The Police & Crime Commissioner for Staffordshire.
The Chief Constable for Staffordshire

Annual Audit Letter for the year ended 31 March 2018

August 2018

Contents

Public Sector Audit Appointments Ltd (PSAA) have issued a ‘Statement of responsibilities of auditors and audited bodies’. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk)

The Statement of responsibilities serves as the formal terms of engagement between 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 ‘Terms of Appointment (updated 23 February 2017)’ issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (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.

01 Executive Summary

Executive Summary

We are required to issue an annual audit letter to The Police & Crime Commissioner (PCC) for Staffordshire and The Chief Constable (CC) for Staffordshire following completion of our audit procedures for the year ended 31 March 2018.

Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinions on the: ► Group and PCC single financial statements; and ► Chief Constable financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Group, PCC and CC as at 31 March 2018 and of its expenditure and income for the year then ended
► Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the 2017/18 Group statement of Accounts and Chief Constable Statement of Accounts.
Concluding on the PCC and CC arrangements for securing economy, efficiency and effectiveness	We concluded that the PCC and CC put in place proper arrangements to secure value for money in your use of resources for the year ended 31 March 2018

Area of Work	Conclusion
Reports by exception:	
► Consistency of Annual Governance Statements	We concluded that the Annual Governance Statements were consistent with our understanding of the PCC and CC.
► Public interest report	We had no matters to report in the public interest.
► Written recommendations to the PCC and CC, which should be copied to the Secretary of State	We had no matters to report.
► Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the PCC and CC Whole of Government Accounts return (WGA).	The Group, PCC single entity and CC financial statements for 2017/18 are below the NAO's specified threshold of £500m. Therefore, there was no requirement to perform audit procedures on the consolidation pack.

Executive Summary (cont’d)

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the PCC and CC communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 24 July 2018
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office’s 2015 Code of Audit Practice.	Our certificate was issued on 31 July 2018

We would like to take this opportunity to thank the PCC and CC staff for their assistance during the course of our work.

Hassan Rohimun

Associate Partner

For and on behalf of Ernst & Young LLP

02 Purpose and Responsibilities

Purpose and Responsibilities

The Purpose of this Letter

The purpose of this annual audit letter is to communicate to the PCC, CC, members of the Ethics, Transparency and Audit Panel (ETAP) and external stakeholders including members of the public, the key issues arising from our work, which we consider should be brought to their attention.

We have already reported the detailed findings from our audit work in our 2017/18 Audit Results Report to the meeting of the ETAP on 25 July 2018 and to the PCC and CC as charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the PCC and CC.

Responsibilities of the Appointed Auditor

Our 2017/18 audit work has been undertaken in accordance with the Audit Plan that we issued on 23 January 2018 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2017/18 Group, PCC and CC financial statements; and
  - On the consistency of other information published with the Group, PCC and CC financial statements.
- Forming a conclusion on the arrangements the PCC and CC has to secure economy, efficiency and effectiveness in its use of resources.
- Reporting by exception:
  - If the annual governance statements are misleading or not consistent with our understanding of the PCC and CC;
  - Any significant matters that are in the public interest;
  - Any written recommendations to the PCC and CC, which should be copied to the Secretary of State; and
  - If we have discharged our duties and responsibilities as established by thy Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on you Whole of Government Accounts return. The PCC and CC returns are below the specified audit threshold of £500m, therefore, we did not perform any audit procedures on the return.

Responsibilities of the PCC and CC

The PCC and CC is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement. In the AGS, the PCC and CC 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 PCC and CC is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

03 Financial Statements Audit

Financial Statements Audit

Key Issues

The PCC and CC Statement of Accounts show how public money has been used and demonstrate financial management and financial health.

We audited the Group, PCC and CC 2017/18 Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 31 July 2018.

