

Government and Public Sector

October 2005

Cheshire Police Authority

2004/05 Audit Letter

The Members
Cheshire Police Authority
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October 2005

Ladies and Gentlemen,

Audit and Inspection Letter 2004/05

We are pleased to present our Audit Letter for 2004/05. We hope that the information contained in this report provides a useful source of reference for Members. The Best Value and Audit Committee will be considering this Letter on 11th October 2005.

Yours faithfully

PricewaterhouseCoopers LLP

Enclosure

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Code of Audit Practice and Statement of Responsibilities of Auditors and of Audited Bodies

We perform our audit in accordance with the Audit Commission’s Code of Audit Practice (the Code), which was issued in March 2002. This is supported by the Statement of Responsibilities of Auditors and Audited Bodies, which was issued in April 2000. Both documents are available from the Chief Executive of each audited body. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end, and what is to be expected of the audited body in certain areas. Our reports and audit letters are prepared in the context of this statement and in accordance with the Code.

Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body, and no responsibility is taken by auditors to any Member or officer in their individual capacity, or to any third party. A new Code of Audit Practice will be in place for the 2005/06 audit year, together with a new Statement of Responsibilities of Auditors and Audited Bodies, both of which were issued in March 2005.

Executive summary

The purpose of this Letter

We write to you each year, usually on completion of our audit, to summarise the more important issues that we wish to bring to your attention.

Under the new Code of Audit Practice which will be in effect for 2005/06, we are encouraged to report our main audit findings as soon as possible after the completion of the audit. We aim to report our Annual Audit Letter to you at the same time as we clear the accounts to ensure that it is timely.

This letter will therefore include the issues we wish to report to you arising from all aspects of our audit programme of work we are formally required to report to you under Statement of Auditing Standard (SAS) 610 - "Communication of audit matters to those charged with governance".

Our audit work during the year was performed in accordance with the plan that we presented to you on 4 May 2004. We have issued a number of reports during the audit year, detailing the findings from our work and making recommendations for improvement, where appropriate. A list of these reports is included at Appendix A to this letter.

Accounts

In 2004/2005 the Authority's reserves were reduced by £3.8m, as recorded in the accounts. Having audited this year's financial statements, we will shortly be issuing an unqualified audit opinion on the financial statements.

The reduction in reserves is part of the longer term financial pressure faced by the Authority, is still forecasting deficits in its Medium Term Finance Strategy for 2006/07 to 2009/10, and must also meet efficiency savings

targets set by the Home Office. The Authority continues to actively identify options to reduce the significant projected deficit and to meet its savings targets over this period.

The Authority struggled to meet the accounts closedown programme it had set itself in 2004/05, with a number of statements in the accounts being delayed partly due to the implementation of a new financial system.

The Authority will need to review its closedown process to meet the 2005/06 deadlines.

Use of resources

We undertook a high level review of the resource management data used by the Authority to identify whether it was sufficiently robust to support the necessary improvements in resource management and productivity required to achieve efficiency targets.

Our preliminary conclusions identified that whilst much good practice exists at the Authority, further enhancements could be made based on the experience of other constabularies. The report from this work is currently at a draft stage and will be presented to the Authority upon completion.

We will discuss the issues contained within this Letter with the Best Value and Audit Committee on October 11th 2005.

Accounts and Governance

We comment on the following key areas in this section:

- accounts;
- financial standing;
- accounting issues;
- systems of internal financial control;
- standards of financial conduct and the prevention and detection of fraud and corruption; and
- legality of transactions.

Accounts

The purpose of our accounts work was to perform an audit of the final accounts of the Authority, in accordance with approved Auditing Standards.

In 2004/05 the Authority showed an overall reduction in its reserves of £3.8m in the annual accounts, this reduced balances to £6.2m at the year end. The reduction in reserves was attributable to an overspend on Pensions costs of £0.9m, a contribution to capital expenditure of £3.0m and a contribution to the revenue budget of £0.4m which was offset by an underspend on the Constabulary of £0.5m. Having audited the accounts, we are pleased to

report we will shortly be issuing an unqualified audit opinion on the financial statements.

