

Forth Estuary Transport Authority

Report to Members and the Controller of Audit
on the 2006/07 Audit



October 2007





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Introduction

1. This report summarises the findings from our 2006/07 audit of the Forth Estuary Transport Authority. The scope of the audit was set out in our audit plan issued in March 2007.
2. The financial statements of the Forth Estuary Transport Authority are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of these resources. It is the responsibility of the authority to prepare financial statements that present fairly its financial position and the income and expenditure for the year.
3. The members and officers of the authority are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
 - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed;
 - the authority's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests;
 - the authority has adequate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability;
 - the systems of internal control provide an appropriate means of preventing or detecting material misstatement, error, fraud or corruption;
 - the authority has proper arrangements for securing best value in its use of resources.



Financial statements

Introduction

4. In this section we summarise key outcomes from our audit of the authority's financial statements for 2006/07. We also summarise key aspects of the authority's reported financial position and performance to 31 March 2007.
5. We audit the financial statements and give an opinion on:
 - whether they present fairly the financial position of the authority and its expenditure and income for the year; and
 - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
6. We also review the Statement on the System of Internal Financial Control by considering the adequacy of the process put in place by the authority to obtain assurances on systems of governance and internal financial control and assessing whether disclosures in the statement are consistent with our knowledge of the organisation.

Overall conclusion

7. We have given an **unqualified** opinion on the financial statements of the Forth Estuary Transport Authority for 2006/07.
8. The unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. The authority is required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). Some amendments were made to the figures included in the unaudited accounts made available for public inspection. In particular, adjustment was required to reflect the prepayment of various insurances which is detailed further below. As part of the closedown arrangements, we would suggest that the CIPFA disclosure checklist is completed to ensure that the unaudited accounts are presented in accordance with the requirements of the SORP. This will minimise the changes required in presentation on conclusion of the audit.
9. Audited accounts were finalised prior to the target date of 30 September 2007 and are now available for presentation to the authority and publication.



Financial position

10. The presentation of the 2006/07 financial statements has changed significantly from previous years to make them more consistent with the accounts of other public and private sector entities. They now include an income and expenditure account and a separate statement on the movement in general fund balance, replacing the revenue account. The latter statement reflects items that require to be taken into account when determining the authority's budget requirement.
11. The surplus or deficit on the income and expenditure account measures the authority's financial result for the year, recognising the resources that have been consumed and generated in accordance with Generally Accepted Accounting Principles. The authority achieved net operating income in 2006/07 of £3.619 million before making a contribution to the capital account of £12.245 million resulting in an overall income and expenditure deficit for the year of £8.626 million.
12. However, the movement on the general fund balance is an important aspect of the authority's stewardship as the main budget preference point, the main difference being:
 - capital investment is accounted for as it is financed, rather than when fixed assets are consumed;
 - retirement benefits are charged as amounts become payable to pension funds and pensioners, rather than as future benefits are earned.
13. After adjusting for these items, the authority incurred a deficit of £5.589 million compared with a planned deficit of £10.197 million. When this deficit is deducted from the amount brought forward from 2005/06, the authority has a general fund balance of £13.054 million. In his foreword to the accounts, the Treasurer sets out the main factors contributing to the budget underspend in the year. The main factor impacting on the year end position was an underspend on supplies and services, due to slippage in the main cable replacement/ augmentation study, main tower cathodic protection and expenditure on minor works during the year.

Accounting practice

14. Overall, the authority has made a satisfactory attempt in preparing the accounts in accordance with the revised SORP. Several amendments were however agreed to improve the presentation of information contained within the accounts and provide the detail required by the SORP. For example:
 - including appropriate explanation for the reader of the accounts about the significant changes required by the 2006 SORP;
 - fuller disclosure on fixed assets and the cash flow statement;
 - improvements in the notes to the accounts.



Prepayment of insurances

15. The main amendment to the draft financial statement was required to reflect the inclusion of a prepayment for a range of insurances. Insurances charged to 2006/07 incorrectly included prepayments totalling £0.233 million, consequently expenditure was reduced by this amount and debtors increased.

Pension costs

16. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. Financial Reporting Standard 17 (Retirement Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future.
17. The authority's estimated pension liabilities at 31 March 2007 exceeded its share of the assets in the Lothian pension Fund by £1.874 million, reducing from £2.940 million in the previous year. The actuary was required to make a three-year assessment of the contributions that should be paid by employing authorities from 1 April 2006 to maintain the solvency of the fund. In addition to the employers' contribution (known as the 'future service rate') of 16.8% of salaries, additional contributions of £57,000, £98,000 and £142,000 are required in the years 2006/07, 2007/08 and 2008/09 respectively.

Legality

18. Each year we request written confirmation from the Treasurer that the authority's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of the General Manager and Senior Management Team, the financial transactions of the authority were in accordance with the relevant legislation and regulations governing its activities.
19. There are no additional legality issues arising from our audit which require to be brought to members' attention.



Looking ahead

20. In the coming years the authority may face significant financial challenges including:

- in view of the Scottish Government's decision to remove bridge tolls, discussions are ongoing to confirm the authority's alternative funding mechanism. This is likely to take the form of a government grant;
- the ongoing maintenance and health and safety requirements of the bridge and in particular, the need to halt the corrosion in the main cables if further loss of strength and potential restriction on heavy goods vehicles is to be avoided;
- the ongoing investigation into the feasibility of replacing/augmenting the main cables including proving the structural integrity of the main cable anchorages;
- specific cost pressures which may arise from the need to fund increased pension costs.

21. These areas and the controls put in place by management to address the issue are likely to be subject to on-going review during the 2007/08 audit.



