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INFRASTRUCTURE, GOVERNMENT & HEALTHCARE

Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee

Annual audit report to the members and the Controller of Audit

2007-08

23 October 2008

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

Executive summary	1
Introduction	3
Financial statements audit	4
Financial position	8
Corporate governance	11
Performance management	15
Appendix 1 – action plan	16

Notice: About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ('the *Code*').

It is for the benefit of only Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee and is made available to the Accounts Commission and Audit Scotland (together the beneficiaries), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the introductory section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the beneficiaries) for any purpose or in any context. Any party other than the beneficiaries that obtains access to this report or a copy and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the beneficiaries.

Executive summary

This report summarises our work for the 2007-08 year and our findings in relation to our audit of the financial statements, corporate governance and performance management arrangements of Strathclyde Partnership for Transport ("the Partnership") and the Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC")

Financial statements

On 19 September 2008 we issued audit reports giving our unqualified opinions on the financial statements of the Partnership and SCTSJC for the year ended 31 March 2008. A number of matters were discussed and resolved with management during the course of the audit process.

The carrying value of the Partnership's fixed assets has increased significantly during the year as a result of revaluations at 31 March 2008, with impairments of £24.8 million offsetting a valuation increase of £61 million. The Partnership's total carrying value of fixed assets at 31 March 2008 was £188.7 million (2007: £96.1 million).

During 2007-08, the Partnership purchased their headquarters, Consort House, from their landlord for £17.6 million. The property was valued at 31 March 2008 at £10 million. The difference between the purchase price, augmented by some tenant improvements resulted in a write-down in the value by £9.2 million. An independent report found that this was more economical than continuing with onerous lease conditions.

After seeking external advice on the best way to secure the land, the Partnership transacted a *de facto* Compulsory Purchase Order, including the purchase and subsequent liquidation of Airlink Security Park Limited as part of the Glasgow Airport Rail Link project. At the 31 March 2008, impairment to the carrying value of land purchased was required of £4.6 million to present the asset at market value in accordance with the 2007 SORP.

The Glasgow Airport Rail Link project was transferred to Transport Scotland during May 2008 and is disclosed as a post balance sheet event. The value of this transfer was £1.9 million. The transfer agreement between the parties confirmed there would be no financial detriment to the Partnership.

Financial position

The Partnership reported a deficit on the general fund balance for 2007-08 due to the utilisation of £4.8 million of general fund reserves to fund capital expenditure from revenue and an audit adjustment to create a provision for early retirements of £0.4 million. The revenue out-turn for the year was in line with budget before these adjustments. The general fund balance of the Partnership has decreased by £5.2 million to £13.6 million (2007: £18.8 million) due primarily to these adjustments.

SCTSJC reported a deficit in 2007-08 of £735,000 against a budgeted deficit of £1,000,000. The deficit is primarily due to the Scottish Government debtor at 31 March 2007 not being recovered in full and a bad debt write off of £586,000 being required, offset by £851,000 of expected payments to bus operators not being made and lower overheads than anticipated. SCTSJC has a general fund balance of around £9.3 million (2007: £10 million) which has accumulated over a number of years.

During 2007-08, the Partnership spent £52.6 million on capital projects. Expenditure for the year was in excess of budget due to the purchase of Consort House, offset to some extent by slippage in a few projects.

At the 31 March 2008, the Partnership had short term investments of £23.6 million. This represented an increase of £8.8 million from the prior year.

Corporate governance

The Partnership's and SCTSJC's statement of internal financial control is in accordance with the 2007 SORP requirements and indicates no significant weaknesses. We have placed formal reliance upon the work of internal audit for 2007-08. The internal audit annual report concluded that "reasonable assurance can be placed upon the adequacy and effectiveness of the Partnership's internal control systems in the year to 31 March 2008."