In addition to the reduction in its 2004/05 balances, the Authority continues to face financial pressures due to deficits forecast in its Medium Term Strategy. The main contributing factors to this deficit are the insufficiency of government grant funding and the Home Office limiting the Authority's ability to reduce police officer numbers and therefore the Authority has to identify savings through other cuts to its services. As part of this Strategy a number of measures have been identified to reduce the forecast deficit and the Authority continue to make progress in this area.

To meet the challenges posed by the Medium Term Strategy the Authority undertook a radical restructuring at the beginning of 2005/06 through its Taking Control programme.

The effects of the Taking Control restructuring will need to be closely monitored during 2005/06 to ensure the anticipated results are achieved and its financial impact managed.

The Authority also faces a challenge to closedown the accounts in 2005/06 due to the new accounts approval deadlines (30 June) for 2005/06. Whilst the 2004/05 accounts were prepared in draft form by the beginning of the audit there were a number of statements unavailable for audit. This was partly due to staff being occupied by the requirement to implement a new financial system, which should not be an issue for the preparation of the 2005/06 accounts.

During the year we reported a number of minor control weaknesses, however we were pleased to note that we had no significant internal control issues identified and we issued an unqualified audit report.

Accounting issues

- **New Financial System**

The Authority introduced a new financial system in February 2005. In addition to work completed by Internal Audit we completed a review of the implementation of the financial system and the transfer of data between systems.

We are pleased to report that the results of this work did not raise any significant concerns about the system and we were able to rely on the system for our final accounts work.

Early closing

The Authority employed an effective closure of accounts process which facilitated good progress against the targets for 2004/05 considering a new financial system was implemented in February 2005. However, a full set of financial statements was not ready for the beginning of the audit as delays were experienced in obtaining the Statement of Internal Control, Best Value Accounting Code of Practice analysis and the Cashflow Statement. The accounts were approved by the Closure of Accounts Committee on 26th July 2005 and the Statement of Internal Control at the Policy and Finance meeting on 13th September 2005.

The accounts deadline dates will move forward again in 2005/06, placing further demands on the Authority in terms of completeness and accuracy of early information which will need to be taken into account when planning the 2005/06 process.

The Authority should review its process for the closure of accounts to ensure it meets its deadlines.

Pension fund valuation

The Authority has received confirmation from the Cheshire Pension Fund administrators, who operate the Local Government Pension scheme for Cheshire Police's administration staff, of employer's contribution rates from 2005/06 which will be 15%, as a result of the need to recover the deficit on the Fund over 20 years.

For the Police Pension Scheme is an unfunded scheme which means it is financed to pay pensions as the liability arises. The Authority reviews the financial impact of Police Pensions as part of its Medium Term Strategy. We have commented on the MTS in the Financial Standing section of this report.

Following our SAS610 report to the Best Value and Audit Committee an issue came to our attention regarding the FRS17 entries made the CPA.

The funds were valued by actuaries who provided the FRS17 accounting entries, which CPA included in its accounts. A technical error was subsequently identified in the information provided by the actuaries which affected the Local Government bodies which used the same actuary.

The error has no impact on the figures reported in the Balance Sheet with only the movement being misallocated. There are also no resource implications for the authority and therefore no impact on council tax.

For CPA the effect was a misstatement of £8.7m for the Police Pension fund and £0.8m for the Local Government Pension Scheme which totals £9.5m. The pensions interest cost and the STRGL/Statement of movements in reserves are affected.

We currently do not consider that this adjustment will be needed to the accounts.

Financial standing

In this section we comment upon the Authority's general financial standing taking into account both its performance during the last year and its ability to meet known financial obligations.

• Overall financial performance in 2004/05

The Police Authority revised net revenue budget was £153.3m for 2004/05 and the final revenue outturn for 2004/05 was an overspend of approximately £0.5m, representing 0.28% of the revised budget. In achieving this result there were some over and underspends to the budget which were the result of :

- Overspends of £0.4m on police pay and allowances and an overspend on the police pensions budget of £0.9m (mainly due to death gratuities of £0.3m and commutations for officers taking early retirement earlier than expected of £0.4m). These overspends were netted off by underspent constabulary budgets and additional income to bring the final figure to £0.5m.

