

# Annual Audit Letter

## Merseyside Fire and Civil Defence Authority

### INSIDE THIS LETTER

#### PAGES 2 - 9

- Key messages
- Executive Summary
- Authority performance
- Accounts and Governance
- Looking forward
- Closing remarks

#### PAGES 10 - 12

#### Appendix 1

- Audit reports issued during 2003/04

#### Appendix 2

- Scope of the audit

#### Appendix 3

- Audit fee update

<b>Reference:</b>	MFCDA - 0304 AAL FINAL 221204.doc
<b>Date:</b>	December 2004

## Key messages

### Background

Over the last year the Authority has faced a number of key challenges including:

- managing local implications of the settlement of the national industrial dispute
- producing an integrated risk management plan (IRMP), to change traditional arrangements by using risk analysis to drive operational deployment
- the Fire and Rescue Service Act 2004
- contributing to the North West Regional Management Board set up December 2003.

These have been against a background of increasing financial constraints, with a lower than anticipated financial settlement and a range of other budgetary pressures.

### Modernisation

The national fire service pay and conditions agreement was subject to verification by the Audit Commission to establish that intended benefits from the national changes were being delivered locally at key stages. Using the Audit Commission's national methodology we concluded that the Authority has made REASONABLE progress with its overall modernisation agenda between January and July 2004.

We found strong evidence of either compliance with guidance or progress on delivery which reflects a good response in many areas of modernisation. In particular, the Authority has a challenging IRMP and has made progress on a number of projects in line with set timescales.

The Authority will be subject to a comprehensive performance assessment (CPA) in April 2005, which will be key to driving forward the modernising agenda.

### Performance

The Authority has developed performance management arrangements this year and performance has improved in a number of key areas. To build on progress made we have

identified further improvements to help to ensure all staff are signed up to the corporate aims and to tighten controls over monitoring and delivery of key projects. There is also scope to develop a more robust approach to follow up audit recommendations. We will continue to track progress in 2005.

### The accounts

We issued an unqualified opinion on the accounts on 22 November 2004. The Authority is well placed to meet the earlier deadlines for the closure of accounts in 2005 and 2006.

### Financial standing

The Authority has had a good track record on maintaining balances and reserves at an adequate level based on the historical level of spending. Annual budgets are set within a longer term financial plan, which is good practice. However, the Authority faces significant financial pressures due to increased staffing costs due to the national pay agreement and pension costs, which are expected to rise sharply in the next few years. The Authority needs to keep this area under review as part of its medium term financial planning process.

### Action needed by Members

We set out below the specific actions we recommend are taken to further enhance the management of the Authority and the Service:

- support the Director of Finance in continuing to focus on the medium term approach financial planning to ensure adequate balances are maintained
- ensure progress in modernising the service continues and IRMP actions are delivered
- ensure the best value review of the safety training centre is finalised and implemented
- continue to develop performance management arrangements
- improve follow up of recommendations from audit and other external agencies
- ensure the Authority is fully prepared for CPA in 2005.

## Executive Summary

### The purpose of this letter

This is our audit 'Annual Letter' for Members presented by the District Auditor. The letter summarises the conclusions and significant issues arising from our recent audit of the Authority.

We have issued separate reports during the year having completed specific aspects of our programme. These reports are listed at:

- Appendix 1 for information
- Appendix 2 sets out the scope of audit
- Appendix 3 provides information about the fees charged.

## Authority performance

### Modernisation

*The Authority made REASONABLE progress with the overall modernisation agenda between January and July 2004. This indicates that we found strong evidence of either compliance with guidance or progress on delivery which reflects a good response in many areas of modernisation. In particular, the Authority has set a challenging integrated risk management plan (IRMP) and has made progress on a number of projects in line with target timescales.*

The national agreement on fire service pay and conditions included a stipulation that the pay awards at stages 2 and 3 were subject to verification by the Audit Commission. Our work was designed to establish that the intended benefits from the national changes, as set out in the pay agreement and the subsequent white paper, were being delivered locally. Our review assessed local progress across eight themes in accordance with prescribed guidance and timetables. We did the work in two phases in January and July 2004 and reported the findings at the end of each phase. The Audit Commission has recently published a national report setting

out the results of phase two of the verification work.

