KPMG

External Audit ISA260 Report 2017/18

Police and Crime Commissioner for Lincolnshire & Chief Constable for Lincolnshire

July 2018

DRAFT

Summary for Joint Independent Audit Committee

This document summarises the key findings in relation to our 2017/18 external audit at the Police and Crime Commissioner for Lincolnshire ('the PCC') and the Chief Constable for Lincolnshire ('the CC').

This report covers both our on-site work which was completed in February and June 2018 on the PCC and CC's significant risk areas, as well as other areas of your financial statements, and the control environment in place to support the production of timely and accurate financial statements.

Organisational and IT control environment	We consider that your organisational and IT control environments are effective overall.
Controls over key financial systems	Based on our work we have determined that the controls over all of the key financial systems are sound.
Accounts production	We consider that the overall process for the preparation of your financial statements is adequate. We also consider the PCC and CC's accounting practices appropriate.
Financial statements	**Subject to all outstanding queries being resolved to our satisfaction and for the necessary assurances being received from the auditors of the LGPS pension scheme we anticipate issuing an unqualified audit opinion on the PCC and CC's financial statements before the deadline of 31 July 2018.** Based upon our initial assessment of risks to the financial statements (as reporting to you in our *External Audit Plan 2017/18* and updated during our audit) we identified the following significant risk (excluding those mandated by International Standards on Auditing – see Page 10): — **Pensions Liabilities** – The valuation of the Police and Crime Commissioner and Chief Constable's pension liabilities, as calculated by the Actuary, are dependent upon both the accuracy and completeness of the data provided and the assumptions adopted. The importance over such data is increased in a year when a triennial revaluation is required, as is the case for 2017/18 in respect of the Police Pension Scheme. We have identified two audit adjustments impacting the primary statements with a total value of £3 million, a further two errors in disclosure with a total value of £18 million and a number of presentational issues. See Page 14 for details. These adjustments result in a no movement in the reported deficits on provision of services. Based on our work, we have raised a single recommendation. Details of our recommendation can be found in Appendix 1. We are now in the completion stage of the audit and anticipate issuing our completion certificate and Annual Audit Letter by the end of August 2018.

Summary for Joint Independent Audit Committee (cont.)

Value for money arrangements

We have completed our risk-based work to consider whether in all significant respects the PCC and CC have proper arrangements to ensure they have taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the PCC and CC have made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money opinion.

We set out our assessment of those areas requiring additional risk based work in our *External Audit Plan 2017/18* and have updated this assessment during our interim visit. As a result of this we have identified the following significant VFM audit risk:

— **Medium Term Financial Planning** – The Police and Crime Commissioner and Chief Constable continue to face significant financial pressures and uncertainties in relation to their future funding levels with grant allocations for future years not yet being published. The Police and Crime Commissioner and Chief Constable need to have effective arrangements in place for managing their annual budgets, generating income and identifying and implementing any savings required to balance their medium term financial plan.

See further details on Page 20.

Exercising of audit powers

We have a duty to consider whether to issue a report in the public interest about something we believe the PCC or CC should consider, or if the public should know about.

We have not identified any matters that would require us to issue a public interest report.

In addition, we have not had to exercise any other audit powers under the Local Audit & Accountability Act 2014.

Acknowledgements

We would like to take this opportunity to thank officers for their continuing help.

Section one

Control Environment

Organisational and IT control environment

We have identified no significant issues with the PCC and CC's organisational and IT control environments and consider that the overall arrangements that have been put in place are reasonable.

Work completed

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit. We obtain an understanding of the PCC and CC's overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

The PCC and CC rely on information technology ("IT") to support both financial reporting and internal control processes. In order to satisfy ourselves that we can rely on the use of IT, we seek to gain an overall understanding over the PCC and CC's IT control environment with the aim of identifying those IT related controls where we may wish to seek assurance over their design and implementation as part of our controls related work.

Key findings

We consider that your organisational and IT control environments are effective overall.

Aspect of controls	Assessment
Organisational controls:	
Management's philosophy and operating style	3
Culture of honesty and ethical behaviour	3
Oversight by those charged with governance	3
Risk assessment process	3
Communications	3
Monitoring of controls	3
IT controls:	
Access to systems and data	3
System changes and maintenance	3
Development of new systems and applications	3
Computer operations and end-user computing	3

Key	
1	Significant gaps in the control environment.
2	Deficiencies in respect of individual controls
3	Generally sound control environment.

Controls over key financial systems

The controls over all of the key financial systems are sound.

Work completed

We review the outcome of internal audit's work on the financial systems to influence our assessment of the overall control environment, which is a key factor when determining the external audit strategy.

Where we have determined that this is the most efficient audit approach to take, we evaluate the design and implementation of the control and then test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