We reported 18 recommendations in our interim report, with one significant recommendation raised concerning business continuity and disaster recovery plans. From Audit Scotland's *Priorities and Risks Framework*, we identified five areas where opportunities exist to enhance current arrangements. These were in respect of focussing on strategies, performance indicators, demonstrating Best Value and developing procurement practices in relation to e-procurement and the findings of the McClelland report. Internal audit has begun monitoring the implementation of recommendations made in internal and external audit reports.

There were no material instances of fraud reported in 2007-08. Overall, we considered that the Partnership has adequate arrangements for managing obligations with respect to the National Fraud Initiative.

Performance management

During 2007-08, the internal audit department completed three value for money audits. These reports resulted in a number of recommendations to management relating to the formal contracts and reviews of the services.

The head of organisational development has been charged with co-ordinating a number of Best Value initiatives going forwards.

No specific requirements have been made of the Partnership in respect of efficient government targets. However, we understand that in response to the council tax freeze and other financial pressures on the constituent local authorities that a 2% efficiency target has been set for future revenue budgets.

Introduction

Audit framework

This was the second year of our five-year appointment as external auditors of Strathclyde Partnership for Transport ("the Partnership") and Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC"). This report to the members and the Controller of Audit outlines our opinion and conclusions and highlights significant issues arising from our work.

In accordance with Audit Scotland's Code of Audit Practice ("the Code"), the scope of the audit was to:

- provide an opinion on the both the Partnership's and the SCTSJC's financial statements;
- review and report on:
  - the Partnership's and SCTSJC's corporate governance arrangements as they relate to: the review of systems of internal control; the prevention and detection of fraud and irregularity; standards of conduct, and prevention and detection of corruption; their financial position
  - the Partnership's and SCTSJC's arrangements to achieve Best Value
  - other aspects of the Partnership's and SCTSJC's arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.

The framework under which we operate under appointment by Audit Scotland was outlined in the audit plan for the year discussed with the audit committee.

KPMG's audit methodology is risk based. To assist in the development of a consistent approach to the audit across bodies, Audit Scotland publishes *Priorities and Risks Framework* guidance, setting out a number of areas for consideration during the audit process. We used the material developed by Audit Scotland in 2007-08 in our assessment of the processes and management arrangements. Our own planning process also identified a number of other areas for specific attention.

Basis of information

External auditors do not act as a substitute for the entity's own responsibilities for putting in place proper arrangements to account for its stewardship of resources made available to it and its financial performance in the use of those resources, to ensure the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the effectiveness of those arrangements and, through accountable officers, to make arrangements to secure Best Value.

We have structured the report around the headings financial statements audit, financial position, governance arrangements and performance management arrangements.

Acknowledgement

We wish to place on record our appreciation of the co-operation and assistance extended to us by staff during the second year of our work in the discharge of our responsibilities.

Financial statements audit

- We have issued unqualified audit opinions on the financial statements of Strathclyde Partnership for Transport and of the Strathclyde Concessionary Travel Scheme Joint Committee for the year ended 31 March 2008.
- The carrying value of the Partnership's fixed assets has increased significantly during the year as a result of revaluations at 31 March 2008, with impairments of £24.8 million offsetting a valuation increase of £61 million. The Partnership's total carrying value of fixed assets at 31 March 2008 was £188.7 million (2007: £96.1 million).
- During 2007-08, the Partnership purchased their headquarters, Consort House, from their landlord for £17.6 million. The property was valued at 31 March 2008 at £10 million. The difference between the purchase price, augmented by some tenant improvements resulted in a write-down in the value by £9.2 million. An independent report found this was more economical than continuing with onerous lease conditions.
- After seeking external advice on the best way to secure the land, the Partnership transacted a *de facto* Compulsory Purchase Order, including the purchase and subsequent liquidation of Airlink Security Park Limited as part of the Glasgow Airport Rail Link project. At the 31 March 2008, impairment to the carrying value of land purchased was required of £4.6 million to present the asset at market value in accordance with the 2007 SORP.
- The Glasgow Airport Rail Link project was transferred to Transport Scotland during May 2008 and is disclosed as a post balance sheet event. The value of this transfer was £1.9 million. The transfer agreement between the parties confirmed there would be no financial detriment to the Partnership.

