting Council has highlighted that auditors need to improve the quality of work on PPE valuations across the sector. We have increased the volume and scope of our audit work to reflect this.	1,750
Raising the bar	The Financial Reporting Council has highlighted that the quality of work by all audit firms needs to improve across local audit. This required additional supervision and leadership, as well as additional challenge and scepticism in areas such as journals, estimates, financial resilience and information provided by the entity.	1,500
Covid-19	The impact of Covid 19 on our audit of the Authority's financial statements was multi-faceted, including the additional time taken to complete an audit remotely.	4,834
Total		9,834



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