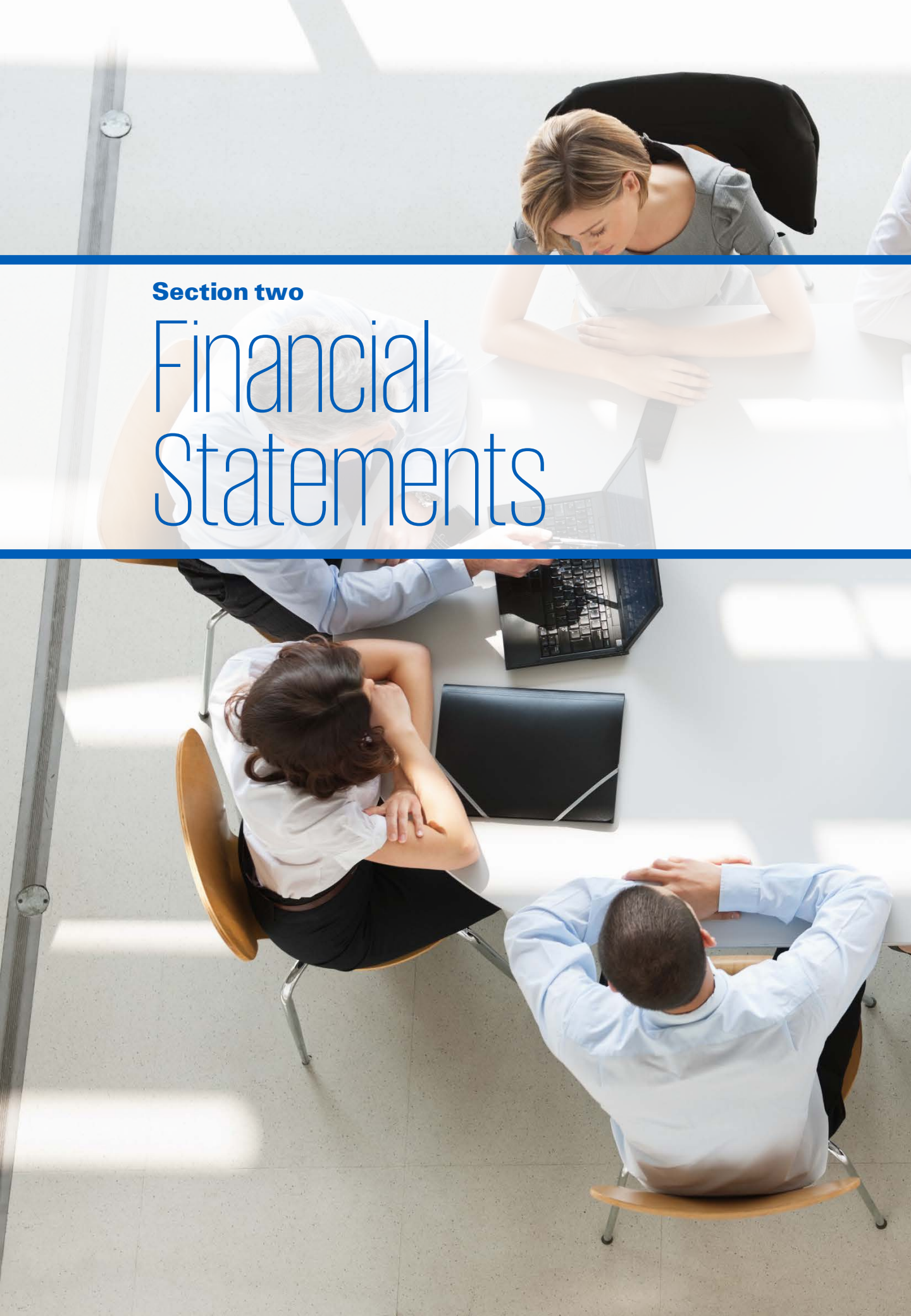
Our assessment of a system will not always be in line with your internal auditors' opinion on that system. This is because we are solely interested in whether our audit risks are mitigated through effective controls, i.e. whether the system is likely to produce materially reliable figures for inclusion in the financial statements.

Key findings

Based on our work, we have determined that the controls over all of the key financial systems are sound.

Aspect of controls	Assessment
Property, Plant and Equipment	3
Cash and Cash Equivalents	3
Pensions	3
Non Pay Expenditure	3
Payroll	3
Regional Collaboration	3

Key	
1	Significant gaps in the control environment
2	Deficiencies in respect of individual controls
3	Generally sound control environment



Section two

Financial Statements

Accounts production and audit process

Audit standards (ISA 260) require us to communicate our views on the significant qualitative aspects of the PCC and CC's accounting practices and financial reporting.

We also assessed the PCC and CC's (the Authority) process for preparing the accounts and its support for an efficient audit. The efficient production of the financial statements and good-quality working papers are critical to meeting the tighter deadlines.

The PCC and CC's overall process for the preparation of the financial statements is adequate, although some slippage has been noted in the quality of the working papers used to support the financial statements.

The Authority has implemented all of the recommendations in our ISA 260 Report 2016/17.

Accounts practices and production process

The PCC and CC have over the past two years implemented a series of incremental changes to their closedown planning processes with the aim of ensuring that the earlier accounts production date could be achieved for the current year. These have been further enhanced in the current year, including a greater level of automation being built into the process and, as part of this, we have actively engaged with officers in the period leading up to the year end in order to proactively address issues as they emerge.

These improvements proved to be effective and we consider that the overall process for the preparation of your financial statements is adequate.

We also consider the PCC and CC's accounting practices appropriate.

Going concern

The financial statements of both the PCC and CC have been prepared on a going concern basis. We confirm that we have identified no significant matters which would, in our view, affect the ability of the PCC or CC to continue as a going concern.

Implementation of recommendations

We raised three recommendations in our ISA 260 Report 2016/17. The PCC and CC has implemented all of the recommendations relating to the financial statements in line with the timescales of the action plan. The table below sets out the PCC and CC's progress against high priority recommendations. Further details are included in Appendix 2.

Issue	Progress
Narrative Report compliance Our review of the PCC and CC's Chief Finance Officer's Narrative Reports identified a number of areas were improvements could be made in order to ensure full compliance with CIPFA's Code of Practice	The format of the PCC and CC Chief Finance Officer's Narrative Reports have been updated to reflect the updated CIPFA guidance for the current year and now incorporate the Code of Practice requirements.

Accounts production and audit process (cont.)