Reporting arrangements and timetable

In accordance with management's timetable, draft financial statements were available for audit on 2 June 2008. This allowed for completion of the audit and consideration and approval of the financial statements on 19 September 2008.

Audit opinion

On 19 September 2008 we issued audit reports expressing unqualified opinions on the financial statements of the Partnership and SCTSJC for the year ended 31 March 2008.

We wish to bring the following issues to your attention.

Transport (Scotland) Act 2006 (the "2006 Act")

Section 3 of the 2006 Act requires that, similar to other Regional Transport Authorities, constituent local authorities meet only the Partnership's net expenses (ie. the expenses for the year not met by grant or other income) for each financial year. Following discussions with the Scottish Government, Audit Scotland issued guidance in late June 2007 clarifying this position. The Partnership, having taken legal advice, does not agree with this interpretation of the 2006 Act, but has prepared its 2007-08 financial statements in accordance with these requirements. The Partnership reported a deficit of £5.2 million, which has been met by the Partnership's general fund reserve. No debtor has been created with the constituent local authorities as they will not finance a deficit whilst the Partnership is able to draw on the general fund reserve, as that is not *ultra vires* per the 2006 Act.

Fixed assets

Revaluation

In order to ensure compliance with the 2007 SORP, the Partnership completed a revaluation exercise of all land and buildings during 2007-08. The revaluation resulted in an increase in value of £61 million taking the total carrying value of fixed assets at 31 March 2008 to £188.7 million (2007; £96.1 million). There was also a write-down of £24.8 million to the carrying value of fixed assets. The revaluation adjustment was recorded through the revaluation reserve in accordance with the 2007 SORP. The write-down in value was charged to the income and expenditure account, then adjusted through the Capital Adjustment Account in accordance with the 2007 SORP.

Consort House

During 2007-08, the Partnership purchased their headquarters, Consort House, from their landlord for £17.6 million. The purchase was financed from the Partnership's existing capital programme (£10.5 million) and additional capital funding from other Regional Transport Partnerships (£2.3 million). The remainder of the cost was financed from revenue funding resulting in a deficit for the year and a draw on the general fund reserve of (£4.8 million). The property was valued at 31 March 2008 at £10 million. The difference between the purchase price, augmented by some tenant improvements resulted in a write-down in the value by £9.2 million. This transaction was completed after an independent report found that purchasing the building was more economical than continuing to lease the building under the onerous conditions of the lease.

Glasgow Airport Rail Link

After seeking external advice on the best way to secure the land, the Partnership transacted a *de facto* Compulsory Purchase Order, including the purchase and subsequent liquidation of Airlink Security Park Limited as part of the Glasgow Airport Rail Link project. At the 31 March 2008, impairment to the carrying value of land purchased was required of £4.6 million to present the asset at market value in accordance with the 2007 SORP.

Assets under construction

The Partnership holds a number of non-operational assets. Assets under construction have increased in value from £12.6 million at 31 March 2007 to £16.8 million at 31 March 2008. The balance refers primarily to two large construction projects at Partick station and Croy park-and-ride. Both of these projects are still in progress. In relation to the Partick station project significant delays have been experienced with the expected completion date behind schedule. The delays have been due to a mixture of contractual, engineering and operational issues. The Partnership has received numerous claims from the contractor in relation to additional costs for the project. An external opinion was received by the Partnership in relation to the claims and concluded that some liability existed. Management have already settled these amounts and have concluded no further liability exists.

Management should ensure that independent valuations are obtained on a periodic basis for major capital projects to ensure that any volatility in the value reflected within the financial statements is minimised and that such major fixed asset additions are valued in accordance with the SORP upon completion.

Recommendation one

Investment properties

At 31 March 2008 the Partnership held investment properties with a value of £10.2 million. These include a number of concessions within subway and bus stations and units within Consort House. The SORP requires that investment properties are valued on an annual basis. The Partnership should ensure that arrangements are established to obtain appropriate valuations in accordance with the requirements of the SORP.