Our detailed findings were reported on 25 July 2018 to the PCC, CC and ETAP.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
Misstatements due to fraud or error The financial statements as a whole are not free of material misstatements whether caused by fraud or error. 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.	In responding to the identified risk we; • Identified fraud risks during the planning stages; • Inquired of management about risks of fraud and the controls put in place to address those risks; • Gained an understanding of the oversight given by those charged with governance of management's processes over fraud; • Considered the effectiveness of management's controls designed to address the risk of fraud; • Assessed the accounting estimates for evidence of management bias; • Performed mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries in the general ledger and other adjustments in the preparation of the financial statements; • Evaluated the business rationale for significant unusual transactions; and • Reviewed capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised. In performing the procedures above we; • did not identify any material weaknesses in controls or evidence of material management override. • did not identify any instances of inappropriate judgements being applied. • did not identify any other transactions during our audit which appeared unusual or outside the organisations normal course of business.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Risk of fraud in revenue and expenditure recognition The financial statements as a whole are not free of material misstatements whether caused by fraud or error. 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. Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income and expenditure accounts. We were focused on whether the income and expenditure had been recorded in the appropriate financial year. Items spanning financial year-end are at greater risk of inappropriate recognition due to either deliberate manipulation of financial reporting or human error when closing down the financial statements under tight deadlines.	In responding to the identified risk we: • Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias; • Reviewed and tested revenue and expenditure recognition policies; • Developed a testing strategy to test material non-grant revenue and operating expenditure streams; and. • Reviewed and tested revenue cut-off at the period end date. In performing the procedures above we concluded: • There were no matters were identified concerning the recognition policies for income from material revenue streams. • There was no evidence of management bias in management's assessment and calculation of accounting estimates for other operating expenditure. We concluded that the financial statements are free from material misstatement with respect to the recognition of income and expenditure.

Financial Statement Audit (cont'd)

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	On receipt of the draft financial statements we determined planning materiality to be: • Group £3.7m (2% of gross expenditure) • PCC single entity £2.3m (2% of group assets) • CC £3.6m (2% of gross expenditure) • Police Pension Fund statement £1.3m (2% of benefits payable)
Reporting threshold	We reported to the PCC and CC that we would report all audit differences as follows; • Group £0.187m • PCC single entity £0.180m • CC £0.113m • Police Pension Fund statement £0.065m

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- Cash and bank balances
- Remuneration disclosures including any severance payments, exit packages and termination benefits:
- Related party transactions.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

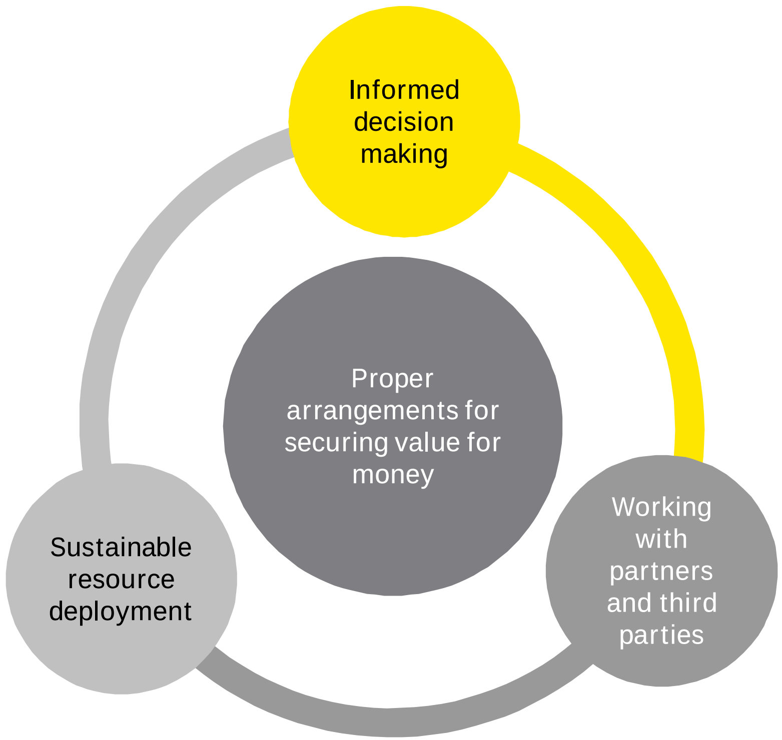
04 Value for Money

Value for Money

We are required to consider whether the PCC and CC has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.



The Audit planning Report presented to ETAP on 23 January 2018 identified three significant risks which were based on matters arising from the audit in 2016/17. The findings which we reported in our Audit Results Report are presented in the tables below.