Completeness of draft accounts

We received a complete set of draft accounts on 30 May 2018 which was in advance of the statutory deadline.

Quality of supporting working papers

We issued our Accounts Audit Protocol to the Deputy Chief Finance Officer on 11 January 2018. This important document sets out our audit approach and timetable. It also summarises the working papers and other evidence we require the PCC and CC to provide to support our audit work. This helps the PCC and CC to provide audit evidence in line with our expectations. We worked with management to ensure that working paper requirements are understood and aligned to our expectations

We found some quality issues in relation to the working papers, noting a slight deterioration from those of the previous year. This included:

- Including multiple versions of the same working paper in the audit documentation;
- Failing to update working paper headings to reflect the correct year; and
- Including a number of other working papers within the audit documentation that were either poorly named or poorly referenced as to their purpose.

Whilst this has not caused any significant delays in the audit process it has increased the number of audit queries to officers with the need to check that each working paper provided was in fact the correct final version. There is an opportunity for improvements to be made in providing clear and concise audit trail of underlying transactions. We have raised a recommendation in respect of this, see recommendation 1.

Response to audit queries

We are pleased to report that our agreed turnaround time for dealing with audit queries was achieved by officers in the majority of cases, although in two instances, where evidence was required from staff who are not part of the Finance team, delays were noted. As a result of this, the majority of our audit work was completed within the timescales expected with only a single outstanding query remaining. This achievement puts the PCC and CC in a relatively good position to take on the 2018/19 closedown with no significant concerns.

Specific audit areas

We anticipate issuing an unqualified audit opinion on the PCC and CC's 2017/18 financial statements by 31 July 2018. We will also report that your Annual Governance Statement complies with the guidance issued by CIPFA/SOLACE ('Delivering Good Governance in Local Government') published in April 2016.

For the year ending 31 March 2018, the PCC and CC has reported a group deficit of £46m. Following accounting/funding basis adjustments and reserve transfers there has been no impact on the General Fund balance.

Auditing standards require us to consider two standard risks for all organisations. We consider these as a matter of course in our audit and will have set out the findings arising from our work in our ISA 260 Report below.

01 Management override of controls

Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to this audit.

In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

There are no matters arising from this work that we need to bring to your attention.

02 Fraudulent revenue recognition

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk.

In our *External Audit Plan 2017/18* we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.

Over the following pages we have set out our assessment of the specific significant risk and area of audit focus we identified in relation to the audit of the PCC and CC's financial statements.

Specific audit areas

Significant Audit Risks

Risk:

Pension Liabilities

The net pension liability represents a material element of the Police and Crime Commissioner and Chief Constable's balance sheets.

The valuation of the pension liabilities rely on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the overall valuations.

There are financial assumptions and demographic assumptions used in the calculations of the valuations, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Police and Crime Commissioner and Chief Constable's employees, and should be based on appropriate data, especially so in a year where a triennial revaluation is necessary. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes.

There is a risk that the assumptions and methodologies used in the valuations of the Police and Crime Commissioner and Chief Constable's pension obligations are not reasonable. This could have a material impact to net pension liabilities accounted for in the financial statements.

Our assessment and work undertaken:

As part of our work we reviewed the controls that the PCC and CC has in place over the information sent directly to the Scheme Actuary. We also liaised with the auditors of the Pension Fund in order to gain an understanding of the effectiveness of those controls operated by the Pension Fund. This included consideration of the process and controls with respect to the assumptions used in the valuation. We also evaluated the competency, objectivity and independence of Hymans Robertson, the Scheme Actuary.

We reviewed the appropriateness of the key assumptions included within the valuation, compared them to expected ranges and involved a KPMG Actuary to provide a specialist assessment of those assumptions. We also reviewed the methodology applied in the valuation by Hymans Robertson.

In addition, we reviewed the overall actuarial valuation and considered the disclosure implications in the financial statements.

In order to determine whether the net pension liability has been appropriately accounted for we also considered the valuation of pension assets. We obtained assurance from the Pension Fund auditors (KPMG LLP) over the overall value of fund assets. We then liaised with the actuary to understand how these assets are allocated across participating bodies and re-performed this allocation.

As a result of this work we determined that the PCC and CC's processes for obtaining an actuarial valuation were adequate and that the disclosures in the financial statements were reasonable.

We have set out our view of the assumptions used in valuing pension assets and liabilities at Page 13.

Specific audit areas (cont.)

Other areas of audit focus

Those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

Issue:

Faster Close

In prior years, the Police and Crime Commissioner and Chief Constable have been required to prepare draft financial statements by 30 June and then final signed accounts by 30 September. For years ending on and after 31 March 2018 however, revised deadlines apply which require draft accounts by 31 May and final signed accounts by 31 July.

During 2016/17, the Police and Crime Commissioner and Chief Constable started to prepare for these revised deadlines and advanced their own accounts production timetables so that draft accounts were ready by 19 June 2017 and the final signed accounts by August 2017. Whilst this was an advancement on the timetables applied in preceding years, further work is still required in order to ensure that the statutory deadlines for 2017/18 are met.

In order to meet the revised deadlines, the Police and Crime Commissioner and Chief Constable may need to make greater use of accounting estimates. In doing so, consideration will need to be given to ensuring that these estimates remain valid at the point of finalising the financial statements. In addition, there are a number of logistical challenges that will need to be managed. These include:

- Ensuring that any third parties involved in the production of the accounts (including valuers and actuaries) are aware of the revised deadlines and have made arrangements to provide the output of their work in accordance with this;
- Revising the closedown and accounts production timetables in order to ensure that all working papers and other supporting documentation are available at the start of the audit process;
- Ensuring that the Joint Independent Audit Committee meeting schedules have been updated to permit signing in July; and
- Applying a shorter paper deadline to the July meeting of the Joint Independent Audit Committee meeting in order to accommodate the production of the final versions of the accounts and our ISA 260 report.