Recommendation two

Infrastructure assets

The 2007 SORP requires that infrastructure assets are held at historic cost. The Partnership has complied with this requirement in the financial statements for 2007-08. Currently a CIPFA/LASAAC working group on infrastructure accounting is discussing the future accounting treatment of infrastructure assets, the outcome of which may impact on future financial statements of the Partnership. The Partnership should ensure that it continues to monitor the progress of these discussions and adopts any changes to the required accounting treatment on a timely basis and in liaison with its external auditors.

Recommendation three

Rail franchise balances

At 31 March 2008, the Partnership held a net liability of £2.2 million due to Transport Scotland from transactions previously entered into by Strathclyde Passenger Transport Executive, some of them over a decade ago. These amounts have been outstanding for a number of years and are yet to be settled. Management have assured us that these balances are valid and recoverable and that the liability will be settled during 2008-09.

Recommendation four

Pension disclosures

The actuarial report provided on the Partnership's share of the assets and liabilities of Strathclyde Pension Fund at 31 March 2008 disclosed a pension asset of £6.8 million. This represents an improvement of £10.6 million from the £3.8 million deficit at 31 March 2007. Management has reviewed the assumptions and found these to be appropriate to the Partnership and are satisfied with the disclosure of a pension asset in the balance sheet in accordance with the actuary's advice. Additional payments were made to the Strathclyde Pension Fund in relation to early retirements. These payments will continue to be made for a number of years and a provision of £0.4 million has been made within the financial statements for this amount.

Post Balance Sheet Events

During May 2008, the GARL project was transferred from the Partnership to Transport Scotland. The GARL project was not a significant operation of the Partnership in terms of revenue and staffing, however, assets of £1.9 million, after impairment of £4.6 million as explained above, were held at 31 March 2008. The Partnership has disclosed this transfer of £1.9 million in its financial statements. The transfer agreement between the parties confirmed there would be no financial detriment to the Partnership.

Financial position

- The Partnership reported a deficit on the general fund balance for 2007-08 due to the utilisation of £4.8 million of general fund reserves to fund capital expenditure from revenue and an audit adjustment to create a provision for early retirements of £0.4 million. The revenue out-turn for the year was in line with budget before these adjustments. The general fund balance of the Partnership has decreased by £5.2 million to £13.6 million (2006-07; £18.8 million) due primarily to these adjustments.
- SCTSJC reported a deficit in 2007-08 of £735,000 against a budgeted deficit of £1,000,000. The deficit is primarily due to the Scottish Government debtor at 31 March 2007 not being recovered in full and a bad debt write off of £586,000 being required, offset by £851,000 of expected payments to bus operators not being made and lower overheads than anticipated. SCTSJC has a general fund balance of around £9.3 million (2006-07; £10 million) which has accumulated over a number of years.
- During 2007-08, the Partnership spent £52.6 million on capital projects. Expenditure for the year was in excess of budget due to the purchase of Consort House, offset to some extent by slippage in a few projects.
- At the 31 March 2008, the Partnership had short term investments of £23.6 million. This represented an increase of £8.8 million from the prior year.
- The budgeting process for 2009-10 is currently underway with the constituent authorities. The Scottish Government has set a Council Tax freeze for the authorities. In response to this the Partnership has set a 2% annual efficiency target going forward.

General fund

The Partnership reported a deficit on the general fund balance for 2007-08 due to the utilisation of £4.8 million of general fund reserves to fund capital expenditure from revenue and an audit adjustment to create a provision for early retirements of £0.4 million. The revenue out-turn for year was in line with budget before these adjustments.

	Actual £000
Income and expenditure result	
Net operating expenditure	48,161
Income: funding from constituent authorities and Scottish Government	(48,094)
(Surplus) / deficit to be met from balances b/forward	**67**
Loan repayments, capital financed from current revenue and fixed asset adjustments	5,123
Result for the year: (Increase) / decrease in general fund balance	**5,190**
Deducted from General fund balance brought forward on 1 April 2007	18,797
To arrive at General fund balance carried forward at 31 March 2008	**13,607**

SCTSJC reported a deficit in 2007-08 of £735,000 against a budgeted deficit of £1,000,000 for the year.