Value for Money (cont'd)

Significant Risk	Conclusion
Securing financial resilience The organisation continues to face significant challenges. The July 2017 medium term financial strategy (MTFS) shows that projected funding gap for the four years to 2020/21 is £11.1m with the transformation change programme estimated to deliver recurring saving £6.5m to assist achieve financial balance. We have performed the following procedures: • Reviewed the MTFS including the adequacy of the major assumptions; • Understood how the PCC has considered the impact of the Local Government settlement for 2018/19 on the MTFS; and • Reviewed the arrangements that the PCC has put in place for identifying the medium term savings requirement.	Overall, based on the results of our procedures we were satisfied that appropriate arrangements were in place to address this significant risk. In preparing the MTFS a number of assumptions are made regarding the likely impact of unknown factors such as inflation levels and interest rates. The assumptions underpinning the MTFS were generally reasonable, however there were two areas where the assumptions used should have been more robustly challenged, These related major contracts, for which no inflationary uplift has been included and an inadequate budget assumption for ill-health retirements. The actual level of ill-health retirements in 2018/19 was in excess of the level assumed which resulted in £1m of additional unplanned costs. Action should be taken to ensure all budget assumptions are robustly reviewed and based on appropriate and complete information. There were overspends in the Force revenue budget and together with the anticipated capital receipt from the sale of an asset not being received before the 31 March 2018, the 2017/18 financial position was achieved through the unplanned use of reserves. The use of earmarked reserves being £2.7m greater than budget. Action will be required to review the level of reserves to ensure they remain appropriate for future needs. The July 2017 MTFS identified a funding gap to 2020/21 of £11.1m. In the updated MTFS dated January 2018, the funding gap to 2020/21, after the delivery of £6.4m of transformation savings, had increased to £12.6m. However, the funding gap identified did not reflect the impact of planned increases in the Council Tax Precept which were also outlined in the MTFS. The medium term financial position should be clearly outlined in the MTFS. A key medium term challenge will be the delivery of the £6.4m transformation savings, the Group will need to have robust processes to monitor the delivery the planned savings and to identify required contingency plans to mitigate any non delivery of key elements of the plan.

Value for Money (cont'd)

Proactive financial reporting and management

Our 2016/17 audit results report highlighted the importance of regular financial reporting. The risk of not maintaining regular financial budget reporting, to include the financial impact of the transformational change programme, will limit management's ability to determine if projected cost saving benefits are being achieved to reduce the budget gaps in the MTFS and safeguard the level of usable reserves.

We have performed the following procedures:

- Assess whether the delegated authorities of the PCC and CC have received regular financial monitoring reports to enable proactive management of the financial position during the financial year including oversight of the financial impact of the transformational change programme;
- Review the re-profiling of the capital programme during 2017/18 and confirm if the timing of the spend has been reflected in cash forecasts and the treasury management strategy for borrowing requirements

Financial Reporting

We reviewed the financial monitoring reports to determine if they provided reliable and timely information to enable senior decision-makers to manage the financial position and identify associated risks.

We found at period 9 the Group were forecasting an overspend of £0.81m We noted that for periods 10 and 11 the position deteriorated with forecasted overspends of £1.2m and £1.1m respectively. The financial position was adversely affected by three key areas;

- Fluctuations in costs associated with a significant contract that ranged from £1.2m in period 9 falling to £0.4m in period 10.
- Unplanned ill-health retirement costs due to inadequate budget assumptions when preparing the 2017/18 budget.
- The Group were planning to use a MHDCLG Flexibility Directive to fund transformation costs from capital rather than revenue. However, the anticipated capital receipt from the sale of an asset did not take place before the 31 March 2018 and as such these costs were funded from reserves

Whilst there were adequate arrangements in place to provide financial monitoring reports, action needs to be undertaken to ensure initial budget assumptions are robust and that there is earlier identification of issues to ensure appropriate mitigating action is identified and undertaken.

Use of reserves

The financial plans for 2017/18 included the use of reserves of £3.2m, however, the Group needed to draw on additional use of reserves to fund the £2.9m overspend.

We noted that although the monthly financial plans reported the impact of reserves the risks arising were not reflected in either the CC departmental or PCC and CC strategic risk registers.