Capital expenditure in 2004/05 amounted to £10.1m (excluding a provision for £10.8m for schemes due to slip into 2005/06), compared with £11.2m expenditure and £9.7m in the previous year.

• Efficiency Savings

The Home Office set a target of 2% efficiency savings in 2004/05 which equated to £3.1m for Cheshire Police. Our work on the budget verified that the Authority had accounted for the efficiency savings in its budget.

By the year-end the Constabulary achieved cashable savings of £1.6m and non-cashable efficiency savings of £2.5m, £1.1m more than required. The cashable savings were mainly achieved through reductions in the rates payable on police properties and by increasing the police staff vacancy factor by 2%.

• Balances and reserves

The Authority holds reserves and balances for both revenue and capital expenditure. Whilst some are earmarked for specific expenditure there is also a general reserve that provides a working balance to allow for the impact of fluctuations in expenditure and income from year to year, and for major unforeseen expenditure outside the control of the Authority.

The level of general reserves as at 31 March 2005 stood at £6.2m, which represents approximately 4% of the net cost of service. Reserves reduced from £10m in 2004/05 due to the overspend on Police Pensions of £0.9m and contributions to capital expenditure.

CIPFA issued revised guidance on reserves and balances during early 2003 (LAAP Bulletin 55 – Guidance note on Local Authority reserves and balances). Within the guidance CIPFA consider it inappropriate to give prescriptive guidance on the minimum or maximum level of reserves required, either as an absolute amount or as a percentage of budget. The guidance states that in order to assess the adequacy of reserves consideration should be given to the strategic, operational and financial risks facing the Authority set in the context of its medium term financial strategy.

As external auditors we have a responsibility to review the arrangements in place to ensure that the Authority's financial standing is soundly based. Given the considerable change programme the Authority is experiencing we do not consider the level to be unreasonable.

• The 2005/06 financial year and outlook

A net revenue budget of £163.8m was set for 2005/06, and currently a small net underspend is forecast although this position will continue to be closely monitored throughout the financial year.

Over the longer term the Authority has updated its Medium Term Financial Scenario. The work completed over the past year has led to the forecast deficit being refined to a total of £10m over the period 2006/07 to 2009/10. This is mainly caused by the £7.5m of efficiency savings the Authority needs to make due to the restrictions on reducing officer numbers.

Were the Authority to achieve these savings, the overall longer term deficit would be nearer £2.5m. The Authority continues to consider a number of options to reduce the projected deficit position, although the future of the Authority over this period will also be subject to the current review of Police forces being undertaken by the Home Office.

As part of its process to improve its performance, the Constabulary implemented a radical restructuring of its operations with effect from 1 April 2005, following its Taking Control review. This created 18 Neighbourhood Policing Units which concentrate on preventing and detecting local crime and building contacts with the local community. The restructuring also created 3 geographical areas within the Constabulary within which specialist units concentrate serious crime, demand management, public protection, intelligence, pro active policing, partnerships and custody investigation teams. Headquarters based teams deliver the major investigations, roads policing, crime recording, contingency planning, specialized support for crime areas eg drugs and Hi tech crimes and the administrative functions of the Authority.

The Custody Suite PFI project also comes into effect in 2005/06. This reduces the number of custody suite in the county to three, with anticipated financial and operations improvements expected to come out of the project.

This is a demanding agenda for the Authority, if it is to deliver against its targets, its local priorities and expectations of the public. Against this backdrop the importance of maintaining financial stability in the 2005/06 and future financial years cannot be underestimated.

Prudential Framework for Capital Expenditure

From 1 April 2004, the Authority has been able to plan its capital expenditure under the new Prudential Framework, which focuses on its ability to afford the consequences of spending decisions from future years' revenue accounts and allows it to set its own limits on the borrowing needed to achieve an affordable capital strategy.

We have reviewed the steps the Authority took in 2004/05 to implement the Prudential Framework and manage the Authority's spending and borrowing in

the second year of operation, including the processes for reviewing limits and indicators under the CIPFA Prudential Code and determining the prudence and affordability of any prudential borrowing undertaken. We were satisfied with the progress being made.