In the event that the above areas are not effectively managed there is a significant risk that the audits will not be completed by the 31 July deadline.

Our assessment and work undertaken:

During the year we have liaised with officers and undertaken a review of your closedown timetable in order to understand the steps that the Police and Crime Commissioner and Chief Constable was taking in order to ensure they meet the revised deadlines. We also advanced all possible audit work into the interim visit in order to streamline the year end audit work.

We have rigorously reviewed all those accounting estimates that are material to the financial statements and we have set out our views on these at Page 12.

Judgements

We have considered the level of prudence within key judgements in your 2017/18 financial statements and accounting estimates. We have set out our view below across the following range of judgements.

Level of prudence

0	1	2	3	4	5	6
Audit Difference	Cautious		Balanced		Optimistic	Audit Difference
	Acceptable Range					

Subjective area	2017/18	2016/17	Commentary
Accruals de minimis level	2	2	There have been no changes in the accruals processes or de minimis levels used by the PCC and CC in the construction of its financial statements over the previous year, with a level of £5,000 being established. However, accruals below this level are often accounted for where they are significant to a particular budget. We consider this approach to be cautious.
Property, plant & equipment	2	3	Since 1st April 2017, property markets have remained relatively stable, with conditions across all commercial property markets remaining challenging. In view of this a cautious approach has been reflected in the valuer's year end valuation with little movement being recognised. A sufficient level of repairs and maintenance expenditure is being incurred by the PCC and there have been no indications of asset impairments during the year. We therefore consider the asset lives to be proportionate.

Judgements (cont.)

Subjective area	2017/18	2016/17	Commentary
Valuation of pension assets and liabilities	5	5	The PCC and CC continue to use Hymans Robertson to provide actuarial valuations in relation to the assets and liabilities recognised as a result of participation in the Local Government and Police Pension Schemes. Due to the overall value of the pension assets and liabilities, small movements in the assumptions can have a significant impact on the overall valuation. For example, a 0.5% change in the discount rate would change the net liabilities of these schemes by £144 million. The actual assumptions adopted by the Actuary fell within our expected ranges as set our below:

LGPS Assumption	Actuary Value	KPMG Range	Assessment
Discount rate	2.70%	2.20-2.60%	1
CPI inflation	2.40%	1.90-2.50%	2
Net discount rate	0.3%	0.10-0.30%	3
Salary Growth	2.80%	3.35-4.85%	4
Life expectancy Current male/female Future male/female	 22.1 / 24.4 24.1 / 26.6	 22.2/24.3 24.0/26.2	5

Police Pension Scheme Assumption	Actuary Value	KPMG Range	Assessment
Discount rate	2.70%	2.20-2.60%	1
CPI inflation	2.40%	1.90-2.50%	2
Net discount rate	0.3%	0.10-0.30%	3
Salary Growth	3.40%	3.35-4.85%	4
Life expectancy Current male/female Future male/female	 29.5 / 31.5 30.8 / 32.8	 22.2/24.3 24.0/26.2	5

Proposed opinion and audit differences

Subject to all outstanding queries being resolved to our satisfaction and for the necessary assurances being received from the auditors of the LGPS pension scheme we anticipate issuing an unqualified audit opinion on the PCC and CC's 2017/18 financial statements by 31 July 2018.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality (see Appendix 4) for this year's audit was set at £2.5 million. Audit differences below £0.125 million are not considered significant.

We did not identify any material misstatements, although our audit identified a total of two significant audit differences, which we set out in Appendix 3. It is our understanding that these will be adjusted in the final version of the financial statements.

The tables below illustrate the total impact of audit differences on the group's movements on the General Fund for the year and balance sheet as at 31 March 2018. Overall there is no impact on the General Fund as a result of audit adjustments.

In addition, we identified a number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 ('the Code'). We have set out details of significant presentational adjustments in Appendix 3. We understand that the PCC and CC will be addressing these where significant.

Movement on the General Fund 2017/18

£m	Pre-Audit	Post-Audit	Ref[1]
Deficit on the provision of services	(46.0)	(46.0)	1
Adjustments between accounting basis and funding basis under regulations	43.9	43.9	1
Transfers from earmarked reserves	2.1	2.1	
Increase/Decrease in General Fund	**0.0**	**0.0**	

Balance Sheet as at 31 March 2018

£m	Pre-Audit	Post-Audit	Ref[1]
Property, plant & equipment	32.1	32.1	
Other long term assets	3.2	3.2	1
Current assets	19.1	19.1	
Current liabilities	(18.8)	(18.8)	
Long term liabilities	(1,400.2)	(1,400.2)	
Net worth	**(1,364.6)**	**(1,364.6)**	
General Fund	(5.7)	(5.7)	
Other useable reserves	(11.5)	(11.5)	
Unusable reserves	1,381.8	1,381.8	1
Total Reserves	**1,364.6**	**1,364.6**	

[1] See referenced adjustments in Appendix 3.

Proposed opinion and audit differences (cont.)

Annual Governance Statement

We have reviewed the PCC and CC's 2017/18 Annual Governance Statements and confirmed that:

- They comply with Delivering Good Governance in Local Government: A Framework published by CIPFA/SOLACE; and
- They are not misleading and are consistent with other information we are aware of from our audit of the financial statements.

Narrative Report

We have reviewed the PCC and CC's 2017/18 Narrative Reports and have confirmed that they are consistent with the financial statements and our understanding of both the PCC and CC.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the PCC and CC's 2017/18 financial statements.