Governance

Introduction

22. In this section we comment on key aspects of the authority's governance arrangements during 2006/07.

Overview of arrangements in 2006/07

23. Corporate governance is concerned with structures and processes for decision making, accountability, control and behaviours at the upper levels of the organisation. The authority has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.

24. A Statement on the System of Internal Financial Control is included within the annual financial statements, and highlights the Treasurer's view that reasonable assurance can be placed upon the adequacy and effectiveness of the authority's internal financial control system.

25. In accordance with good practice, the statement was reviewed by the Authority in August 2007 and is supported by a high level review of the adequacy and effectiveness of internal financial controls undertaken by Internal Audit. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.

26. The authority formally adopted a local code of governance in June 2006 based on best practice identified jointly by CIPFA and SOLACE. A Statement of Assurance on Corporate Governance is included within the annual financial statements and has been signed by the Convener, Chief Executive and General Manager.

Audit committee and internal audit

27. Effective scrutiny is central to good governance, with a significant role for authority members to scrutinise performance and hold management to account. Due to the size of the organisation, the authority has not established an audit committee. That said, the authority considers reports by internal and external audit. In addition, the Chief Internal Auditor provides an annual report, including a statement on the adequacy and effectiveness of the internal control system.



28. Internal audit plays a key role in the authority's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. An internal audit service is provided to the authority by the City of Edinburgh Council's Chief Internal Auditor. From our review of the service, we found that the work is conducted in accordance with CIPFA's Code of Practice for Internal Audit in Local Government, that the audit plan was sufficient and that all work on which we planned to place reliance was completed and the relevant assurances obtained.
29. Arising from a review of the authority's risk management activities, internal audit reported that the overall risk maturity assessment for the authority was level 3 (of a 5 stage process) which is described as 'risk defined' i.e. that the entity has reasonable knowledge of risk management as a result of the strong corporate governance culture. While there is a clear commitment to identifying and managing risks, it was noted that some processes required to be strengthened to enable the bedding in of risk management practices across the organisation. For example, the identification of risk needs to be considered on an ongoing basis, risk registers should be formally reviewed on a regular basis and specific risks should be allocated to responsible officers for monitoring and managing. These matters are contained within an action plan which management have agreed with internal audit for action in 2007/08.
30. We also note that the authority approved a business continuity plan in June 2006. The existence of such a plan is an important aspect of an organisation's corporate governance arrangements but is also integral to its risk management framework. A business continuity plan is intended to provide an overall framework for managing the repercussions of serious incidents affecting an organisation by setting out the necessary actions to be taken. It is intended that processes will be put in place to revise the plan in light of operational experience.

Systems of internal control

31. The authority's financial transactions are processed through the City of Edinburgh's financial systems. It is therefore the responsibility of the Council's management to maintain adequate financial systems and associated internal controls. The auditor evaluates significant financial systems and associated internal controls both for the purpose of giving an opinion on the financial statements and as part of a review of the adequacy of governance arrangements.
32. Our review of these systems was conducted as part of the audit of City of Edinburgh Council, supplemented by specific audit work on the authority's financial statements. Overall there are no material issues of concern in relation to the operation of the main financial systems.



33. We noted however that the authority tracks movements in fixed assets through a series of spreadsheets. At 31 March 2007, we sought and received assurances from the Treasurer that these spreadsheets provided a complete record of fixed assets in the ownership of the authority and that all were appropriately classified. We would suggest that a more comprehensive asset register is compiled not only to support the disclosures in the accounts but to assist management in ensuring that all assets are effectively used.

Key Risk Area 1

Prevention and detection of fraud and irregularities

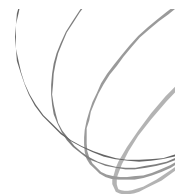
34. The authority has arrangements in place to prevent and detect fraud, inappropriate conduct and corruption. These arrangements include standing orders and financial regulations, a whistle blowing policy, an anti-fraud and corruption policy and codes of conduct for elected members and staff. We are pleased to note that the authority continues to have appropriate arrangements in place to minimise the risk of fraud and corruption.

Looking ahead

35. In the coming years, the authority may face significant challenges including:

- in light of the increasing challenges the authority faces e.g. ensuring compliance with health and safety requirements; proving the integrity of the main cable anchorages; halting corrosion in the main cables etc, a review was undertaken of the organisational structure in 2006 to ensure it was fit for purpose. The authority, and the effectiveness of its current structure, is likely to continue to face challenges as its remit is revised in light of recent and anticipated future Scottish Government decisions around the removal of tolls and a new Forth crossing;
- the authority had approved a borrowing strategy for 2007/08 and 2008/09 including the approval of prudential indicators covering its estimated borrowing requirement of £15 million in connection with the A8000 project. However, in light of the possible removal of tolls, discussions are continuing with the Scottish Government to identify alternative funding sources, through grant aid. The authority will need to operate in accordance with the grant aid made available by the Scottish Government and continue to avoid slippage in its capital programme.

36. These areas and the controls put in place by management to address the issue are likely to be subject to on-going review during the 2007/08 audit.



Final Remarks

37. The members of the Forth Estuary Transport Authority are invited to note this report. We would be pleased to provide any additional information that members may require.
38. The co-operation and assistance given to us by officers of the authority and the City of Edinburgh Council is gratefully acknowledged.

Audit Scotland
October 2007



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1	33	<p>Asset Register</p> <p>Fixed assets are tracked through a series of spreadsheets each year making it difficult to inspect a comprehensive list of assets.</p> <p><i>Risk: The asset register may not be complete leading to a loss of assets.</i></p>	Authority management will assist the Treasurer develop a fuller asset register.	Authority management and Treasurer	March 2009