In January we assessed the Authority as making SOME progress implementing the national changes. In June we assessed further progress made, focussing on the changes that had taken place since January. We concluded that the Authority had made REASONABLE progress between January and July 2004 with its modernisation agenda. Our key findings are that:

- the Authority set a challenging IRMP and has started to progress a number of actions in line with target timescales
- there is significant emphasis on developing the use of risk analysis and the Service has started to use this to underpin its decision making on operational deployment
- the Authority continues to make progress in implementing the integrated performance development system (IPDS) and plays a key role regionally in the development of assessment centres
- the Authority has clearly set out its vision which reflects the role of a modern fire service and places significant emphasis on community fire safety. Fire deaths and injuries have reduced since the inception of in the local home fire risk assessment programme in 1999. The Authority continues to work well in this area with almost 27,000 home fire risk assessments carried out in 2003/04
- the Authority has continued to develop its partnerships and create new projects to support its vision and a significant amount of preventative work undertaken through partnership approaches
- progress in other areas has been slower but the Authority is committed to addressing these areas including duty systems and part-time working. Historically staffing in Merseyside has been on a full time basis but the Authority has a number of specific proposals which will require alternative duty systems and more flexible working arrangements.

Our overall findings from each of the themes at phases 1 and 2 are set out below:

Theme	Phase 1 assessment	Phase 2 assessment
IRMP	Some progress	Good progress
Rank to Role	Some progress	Good progress
IPDS	Some progress	Good progress
Overtime	Some progress	Good progress
Duty Systems	Some progress	Some progress
Part-time working	Little or no progress	Some progress
Modernisation Agenda	Some progress	Good progress
Financial Diagnostic	N/A	Some progress

The Authority does not have a formal project management system to support the challenging change agenda it has set itself. However we did not find evidence that the lack of such a process has inhibited progress to date and the Authority has already started to make changes to improve project management.

The Authority now needs to incorporate this large number of changes into its resource planning and to reflect them effectively in its workforce and financial plans. This highlights the need for close working between operational and support departments in delivering actions. This is clearly developing within Merseyside but there is further work to do. We have agreed an action plan with the Authority and we will follow up progress in early 2005. Progress will also be considered as part of the Comprehensive Performance Assessment in April 2005.

### Other performance work

*The Authority has made considerable progress this year in improving its performance management arrangements and performance has improved in a number of key areas. To build on this the Authority needs to improve ownership of corporate aims through a staff appraisal process for all staff and formalise arrangements for monitoring delivery and following up progress. There is also scope to develop a more robust approach to follow up audit recommendations from previous years. We will continue to track progress in 2005.*

### Best Value Performance Plan

We completed our statutory audit of your 2004/05 best value performance plan (BVPP) and issued an unqualified opinion on 22 November 2004. This indicates our general satisfaction that the Authority met its statutory requirements in the preparation of the plan.

The Authority met the statutory deadline to publish a detailed BVPP by 30 June 2004 and the arrangements for producing and publishing the required performance information are satisfactory. We shared our detailed findings with officers during the course of our audit, which resulted in amendments to the website version of the plan, and we also agreed improvements to secure the completeness and accuracy of performance indicators in future years.

### Performance information

The BVPP shows that the Authority's performance on fire safety has improved in some key areas, in particular the number of deaths and injuries in accidental dwelling fires have continued to fall. The Authority has also developed local performance measures, which show more home fire risk assessments are carried out and the number of staff injuries is lower than last year.