Before we can issue our opinions we require signed management representation letters.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of the Police and Crime Commissioner for Lincolnshire and the Chief Constable for Lincolnshire for the year ending 31 March 2018, we confirm that there were no relationships between KPMG LLP and the Police and Crime Commissioner for Lincolnshire and the Chief Constable for Lincolnshire, their directors and senior management and their affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 6 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Deputy Chief Finance Officer for presentation to the PCC and CC. We require a signed copy of your management representations before we issue our audit opinion.

As part of this process we are seeking specific management representations in respect of the assurances you have gained over the completeness and accuracy of the figures consolidated for the regional collaboration.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process; and
- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc.).

With regards to the above items there are no matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the PCC and CC's 2017/18 financial statements.

Completion

Other matters - continued…

However, there is one outstanding issue regarding the legality of an item of expenditure amounting to £14,579 which is recorded in the Chief Constable's Accounts. The draft accounts produced in May 2018 revealed expenses payments to a member of the Chief Constable's chief officer team of which the Force CFO (FCFO) had previously been unaware. The FCFO wrote to the Assistant Chief Officer (ACO) on 25 May 2018, as the Chief Constable's strategic HR lead, requesting advice on the legality of this expenditure. In the absence of a reply from the ACO, the Police & Crime Commissioner wrote to the Chief Constable on 18 June 2018 requesting advice on the legal basis of this expenditure. At the time of writing this report, no response had been received.

Both CFOs will need to take a view on the legality before the accounts are finalised. If a response is received from the Chief Constable and from our point of view as the external auditors whilst this amount is clearly not material to our audit there are clear governance and policy procedures that have not been followed. As a minimum the Authority needs to put in place robust controls to ensure such occurrences do not occur in the future..

There are no others matters which we wish to draw to your attention report or our previous reports relating to the audit of the PCC and CC's 2017/18 financial statements.

Section three

Value for Money Arrangements

Specific value for money risk areas

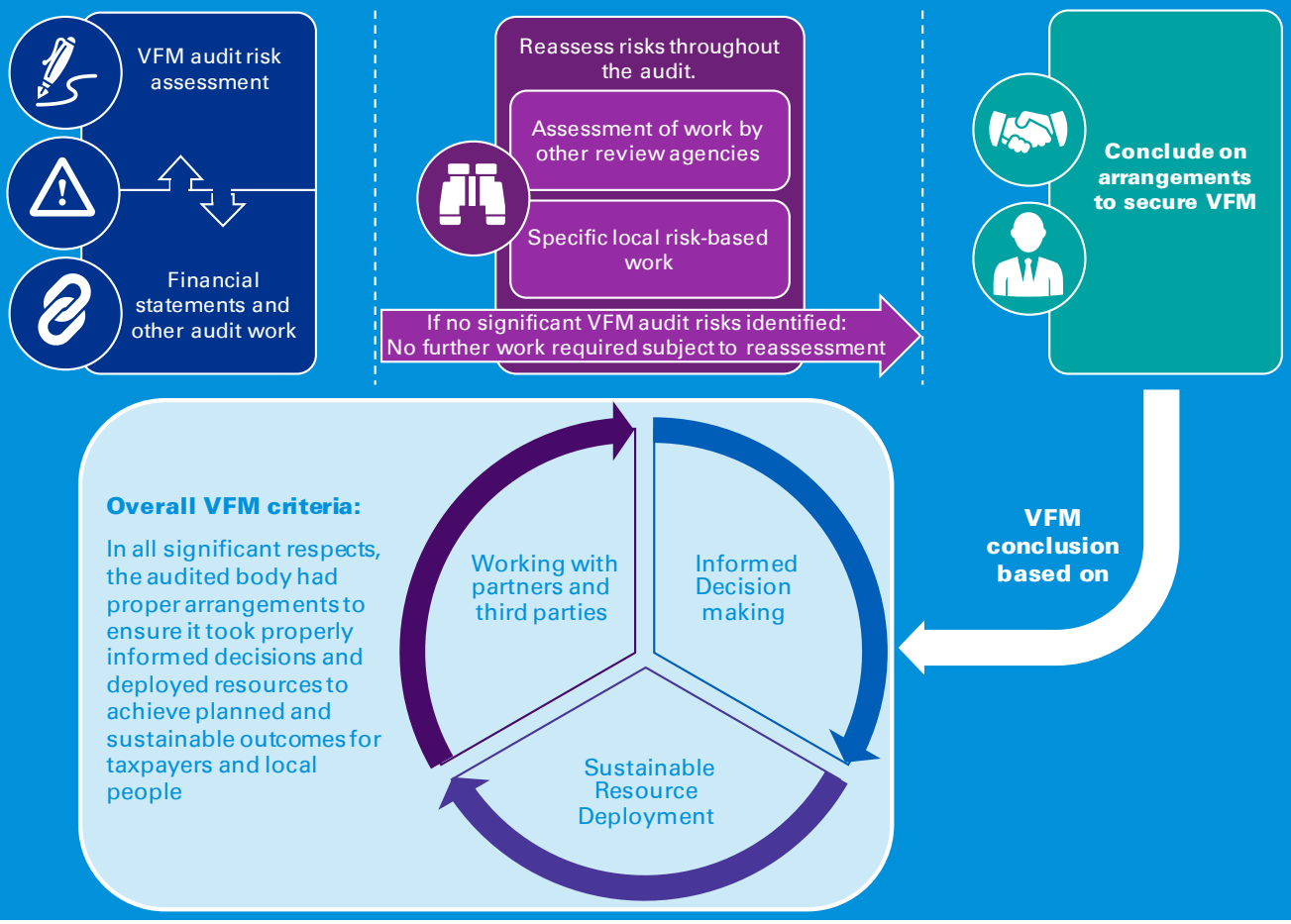
Our 2017/18 VFM conclusion considers whether the PCC and CC had proper arrangements to ensure they took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the PCC and CC have made proper arrangements to ensure they took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the PCC and CC 'have made proper arrangements for securing economy, efficiency and effectiveness in their use of resources'.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to 'take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor's judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body's arrangements.'