	Actual £000
Income and expenditure result	
Net operating expenditure	3,783
Income: funding from constituent councils	(3,048)
(Surplus) / deficit to be met from balances b/forward	**735**
Result for the year: (Increase) / decrease in general fund balance	**735**
Deducted from General fund balance brought forward on 1 April 2007	9,988
To arrive at General fund balance carried forward at 31 March 2008	**9,253**

The deficit is primarily due to the Scottish Government debtor at 31 March 2007 not being recovered in full and a bad debt write off of £586,000 being required, offset by £851,000 of expected payments to bus operators not being made and lower overheads than anticipated.

Reserves and balances

On 1 April 2007 the Partnership was required to amalgamate the fixed asset restatement account and the capital financing account to create a capital adjustment account in accordance with the 2007 SORP. The SORP also required a revaluation reserve to be created. The Partnership has created and appropriately utilised these reserves in accordance with the 2007 SORP.

The general fund balance of the Partnership has decreased by £5.2 million to £13.6 million (2007: £18.8 million) due primarily to the funding of capital expenditure from revenue of £4.8 million and the creation of a provision for early retirement costs of £0.4 million.

SCTSJC has a general fund balance of around £9.3 million (2007: £10 million) which has accumulated over a number of years. SCTSJC intends to return the excess reserves to the constituent local authorities through reducing requisitions in future years and utilising these reserves to fund the annual shortfall against expenditure. SCTSJC continue to hold significant liabilities (£745,000) due to bus operators who have yet to make a final claim for income due for financial years 2005-06 and earlier.

Capital investment programme and prudential borrowing

During 2007-08, the Partnership spent £52.6 million on capital projects. Expenditure for the year was in excess of budget due to the purchase of Consort House, offset to some extent by slippage in a few projects. Underspend against budget at 31 March 2008 were experienced in relation to the work at Partick station and the Glasgow Airport Rail Link.

The Partnership utilised the services of Glasgow City Council for short term treasury management until 2006-07. The Partnership now has full responsibility for its own treasury management function. The Partnership has complied with the prudential indicators set for the year.

At the 31 March 2008, the Partnership had short term investments of £23.6 million. This represented an increase of £8.8 million from the prior year. The majority of the balance has been earmarked for capital projects currently underway and the repayment of loans managed by Glasgow City Council amounting to £15 million at 31 March 2008. At 31 March 2008, capital commitments in excess of £6.7 million were disclosed, of this amount £1.4 million related to the GARL project which was transferred to Transport Scotland subsequent to the year end.

Future financial plans

A significant proportion of the funding for the Partnership is requisitioned from constituent local authorities. The budgeting process for 2009-10 is currently underway with the constituent local authorities. The Scottish Government has set a Council Tax freeze for the authorities. In response to this the Partnership has set a 2% annual efficiency target going forward.

The Partnership also receives funding directly from the Scottish Government. A ten year agreement is in place ensuring core funding will be available in future years. The Scottish Government may also make additional funding available for specific projects. The latest budgetary information for 2008-09 to July 2008 currently indicates a modest underspend for the period on revenue activities and an expected out-turn on budget.

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Corporate governance

- The Partnership's and SCTSJC's statement of internal financial control is in accordance with the 2007 SORP requirements and indicates no significant weaknesses. We have placed formal reliance upon the work of internal audit for 2007-08. The internal audit annual report concluded that *"reasonable assurance can be placed upon the adequacy and effectiveness of the Partnership's internal control systems in the year to 31 March 2008."*
- We reported 18 recommendations in our interim report, with one significant recommendation raised concerning business continuity and disaster recovery plans. In respect of Audit Scotland's Priorities and Risks Framework, we identified five areas where opportunities exist to enhance current arrangements. These were in respect of focussing on strategies, performance indicators, demonstrating Best Value and developing procurement practices in relation to e-procurement and the findings of the McClelland report. Internal audit has begun monitoring the implementation of recommendations made in internal and external audit reports.
- There were no material instances of fraud reported in 2007-08.
- Overall, we considered that the Partnership has adequate arrangements for managing obligations with respect to the National Fraud Initiative.