### Performance management

The Service has made considerable progress this year in improving arrangements to deliver key objectives and targets as defined in the best value performance plan, service plan and the integrated risk management plan. Most elements of an effective performance management framework are now in place. Following the pilot CPA in November 2003 the Service reduced the number of corporate aims to improve focus. The key development this year was the introduction of station level plans and targets, and the facility to monitor performance at station level.

We have identified areas for further development, in particular we recommend that the Service:

- extends the staff appraisal process to cascade key corporate aims to all staff and managers
- introduces detailed SMART action plans for major projects
- develops a clear process to take action when monitoring indicates that performance targets are not being achieved.

### Early medical retirements

Following our review of planning and control of early medical retirements in September 2002 the Authority has made some improvements in 2004 but has not yet introduced regular reporting to members to improve accountability in this area. The key issues are shown below:

Agreed action	Progress this year	Still to do
Produce a comprehensive ill health retirement policy.	Members approved a policy in January 2004, which follows good practice in most areas.	Extend policy and procedural guidelines to include the appeals process and timescales.
Improve accountability by introducing quarterly reporting on numbers and costs to members.	Reports deferred pending national pay settlement. Officers plan to report numbers and costs for 2003/04 and first half of 2004/05 to Members in December.	Introduce regular reporting to Members on numbers and cost of early retirements.
Improve reporting of performance compared to other authorities to put local performance into context.	No reporting to date. Merseyside figures are low nationally and compared with family group*.	Put local performance in context by comparing performance with other authorities.

*\*Audit Commission analysis of ODPM data for BVPI 15a (% of those eligible for pension scheme taking ill health retirement) 2002/03.*

There is scope for the Authority to be more robust in its approach to help maintain good overall performance in this area compared to

other authorities. We will continue to track progress in 2005.

### Safety Training Centre

In September 2003 we identified considerable scope to improve arrangements for managing performance of the safety training centre (STC). The Service set up a best value review of the STC in April 2004 to respond to our findings and also to take account of the impact of modernisation and regionalisation. A draft report was produced in November and we will review this to ensure that it addresses the issues we raised. Also, since our review, training was identified as an area to be reviewed and progressed at a regional level and Merseyside, as the lead Authority for training, has commissioned an independent review across the region.

Whilst we understand that officers wanted to conduct a comprehensive in-depth review of this important area we remain concerned that the identified improvements have not been implemented over the last twelve months. We urge Members to ensure that the best value and regional reviews are finalised and implemented quickly. We will continue to track progress and assess your arrangements for ensuring that the STC supports delivery of service objectives.

More generally there is scope to improve accountability for progress against key audit recommendations. Last year we reported that officers were developing formal processes to ensure recommendations from external agencies are implemented. However, in our follow up work this year, we have seen no evidence of formal monitoring of progress at a corporate level.

### Working with other inspectorates and regulators

The Audit Commission has agreed a memorandum of understanding with the Office of the Deputy Prime Minister's Fire Service Inspectorate to ensure that effective liaison takes place at a national level. During 2004 there has not been any need to liaise with them in respect of our local audit work.

## Accounts and Governance

*We have given your accounts an unqualified audit opinion.*

*Your overall corporate governance arrangements are satisfactory in most key areas. We will follow up progress on risk management in January 2005.*

### Audit of 2003/04 accounts

*We gave an unqualified opinion on the Authority's accounts on the 22 November 2004.*

The published accounts are an essential means by which the Authority reports its stewardship of the public funds at its disposal and its financial performance in the use of those resources. Members approved the Authority's annual accounts on 12 August 2004.

We worked closely with the Director of Finance and his staff throughout the closedown process. The Authority shared draft accounts with us nearly a month ahead of the national deadline and we finalised the audit to meet the new earlier deadline of 30 November. The tighter national deadlines will become increasingly difficult to achieve over the next two years and will require earlier planning. We will continue to work closely with officers over the coming months to ensure earlier deadlines for 2004/05 accounts (31 July for production and 31 October for audit) are met.