We follow a risk based approach to target audit effort on the areas of greatest audit risk.



Specific value for money risk areas (cont.)

The table below summarises our assessment of the individual VFM risk identified against the three sub-criteria. This directly feeds into the overall VFM criteria and our value for money opinion.

Applicability of VFM Risks to VFM sub-criteria			
VFM Risk	**Informed decision making**	**Sustainable resource deployment**	**Working with partner and third parties**
Medium term financial planning			

In consideration of the above, we have concluded that in 2017/18, the PCC and CC have made proper arrangements to ensure they took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Further details on the work done and our assessment are provided on the following pages.

Specific value for money risk areas (cont.)

As communicated to you in our *External Audit Plan 2017/18* we have *identified a single risk* requiring specific audit attention and procedures to address the likelihood that proper arrangements are not in place to deliver value for money.

In all cases we are satisfied that external or internal scrutiny provides sufficient assurance that the PCC and CC's current arrangements in relation to these risk areas are adequate.

We have provided below a summary of the risk areas identified, our work undertaken and the conclusions reached.

Risk:

Medium Term Financial Planning

The Police and Crime Commissioner and Chief Constable identified the need to make savings of £1.9 million in 2017/18. The current forecast shows that they will deliver an underspend of approximately £0.8 million for the financial year but are anticipating that further operational priorities will emerge that have the potential to reduce the underspend to a position closer to meet the approved balanced budget.

The overall budget was approved by the Police and Crime Commissioner on 24 February 2017 and recognised a need for £1.9 million in savings. The approved budget includes individual proposals to support the delivery of the overall savings requirement. Further savings of £1.7 million will be required over the period 2018 to 2020 to principally address future reductions to funding levels alongside service cost and demand pressures. As a result, the need for savings will continue to have a significant impact on the Police and Crime Commissioner and Chief Constable's financial resilience.

Our assessment and work undertaken:

Like most policing bodies, Lincolnshire faces a challenging future driven by funding reductions and an increase in demand for services, although this has been partly offset by the Government's relaxation in local Council Tax precepting limits. This position is highlighted by HMICFRS VFM profiles which shows the force as being one of the lowest funded forces per head of population nationally.

The group reported an overall breakeven position on its net expenditure budget for 2017/18 after the net contribution of £2.1 million from earmarked reserves. This enabled the General Fund balance to remain at £5.7 million as of 31 March 2018.

The PCC's MTFP details a balanced budget for 2018/19 although requires the need to draw down on reserves to the value of £4.9m. The plan takes into account an increase in Council Tax income of some 6.9% and savings of £3.1 million, all of which have been identified, and removes the previous assumptions around additional national funding being received. However, the MTFP details the increasingly difficult financial challenges faced each year, resulting in the need for ever rising savings, up to £11.2 million by 2021/22. Given that the PCC has already made significant savings in its back office functions by fully leveraging its strategic partnership with G4S, it is inevitable that these can only be met by staffing reductions going forward.

We have assessed the arrangements put in place by the PCC and CC to maintain its record of meeting efficiency savings to the funding gap, by relying on our accounts audit work where relevant, underpinned by a review of the PCC and CC's budget setting process, financial management processes, and discussions with the senior management team. Whilst we have no concerns in respect of the VFM conclusion for 2017/18 this position will need careful consideration in 2018/19 given the future funding shortfalls beyond this period and the levels of savings required.

Appendices

Appendix 1:

Key issues and recommendations

Our audit work on the PCc and CC's 2017/18 financial statements has identified a single issue. We have listed this issue in this appendix together with our recommendation which we have agreed with Management. We have also included Management's responses to this recommendation.

The PCC and CC should closely monitor progress in addressing the risk, including the implementation of our recommendation.

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority Rating for Recommendations

1	**Priority One:** Issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk. Recommendations Raised: 0	2	**Priority Two:** Issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system. Recommendations Raised: 1	3	**Priority Three:** Issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them. Recommendations Raised: 0

No.	Risk	Issue & Recommendation	Management Response
1	2	***Quality of working papers*** We have noted a deterioration in the quality of working papers provided in support of the financial statements over the previous year. ***Risk*** There is a risk of audit work being delayed or additional costs being incurred in the audit process. ***Recommendation*** Sufficient time should be built in to the closedown timetable to enable an appropriate review of working papers to be undertaken and any necessary corrective action implemented before the commencement of the audit process.	We agree that working papers should be of the required standard. Appropriate time will be given to review the working papers for 2018/19. ***Responsible Officer*** Head of Finance ***Implementation Deadline*** 2018/19 Statement of Accounts

Appendix 2:

Follow-up of prior year recommendations

The Authority has implemented all of the recommendations raised through our previous audit work.

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2016/17* and re-iterates any recommendations still outstanding.