The estimates of net external borrowing for the next three years are as follows (brackets indicate investments exceed borrowing) –

- 2005/2006 – (3.0m)
- 2006/2007 – (4.3m)
- 2007/2008 – (1.8m)

Control issues

There were no significant controls issues, identified during the audit, to report. We made minor recommendations in our 2004/05 interim report and SAS 610 reports:

Systems of internal financial control

It is the responsibility of the Authority to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility, as auditors, is to consider whether the Authority has met its responsibility to establish systems of internal financial control that are both adequate and effective in practice.

We have reported our conclusions on the our review of systems of internal financial control to the Best Value and Audit Committee. This also included the results of our review of computer controls where we concluded that the operation of the Authority's systems was sufficient to support our planned audit approach.

We were pleased with the level of internal control in place considering the changes experienced by the Authority during the year.

Statement of internal control

The Accounts and Audit Regulations 2003 included a requirement that the statement of accounts prepared by an authority in England should contain a statement on internal control (SIC). These statements refer to much wider systems of control than purely financial systems and require the Authority to have in place such systems of control. Authorities are required to conduct annual reviews of the effectiveness of the system of internal control, which will provide the findings to support the SIC.

We reviewed the SIC for 2004/05 and found that it had been compiled in accordance with recommended practice and we agreed with the key issues raised in the SIC with respect to the constabulary's sickness levels and failing to meet its call management target of 90% (actual 81.2%)

Going forward into 2005/06 the Constabulary implemented a radical restructuring of its operations at the beginning of the year, following the Taking Control review. The Authority need to take care that this restructuring does not impact on its controls during 2005/06.

Internal Audit

We experienced delays from Internal Audit in producing their work upon which we would place reliance for the final accounts audit. The delay led to certain sections of the work being dropped with regards to debtors and additional work being undertaken at our year-end audit.

We do, however, recognise that the delay in the work was caused by Internal Audit staff, working for Cheshire Police, being committed to working on audits of Estates and the Premises Improvement Fund as requested by the Best Value and Audit Committee.

We reviewed the work completed by Internal Audit and were satisfied with the conclusions drawn from the work, which were reported to the Best Value and Audit Committee.

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

The prime responsibility for the prevention and detection of fraud and irregularities rests with the Authority's management. It is the responsibility of the Authority to ensure that its affairs are managed in accordance with proper standards of financial conduct and to prevent and detect fraud and corruption. It is our responsibility to consider whether the Authority has put in place adequate arrangements to maintain proper standards of financial conduct and to prevent and detect fraud and corruption. It is not the auditors function to prevent or detect breaches of proper standards and our work does not remove the possibility that fraud or corruption has occurred and remained undetected.

Our work in respect of the standards of financial conduct and the prevention and detection of fraud and corruption focussed on an assessment of the control environment at the Authority and the monitoring controls in operation designed to prevent and detect fraud and corruption.

In order to meet our Code objective we:

- reviewed the arrangements in place within the Authority for ensuring proper standards of financial conduct and for preventing and detecting fraud and corruption;
- reviewed the local applicability of relevant national issues; and
- have taken account of advice issued by the Audit Commission.

There are no issues which we wish to draw to your attention in relation to this area.

The legality of financial transactions

In order to meet our objectives in this area, we have:

- reviewed the arrangements in place within the Authority for ensuring the legality of financial transactions;
- reviewed the minutes of the Authority and relevant Committees;
- discussed key issues and concerns with management;
- had regard to the Authority's implementation of significant new legislation/statutory requirements;
- reviewed the local applicability of relevant national issues;
- taken account of advice issued by the Audit Commission; and
- had regard to matters coming to the auditor's attention where legality, losses or deficiencies may be an issue.

There are no issues which we wish to draw to your attention in relation to this area.

Performance management

Resource Management Data

As a result of the Gershon Efficiency Review, the Authority is seeking efficiency savings of £4.5 million per year. Eighty-two per cent of the Authority's funds are expended on human resources, the majority on front line policing. The Authority has identified the need for effective resource management to achieve increases in productivity. The Authority has processes for collating crime management and incident related data available but it doubts whether it has sufficiently robust management information to support the necessary improvements in resource management and productivity.