### Report to those with responsibility for governance in the authority

We are required by professional standards to report to those charged with governance certain significant matters before we give an opinion on the financial statements. We are pleased to say there were no significant issues that we needed to discuss with members this year before issuing our opinion and this was confirmed in a letter to members of the Policy and Finance Committee on 22 November 2004.

## Financial standing

*The Authority has had a good track record on maintaining balances and reserves at an adequate level based on the historical level of spending. Annual budgets are set within a longer term financial plan, which is good practice. However, the Authority faces significant financial pressures due to increased staffing costs following the national pay agreement and pension costs, which are expected to rise sharply in the next few years. The 2004/05 revenue budget has been set to cover anticipated pension costs and there is scope to apply the pensions reserve to smooth the cost of pension lump sum payments if required. The Authority needs to keep this area under review as part of its medium term financial planning process.*

The Authority is required to put in place proper arrangements to ensure that financial standing is soundly based. We are required to consider your arrangements for managing financial performance, the Authority's ability to meet known obligations and your ability to respond to developments.

The Authority has maintained sound control over its resources, with good arrangements to identify financial risks and keep Members appropriately informed of progress. The Authority has a five year financial plan 2004/05 to 2008/09, which includes targets for council tax increases of less than 4% and savings plans. This provides a good framework to identify and respond to financial pressures as they arise.

### 2003/04 outturn

The Authority's gross expenditure for 2003/04 was £69.1million, which was £746,000 less than the revised budget figure. The under spend, which was attributed to savings and additional grant income, meant that the Authority was able to increase the level of reserves as set out below:

Reserve	31 March 2003	31 March 2004	Comments
Earmarked pensions	£4.1m	£4.6m	To meet expected fluctuations in pensions costs, in particular peaks in lump sum payments in 04/05 and 08/09 due to recruitment drives in the mid 1970s.
Earmarked other	£2m	£2m	Includes: <ul style="list-style-type: none"> <li>£0.8m for capital programme</li> <li>£0.4m for modernisation costs.</li> </ul>
General revenue	£2.5m	£2.6m	
Total	£8.6m	£9.2m	

The General Reserve year end balance of £2.6m is approximately 4% of total expenditure in 2003/04. This represents a prudent level of reserves in relation to the Authority's overall spending.

#### 2004/05 current position

The Authority's revenue budget for 2004/05 is £73.6m which would require a £0.2m contribution from reserves. The Authority has identified its main financial pressures for 2004/05 and future years as:

- increasing pension costs, and an expected a peak in the number of officers retiring from 2004/05 onwards following recruitment drives in the 1970s
- a lower than anticipated grant allocation for 2004/05 and uncertainty about future levels of funding
- making the firefighters pay award self financing
- implementing the IRMP.

The pension scheme for uniformed personnel is unfunded and the Authority is required to meet pension and lump sum costs from revenue resources. The Authority has budgeted for anticipated pension costs in the 2004/05 revenue budget, including £3 million to fund expected lump sum payments. If lump sums exceed this amount the Authority will apply the

earmarked pensions reserve (£4.6 million at 31 March 2004) to smooth the cost of lump sum payments as required.

The Authority has always adopted a prudent approach towards financial management and it is important over the coming months that this is maintained to ensure that overall financial health remains sound.

#### 2005/06 and beyond

Looking ahead, the Authority recently received its funding allocation for the 2005/06 financial year. This represents a 2.6% increase, which is less than anticipated in the Authority's medium term financial plan.

The financial pressures due to the need to make the pay award self financing, the tight financial settlement for 2005/06 and the need to resource improvements to the service through the IRMP, mean that members face difficult choices over the coming months in meeting their targets for council tax increases and ensuring effective fire services are maintained. Members will need to support the Director of Finance in continuing to focus on a medium term approach to financial planning which ensures adequate balances are maintained, particularly to meet the cost of a further expected peak in the numbers of firefighters reaching retirement age from 2008.