Next steps

A joint financial sustainability plan has been now produced and includes the need to replenish the level of usable reserves. It is imperative that during the 2018/19 financial year, the plan is monitored by senior management in conjunction with monthly finance reports and the revised MTFS, to ensure that emerging issues are reported on a timely basis and risks are managed in accordance in with the risk management process

Value for Money (cont'd)

Arrangements to ensure key partnerships are delivering strategic objectives and cost savings	We reviewed the PCC and CC's progress against the prior year recommendation and assessed if the Group had implemented arrangements to enable it to form a clear understanding of the performance and effectiveness of its key strategic partnerships. Based on the results of our procedures we confirmed that progress had been made during 2017/18, which included the publication of a joint PCC/Force policy paper on partnership working and a partnership register which focuses mainly on the local community engagement. However, further action was still required for the PCC and CC to develop and embed arrangements to determine if the investment of staff and financial resources in key and strategic partnerships delivers the policing priorities and intended outcomes for the organisations and stakeholders of Staffordshire.

05 Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

The Group, PCC and CC financial statements are below the specified audit threshold of £500mn. Therefore, we did not perform any audit procedures on the consolidation pack.

Annual Governance Statement

We are required to consider the completeness of disclosures in PCC and CC annual governance statement, to identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any matters to report to you.

Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the PCC or CC or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the PCC or CC to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

Objections Received

We did not receive any objections to the 2017/18 financial statements from members of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the ETAP meeting on 25 July 2018 and the PCC and CC. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

Other Reporting Issues (cont'd)

Control Themes and Observations

We adopted a fully substantive approach and have therefore did not test the operation of controls. Although our audit was not designed to express an opinion on the effectiveness of internal control we were required to communicate to you significant deficiencies in internal control.

Other than the matter outlined below we did not identify any significant deficiencies in the design or operation of an internal control that might result in a material misstatement of which you are not aware.

- Inadequate processes and controls for month-end reporting:

    The account to which the monthly costs for ill-health retirements are posted had not been reviewed by management on a monthly basis. This resulted in a build up of costs which were omitted from the monthly finance reports to senior management. Consequently the expenditure and the overall revenue position was understated and the adverse position not identified at earlier stage.

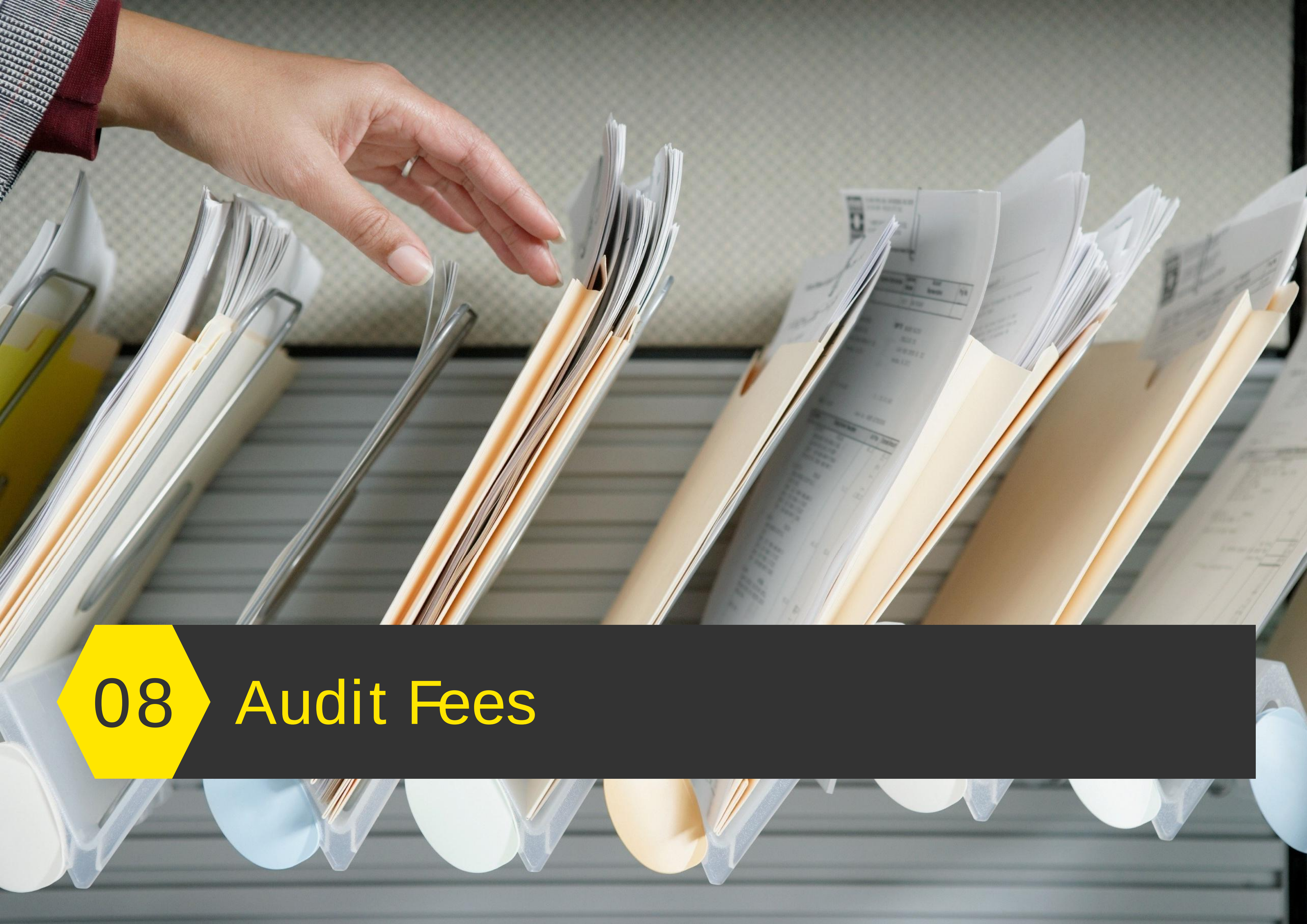
07 Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the PCC and CC is summarised in the table below.