The scope of our review extended to:

- determining the approach and types of data required to assess productivity of front line services;
- determining the data the Authority currently has; and
- providing a gap analysis of the difference between the two.

This was a high-level overview of the Authority's needs, capacity and requirements. It is currently at the draft report stage. We outline below its main conclusions.

The Authority requires data which indicates the level of resources required at

any time. For this it needs data on the numbers of different types of incident and the resources required on average to deal with them. It also needs an analysis of current productivity of individual police officers, Basic Command Units and Areas.

Under the Taking Control initiative the Authority undertook the analysis of data concerning 3,500 incidents in respect of the responses they received and the difference this made in bringing them to a successful conclusion. Based upon this analysis, it was able to reorganise its resources. It now deploys half as many officers to give immediate responses to incidents, which are graded Urgent or Routine and prioritised accordingly. The remaining officers are deployed to deal with the workload more effectively by:

- following up incidents on an appointment basis or by desk-based staff;
- in community policing; and
- in specialist units.

However, further improvements must come from increasing the productivity of individual police officers. The Authority uses data to allocate officers on duty to meet the demand expected at different times of the day and days of the week. From October 2005 an Automatic Vehicle Location System will allow the Authority to know the geographical position of police vehicles and their proximity to likely incidents. The challenge at that time will be to combine this technology with data on the location of incidents for the purpose of positioning police vehicles at locations appropriate to minimising response times.

We visited Lancashire Constabulary to evaluate the work done there with the Airwave communication technology. Cheshire Police has Airwave but Lancashire is piloting its extended use with status messaging to be able to track the use of their human resources. We found that this allows Lancashire to produce useful data on the productivity of its five policing areas and on individual police officers. It is hoped to be able to analyse the data by Division in the future.

Meanwhile the data is being used to address performance issues related, for example, to the excessive amounts of time spent in the police station or attending incidents at the end of shifts to engineer increased overtime. In this way it can be used to increase the time police spend outside the police station, giving greater visibility and assurance to the public.

However, this development of Airwave cannot be used to determine the amount of time a particular type of incident should take. All incidents vary in their nature and complexity. Consequently, even two incidents of the same type might legitimately take very different amounts of time. This means that it cannot be used as a tool to determine which individual police officers are more or less efficient than are others. Consequently, it cannot be used in this way to identify centres of good practice to spread to others.

Best Value

Under the Local Government Act 1999 we are required to carry out an audit of the Council's Best Value Performance Plan (BVPP). We issued an unqualified opinion with respect to our audit work in relation to the BVPP issued in June 2004.

2003/04 work

In 2003/04 we completed the Audit Commission's mandated studies on Data Quality and Activity Based Costing. These studies are subject to follow up work being completed by the Audit Commission which will be reported to you in due course.

Audit plans and fees update for 2004/05

Audit Plan 2004/05

We issued our Audit Plan for 2004/05 and presented it to the Audit Committee in May 2004.

We have performed appropriate reporting procedures for each of the risks identified in our Audit Plan of 2004/05. We use this Audit Letter to comment only on those areas where we believe we need to communicate these with those charged with governance.

Fees update for 2004/05

We reported our fee proposals as part of the Audit Plan for 2004/05, which we presented to the Audit Committee in May 2004. These fee proposals covered the audit year 2004/05.

Our actual fees were in line with our proposals.

Appendix A: Audit reports issued in relation to the 2004/05 financial year

- *Performance reports for work carried out in 2004/05*
- *Internal control report – as part of progress report*
- *Audit opinion for 2004/05 financial statements*

Appendix B: Summary of recommendations contained in this letter

Page	Recommendation	Management Response
5	The effects of the Taking Control restructuring will need to be closely monitored during 2005/06 to ensure the anticipated results are achieved and its financial impact managed.	Agreed
6	The Authority should review its process for the closure of accounts to ensure it meets its deadlines	Agreed

In the event that, pursuant to a request which Cheshire Police Authority has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PwC promptly and consult with PwC prior to disclosing such report. Cheshire Police Authority agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Cheshire Police Authority shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC, Cheshire Police Authority discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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