#### Systems of internal financial control

*We have not identified any significant weaknesses in the overall control framework. We will follow up progress on non operational risk management in January 2005.*

Last year we reported that the Authority needed to make more progress to develop risk management arrangements for all key financial and operational risks.

This year the Authority has made significant progress in identifying and addressing operational risks through the development of an integrated risk management plan. However risk management is less developed in terms of corporate arrangements. We will undertake a more detailed assessment of the Authority's ongoing work on non operational risk management in January 2005 as part of our auditor assessment for the CPA.

## Standards of financial conduct and the prevention and detection of fraud and corruption

*We have not identified any significant weaknesses in your arrangements for monitoring standards of financial conduct or the prevention and detection of fraud and corruption.*

The Authority has taken a positive approach to ensuring proper financial conduct and the prevention and detection of fraud and corruption. The Authority has a good track record of developing policies and procedures to implement new requirements in a timely manner.

### National Fraud Initiative

The Authority is taking part in the Audit Commission's national fraud initiative (NFI) 2004. The NFI, which is undertaken every two years, brings together data from local authorities, NHS bodies, government departments and other agencies, to detect a wide range of frauds against the public sector. Total national savings from the 2002/03 exercise exceeded £83m.

## Legality of transactions

*We have not identified any significant weaknesses in the framework established by the Authority for ensuring the legality of its significant financial transactions.*

We reviewed the arrangements that the Authority have put in place to ensure legality of financial transactions and we did not identify any weaknesses. The Director of Legal Services continues to be proactive in assessing implications of new legislation and assessing the legality of decisions taken by the Authority. We are kept adequately informed of any significant

issues concerning legality and there are currently no matters that we wish to bring to the attention of Members.

## Looking Forward

### Future audit work

We have an agreed plan for 2004/05 and we have reported in this letter those aspects that have already been completed. We have recently completed a review of ICT arrangements and expect to finalise our report with officers in January. This and the remaining elements of that plan, including our audit of the 2004/05 accounts, will be reported in next year's Annual Letter. We have sought to ensure, wherever possible, that our work relates to the key priorities of the Authority.

We will continue with this approach when planning our programme of work for 2005/06. We will seek to reconsider, with you, your key priorities and your own analysis, and develop an agreed programme by 31 March 2005. We will continue to review our planned work in the light of the Comprehensive Performance Assessment in April 2005.

## Comprehensive Performance Assessment (CPA)

As part of the Government's improvement agenda CPA is being extended from local government to the fire service in 2005. Merseyside was a CPA test site for the pilot methodology in November 2003. All fire authorities will be subject to CPA in the next 12 months. CPA in Merseyside will take place in April 2005. As part of the process we will liaise with your officers to complete an auditor assessment by 7 March 2005. The Authority's performance will be assessed in one of five categories (poor, weak, fair, good or excellent) and an action plan will be produced which will be key to driving forward the modernisation agenda.

## Revision to the Code of Audit Practice

The Audit Commission has consulted on a revised Code of Audit Practice for application to the audit of the 2005/06 accounts. The new Code, which will be laid before Parliament in January 2005, is designed to secure:

- a more streamlined audit, which is proportionate to risk and targeted on areas where auditors have most to contribute to improvement
- a stronger emphasis on value for money, focussing on bodies' corporate performance and financial management arrangements
- clearer reporting of the results of audits.

Further details will be provided in the Audit Plan for 2005/06.

## Closing remarks

This letter has been discussed and agreed with Corporate Leadership team on 14 December 2004. A copy of the letter will be presented to the Authority on 10 January 2005.

The Authority and the Service have taken a positive and constructive approach to our audit and I would like to take this opportunity to express my appreciation for your assistance and co-operation – particularly from staff involved in our verification work this year.