Standard	Issue	Impact
IFRS 9 Financial Instruments	Applicable for local authority accounts from the 2018/19 financial year and will change: • How financial assets are classified and measured; • How the impairment of financial assets are calculated; and • The disclosure requirements for financial assets. There are transitional arrangements within the standard and the 2018/19 Accounting Code of Practice for Local Authorities has now been issued, providing guidance on the application of IFRS 9. In advance of the Guidance Notes being issued, CIPFA have issued some provisional information providing detail on the impact on local authority accounting of IFRS 9, however the key outstanding issue is whether any accounting statutory overrides will be introduced to mitigate any impact.	Although the Code has now been issued, providing guidance on the application of the standard, along with other provisional information issued by CIPFA on the approach to adopting IFRS 9, until the Guidance Notes are issued and any statutory overrides are confirmed there remains some uncertainty. However, what is clear is that the PCC and CC will have to: • Reclassify existing financial instrument assets • Re-measure and recalculate potential impairments of those assets; and • Prepare additional disclosure notes for material items.
IFRS 15 Revenue from Contracts with Customers	Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except: • Leases; • Financial instruments; • Insurance contracts; and • For local authorities; Council Tax and NDR income. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. Now that the 2018/19 Accounting Code of Practice for Local Authorities has been issued it is becoming clear what the impact on local authority accounting will be. As the vast majority of revenue streams of Local Authorities fall outside the scope of IFRS 15, the impact of this standard is likely to be limited.	As with IFRS 9, some provisional information on the approach to adopting IFRS 15 has been issued by CIPFA in advance of the Guidance Notes. Now that the Code has been issued, initial views have been confirmed; that due to the revenue streams of Local Authorities the impact of this standard is likely to be limited. The standard is far more likely to impact on Local Authority Trading Companies who will have material revenue streams arising from contracts with customers. The PCC and CC will need to consider the impact of this on their own group accounts when that trading company is consolidated.

Focused on your future (cont'd)

Standard	Issue	Impact
IFRS 16 Leases	It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. There are transitional arrangements within the standard and although the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.	Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the PCC and CC will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them and ensure that all lease arrangements are fully documented.



08 Audit Fees

Audit Fees

Our fee for 2017/18 is in line with the scale fee set by the PSAA and reported Annual Results Report dated 24 July 2018.

	Final Fee 2017/18	Planned Fee 2017/18	Scale Fee 2017/18	Final Fee 2016/17
	£	£	£	£
Total Audit Fee – PCC Code work	35,558*	31,733	31,733	31,733
Total Audit Fee – CC Code work	16,850*	15,000	15,000	15,000
Other fees	0	0	0	0
Total	52,408	46,733	46,733	46,733

* The final fee for 2017/18 includes a total of £5,675 of additional fees for work carried out in response to the significant risks associated with the value for money conclusion. The additional fees are subject to approval by the PSAA.

We confirm we have not undertaken any non-audit work outside of the PSAA's requirements.

We have adopted the necessary safeguards in completing this work and complied with Auditor Guidance Note 1 issued by the NAO.

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ED None

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