Introduction

Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all bodies.

Entities are responsible for establishing arrangements for ensuring the proper conduct of their affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. The Code requires auditors to review and report on corporate governance arrangements as they relate to:

- reviews of its systems of internal control, including its reporting arrangements;
- the prevention and detection of fraud and irregularity; and
- standards of conduct and arrangements for the prevention and detection of corruption.

Structural reorganisation

A major review of the Partnership's activities was commissioned in May 2006. This identified a need for significant change including structural reorganisation. During 2007-08 this re-organisation was completed with a small number of early retirements to facilitate the changes, provision has been made in the financial statements for the additional pension payments to these individuals.

Systems of internal control

Statement on internal financial control ("SIFC")

SCTSJC utilises the systems and controls of the Partnership in carrying out its business. SCTSJC has therefore included a Statement of System of Internal Financial Control which explains this and reproduces the content of the Partnership's statement. The Statement of System of Internal Financial Control prepared by the Partnership reflects, in accordance with the 2007 SORP, the systems and controls in place. In addition to this statement, Corporate Governance Statements have been prepared providing further information on the Partnership and SCTSJC's control environment.

The Partnership has established operational risk registers and has a strategic level risks register which are reviewed on a periodic basis. Management continues to work to ensure that risk is fully embedded within the organisations and that the risk registers remain 'live' documents.

Internal audit

During 2007-08 internal audit planned to complete reviews in respect of a number of areas directly relevant to governance arrangements and systems of control. Similar to 2006-07 we have completed an evaluation of the internal audit service in order to inform our approach in terms of reliance. This has allowed us to take into account internal audit's findings and conclusions in our work. In our annual audit plan we identified that work in respect of risk management, payroll, value for money, debtors, budgetary control, subway station visits and travel centre visits was relevant to our own responsibilities and have placed reliance on this work, where appropriate. The annual assurance statement by internal audit concluded that *"reasonable assurance can be placed upon the adequacy and effectiveness of the Partnership's internal control systems in the year to 31 March 2008."*

Internal controls

Drawing on the work of internal audit, in accordance with our plan, we completed detailed testing in relation to organisation-wide, IT controls and key financial controls. Our work on organisation-wide and IT controls included consideration of financial reporting, risk management, information systems and communication, and the general tone and conduct set by the Partnership's leaders. We utilised Audit Scotland's *Priorities and Risks Framework* in the completion of this work. Our key financial controls work considered the principal accounting systems to assess whether the related controls were designed appropriately and operating effectively to prevent or detect a material misstatement of the financial statements. The findings of this work were reported in the interim management report on 28 March 2008.

In respect of the Partnership's corporate governance arrangements while we found that these provide an effective framework for the governance of the Partnership, we made some recommendations aimed at improving these arrangements. We made one recommendation noting that the members' register of interests was not complete at the time of our interim audit visit. In respect of Audit Scotland's *Priorities and Risks Framework*, we identified five areas where opportunities exist to enhance current arrangements. These were in respect of focussing on strategies, performance indicators, demonstrating Best Value and developing procurement practices in relation to e-procurement and the findings of the McClelland report.

Our review of the IT control environment identified one significant risk in respect of business continuity due to the lack of a disaster recovery plan and five other recommendations. Our work over the key financial systems found no significant issues with six recommendations made.

The implementation of audit recommendations, from both internal and external audit reports, is being monitored by the internal audit function. It is management's intention that progress will be reported to the audit and standards committee on a periodic basis.