## Availability of this letter

This letter will be published on the Audit Commission's website at [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk), and also on the Authority's website.



**Judith Tench**  
District Auditor

**Date 22 December 2004**

## Status of our reports to the Authority

Our annual audit letter is prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. Annual audit letters are prepared by appointed auditors and addressed to members and officers. They are prepared for the sole use of the audited body, and no responsibility is taken by the Audit Commission or its appointed auditors to any member or officer in their individual capacity, or to any third party.

## Audit reports issued

Audit plan	March 2003*
Fire verification phase 1	February 2004
Fire verification phase 2	July 2004
Audit opinion on 2003/04 accounts	November 2004
SAS610 letter	November 2004
Best Value statutory report	November 2004
Best Value detailed report	November 2004

\* Covered two audit years 2002/03 and 2003/04

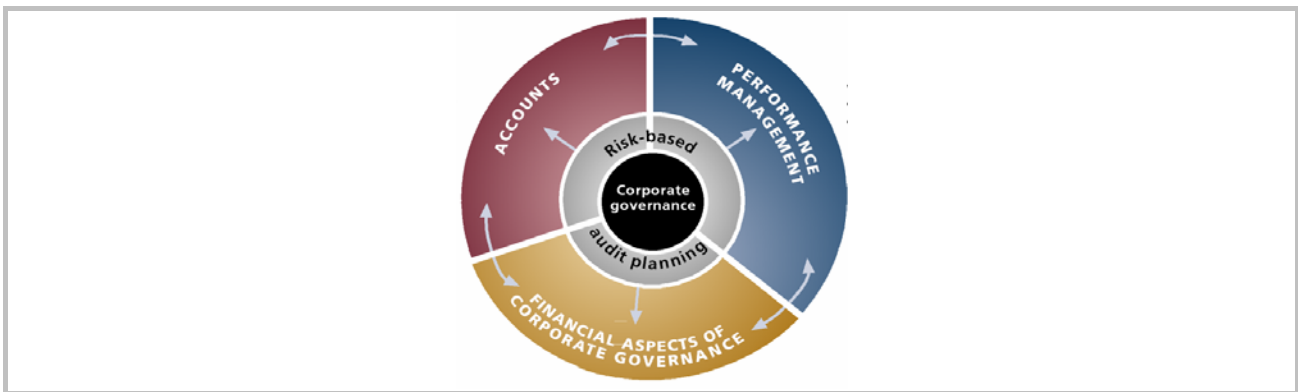
## Scope of the audit

### Audit

Our main objective as your appointed auditor is to plan and carry out an audit that meets the requirements of the Code of Audit Practice. We adopt a risk-based approach to planning our audit, and our audit work has focused on your significant financial and operational risks that are relevant to our audit responsibilities.

Central to our audit are your corporate governance arrangements. Our audit is then structured around the three elements of our responsibilities as set out in the Code and shown in Exhibit 1.

#### The three main elements of our audit objectives



#### Accounts

- Opinion.

#### Financial aspects of corporate governance

- Financial standing.
- Systems of internal financial control.
- Standards of financial conduct & the prevention and detection of fraud and corruption.
- Legality of transactions.

#### Performance management

- Use of resources.
- Performance information.
- Best Value Performance Plan.

The Audit Commission has circulated to all audited bodies a statement that summarises the key responsibilities of auditors. Our audit has been conducted in accordance with the principles set out in that statement. What we say about the results of our audit should be viewed in the context of that more formal background.

## Audit fee update

Audit area	Plan 2003/04 £	Actual 2003/04 £
Accounts	11,700	11,700
Financial aspects of corporate governance	19,258	22,870
Performance	28,612	25,000
<b>TOTAL CODE OF AUDIT PRACTICE FEE</b>	<b>59,570</b>	<b>59,570</b>
Grant Claim certification	-	400
Additional voluntary work (under Section 35)	nil	nil