Number of recommendations that were	
Included in the original report	3
Implemented in year or superseded	3
Outstanding at the time of our interim audit	0

No.	Risk	Issue & Recommendation	Management Response	Status as at July 2018
1	1	***Narrative Report compliance*** Our review of the PCC and CC's Chief Finance Officer's Narrative Reports has identified a number of areas were improvements could be made in order to ensure full compliance with CIPFA's Code of Practice. ***Recommendation*** The PCC and CC should ensure that its Narrative Reports fully comply with CIPFA's Code of Practice and that clarity is provided over any figures reported within the Narrative Report and the financial statements.	Accepted. ***Responsible Officer*** PCC CFO/CC CFO ***Implementation Deadline*** 2016/17 and 2017/18 Statement of Accounts	The format of the PCC and CC Chief Finance Officer's Narrative Reports have been updated to reflect the updated CIPFA guidance for the current year and now incorporate the Code of Practice requirements.
2	2	***Review of pensions data submitted to the actuary*** Our testing of the PCC and CC's processes over the provision of data to the actuary highlighted an error in the information submitted in respect of the Police Pension Scheme ***Recommendation*** The PCC and CC should ensure that an appropriate level of review is put in place over the data being submitted to the actuary to ensure its completeness and accuracy.	Accepted. ***Responsible Officer*** Head of Finance ***Implementation Deadline*** 2017/18 Statement of Accounts	The 2017/18 pensions data was subject to scrutiny and review by the Head of Finance prior to its submission to the actuary.

Appendix 2:

Follow-up of prior year recommendations (cont.)

No.	Risk	Issue & Recommendation	Management Response	Status as at July 2018
3	2	***Review of fair value disclosures*** Our testing identified that a number of the required 'fair value' disclosures required by CIPFA's Code of Practice, including the accounting policy and detailed measurement bases, had not been made within the Statement of Accounts. These omissions should have been identified from the correct completion of CIPFA's Code Disclosure Checklist. ***Recommendation*** The PCC and CC should ensure that sufficient time and resource is devoted to the accurate completion of CIPFA's Code Disclosure Checklist, with any uncertainties over answers being investigated more thoroughly.	Accepted. ***Responsible Officer*** Head of Finance ***Implementation Deadline*** 2017/18 Statement of Accounts	Time was included in the closedown plan and the 2017/18 CIPFA's Code Disclosure Checklist was completed as part of the accounts production process.

Appendix 3:

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the PCC and CC).

We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

A number of minor amendments focused on presentational improvements have also been made to the 2017/18 draft financial statements. The Finance team is committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Adjusted audit differences impacting the primary statements

The following table sets out the significant audit differences impacting on the primary statements identified by our audit of Police and Crime Commissioner for Lincolnshire and the Chief Constable for Lincolnshire's financial statements for the year ended 31 March 2018, at a group level. Similar adjustments are also required in respect of the individual entities accounts. It is our understanding that these will be adjusted. However, we have not yet received a revised set of financial statements to confirm this.

Table 1: Adjusted audit differences impacting the primary statements – Group (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1	Dr Gross expenditure – Other operating expenditure 1,277 Cr Gross income – PCC (1,277) Dr Gross expenditure - Interest element of finance lease 71 Cr Gross expenditure – PCC (71)	Dr Capital expenditure financed from revenue balances 1,277 Cr Reversal of entries included in the CIES in relation to capital expenditure (1,277)	Dr Intangible assets – Additions purchased 1,277 Cr Intangible assets – Additions leased (1,277)		Dr CAA – Amounts of assets written off 1,277 Cr CAA – Capital expenditure charged against the General Fund (1,277)	The associated transactions in respect of the NICHE passthrough costs with City of London Police were incorrectly accounted for. This error also required amendments to the Expenditure and Funding Analysis and Notes 5, 6, 8, 9, 15 17, 27 and 33 within the group statements
2	-	-	-	-	-	The cash flow figures in respect of adjustments for non-cash movements and financing activities had been incorrectly calculated by £1,231. This error also required amendments to the Expenditure and Funding Analysis and Notes 31 and 35 within the group statements.
	Dr/Cr 0	**Dr/Cr 0**	**Dr/Cr 0**	**Dr/Cr 0**	**Dr/Cr 0**	**Total impact of adjustments**

Audit differences (cont.)

Adjusted numerical audit differences impacting disclosure notes

The following table sets out the significant numerical audit differences impacting on the disclosure notes identified by our audit of the Police and Crime Commissioner for Lincolnshire and the Chief Constable for Lincolnshire's financial statements for the year ended 31 March 2018, at a group level. Similar adjustments are also required in respect of the individual entities accounts. It is our understanding that these will be adjusted. However, we have not yet received a revised set of financial statements to confirm this.

Table 2: Adjusted numerical audit differences impacting disclosure notes – Group

No.	Disclosure note	£,000	Basis of audit difference
3	42 – Related Party Transactions	18,214	Incorrect extraction of transactions in relation to other public bodies from the underlying accounting system.
		18,214	**Total value of adjustments**

Presentational adjustments - Group

We identified a number of presentational adjustments required to ensure that the PCC and CC's financial statements for the year ending 31 March 2018 are fully compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 ('the Code').

Whilst the majority of these adjustments were not significant, we identified a limited number of adjustments of a more significant nature and details of these are provided in the following table.

It is our understanding that these will be adjusted. However, we have not yet received a revised set of financial statements to confirm this.

Table 3: Presentational adjustments – Group

No.	Basis of audit difference
4	Note 1 Accounting policies: A number of inconsistencies and omissions were noted between the Code requirements and those disclosed by the PCC and CC;
5	Note 45 Financial instruments: A number of inconsistencies and omissions were noted between the Code requirements and the PCC and CC's disclosures most notably the fair value disclosures in relation to PWLB debt.

Unadjusted audit differences

We confirm that there are no uncorrected misstatements, other than those that we believe are clearly trivial.

Appendix 4:

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgement and includes consideration of three aspects: materiality by value, nature and context.

Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.

Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.

Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2017/18, presented to you in April 2018.

Materiality for the PCC and CC's accounts was set at £2.5 million which equates to around 1.7 percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Joint Independent Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Joint Independent Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the PCC and CC, an individual difference is considered to be clearly trivial if it is less than £0.125 million.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Joint Independent Audit Committee to assist it in fulfilling its governance responsibilities.

Appendix 5:

Required communications with the Joint Independent Audit Committee

We have provided below at-a-glance summary of the information we are required to report to you in writing by International Accounting Standards.

Required Communication	Commentary
Our draft management representation letter	We have requested a single specific representation in relation to Regional Collaboration assurances in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2018.
Adjusted audit differences	We have identified two audit adjustments impacting the primary statements with a total value of £3 million, a further two errors in disclosure with a total value of £18 million and a number of presentational issues. See Page 14 for details. These adjustments result in a no movement in the reported deficits on provision of services. See Page 26 for further details.
Unadjusted audit differences	We have identified no unadjusted differences as a result of our audit of the PCC and CC's financial statements
Related parties	There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Joint Independent Audit Committee	There were no matters to report arising from the audit that, in our professional judgement, are significant to the oversight of the financial reporting process.
Control deficiencies	We have set out our assessment of the PCC and CC's internal control environment, including confirmation that there were no significant deficiencies identified, in Section one of this report (see Page 4).
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	We identified no actual or suspected fraud involving the PCC or CC's officers with significant roles in internal control, or where the fraud resulted in a material misstatement in the financial statements.
Significant difficulties	No significant difficulties were encountered during the audit.
Modifications to auditor's report	There are no modifications to our audit report.
Disagreements with management or scope limitations	The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.

Appendix 5:

Required communications with the Joint Independent Audit Committee (cont.)

Required Communication	Commentary
Other information	No material inconsistencies were identified related to other information in the Narrative Report or Annual Governance Statement. These reports were found to be fair, balanced and comprehensive, and compliant with applicable requirements.
Our declaration of independence and any breaches of independence	No matters to report. The engagement team have complied with relevant ethical requirements regarding independence. See Appendix 6 for further details.
Accounting practices	Over the course of our audit, we have evaluated the appropriateness of the PCC and CC's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate. We have set out our view of the assumptions used in valuing pension assets and liabilities at Page 13.
Significant matters discussed or subject to correspondence with management	There were no significant matters arising from the audit which were discussed, or subject to correspondence, with management.

Appendix 6:

Declaration of independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF THE POLICE AND CRIME COMMISSIONER FOR LINCOLNSHIRE AND THE CHIEF CONSTABLE FOR LINCOLNSHIRE

Professional ethical standards require us to provide to you at the conclusion of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code of Audit Practice, the provisions of Public Sector Audit Appointments Limited's ('PSAA's') Terms of Appointment relating to independence, the requirements of the FRC Ethical Standard and the requirements of Auditor Guidance Note 1 - General Guidance Supporting Local Audit (AGN01) issued by the National Audit Office ('NAO') on behalf of the Comptroller and Auditor General.

This Statement is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

— General procedures to safeguard independence and objectivity;

— Independence and objectivity considerations relating to the provision of non-audit services; and

— Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

— Instilling professional values

— Communications

— Internal accountability

— Risk management

— Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Declaration of independence (cont.)

Independence and objectivity considerations relating to the provision of non-audit services

Summary of fees

We have considered the fees charged by us to the PCC and CC and its controlled entities for professional services provided by us during the reporting period. We have detailed the fees charged by us to the PCC and CC and its controlled entities for significant professional services provided by us during the reporting period in Appendix 7, as well as the amounts of any future services which have been contracted or where a written proposal has been submitted. Total fees charged by us for the period ended 31 March 2018 can be analysed as follows:

	2017/18 £	2016/17 £
Audit of the Police and Crime Commissioner	29,291	30,855
Audit of the Chief Constable	15,000	15,235
Total audit services	**44,291**	**46,090**
Allowable non-audit services	0	0
Audit related assurance services	0	0
Mandatory assurance services	0	0
Total Non Audit Services	**0**	**0**

We are required by AGN 01 to limit the proportion of fees charged for non-audit services (excluding mandatory assurance services) to 70% of the total fee for all audit work carried out in respect of the PCC and CC under the Code of Audit Practice for the year. The ratio of non-audit fees to audit fees for the year was 0:1. We do not consider that the total of non-audit fees creates a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed to the Joint Independent Audit Committee.

Confirmation of audit independence

We confirm that as of the date of this report, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the Joint Independent Audit Committee of the PCC and CC and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

KPMG LLP

KPMG LLP

Appendix 7:

Audit fees

As communicated to you in our *External Audit Plan 2017/18*, our scale fee for the audits are detailed below:

Component of the audit	2017/18 Planned Fee £	2016/17 Actual Fee £
Accounts opinion and value for money work		
PSAA Scale fee (Police and Crime Commissioner)	29,291	29,291
PSAA Scale fee (Chief Constable)	15,000	15,000
Additional fee in relation to accounts restatement and consideration of accounting treatment of strategic partnership contract costs	0	1,799
Total audit services	**44,291**	**46,090**
Total non-audit services	**0**	**0**
Grand total fees for the PCC and CC	**44,291**	**46,090**

All fees quoted are exclusive of VAT.

The key contacts in relation to our audit are:

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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. We draw your attention to the Statement of Responsibilities of auditors and audited bodies, which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Andrew Cardoza, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers, by email to Andrew.Sayers@kpmg.co.uk. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

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