Prevention and detection of fraud and irregularity

There is a formal whistle-blowing policy governing the procedures to be followed in the event of a fraud or suspected fraud. Where management are made aware of a suspected fraud, procedures are in place to co-ordinate an investigation. During 2007-08 written fraud procedures were updated following the creation of the Partnership and fully publicised to all staff. There were no material instances of fraud or irregularity reported during 2007-08.

National Fraud Initiative

NFI brings together data from, councils, police and fire and rescue boards, health bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud and payroll fraud. The Partnership provided payroll data for the exercise. The NFI has generated significant savings for Scottish public bodies, but if fraud or overpayments are not identified, assurances may be taken about internal arrangements for preventing and detecting fraud. Participating bodies follow up the matches, as appropriate, and record the outcomes of their investigations in the application.

The overpayments and savings identified by participating bodies in Scotland during the 2006-07 exercise is currently £9.7 million. This is likely to increase in the months ahead as bodies complete their follow up work. Guidance was issued in April 2008 to outline the requirements for data preparation and submission for inclusion in the 2008-09 NFI exercise which commences on 6 October 2008.

The NFI 2006-07 results (data matches) were made available via a new secure web-based application. Participating bodies follow up the matches, as appropriate, and record the outcomes of their investigations in the application. We monitored the Partnership's involvement in NFI during the course of the 2006-07 audit, and updated our understanding of the status of investigations into data matches as part of our interim audit visit in January 2008. Our responsibilities in relation to the NFI exercise include completing a questionnaire evaluating the Partnership's response to NFI and sample testing of cleared matches, which was submitted to Audit Scotland in February 2008

The Partnership has investigated all of the matches from the 2006-07 NFI exercise, updated the online records and reported progress to their audit and standards committee. Testing of the matches found that appropriate action had been taken by the Partnership and evidence obtained to support the conclusions made. Overall, we considered that the Partnership has adequate arrangements in place for managing obligations with respect to NFI.

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Standards of conduct

There exists a Code of Conduct for members and staff which is provided to all new employees and is available on the intranet. Also available on the intranet are comprehensive human resources policies and procedures providing additional guidance to staff.

There is a formal register of interests for recording board members and senior managers' interests. This is regarded as best practice and assists in demonstrating consideration of independence in decision-making and the awarding of contracts. We noted in our interim report, that this required to be updated for the new members subsequent to the local government elections in May 2007; all members have since updated their disclosure.

Impact of May 2007 elections

We have reviewed the impact of the local authority elections in May 2007. This resulted in a number of new members being appointed to the Partnership board by constituent local authorities. The Partnership provided training to all new members including specific training on the roles of each committee.

Financial statements review

The financial statements for 2007-08 were not considered by the audit and standards committee prior to their presentation to a meeting of the Partnership for approval. This is not in line with the terms of reference of the audit and standards committee which requires that (amongst other things) "the committee is satisfied that the Partnership's assurance statements including the Statement on Internal Controls properly reflect the risk environment …and to review the financial statements". In addition, this practice is not in compliance with the principles of good corporate governance.

Recommendation five

Performance management

- During 2007-08, the internal audit department completed three value for money audits. These reports resulted in a number of recommendations to management relating to the formal contracts and reviews of the services.
- The head of organisational development has been charged with co-ordinating a number of Best Value initiatives going forwards.
- No specific requirements have been made of the Partnership in respect of efficient government targets. However, we understand that in response to the council tax freeze and other financial pressures on the constituent local authorities that a 2% efficiency target has been set for future revenue budgets.

The Code requires that, in accordance with guidance provided by Audit Scotland, we consider the Partnership's arrangements in relation to Best Value and other aspects of the arrangements to manage performance in relation to economy, efficiency and effectiveness in the use of resources.

The responsibility to ensure that the Partnership has appropriate arrangements in place to manage and monitor performance lies with management and the members of SPT and SCTSJC.

Best Value

The Local Government in Scotland Act 2003 introduced new statutory duties relating to Best Value and community planning. As a result, the Accounts Commission introduced new arrangements for the audit of Best Value. Audit Scotland has intimated that they will not be subjecting the Partnership to a review during the five year appointment of KPMG as external auditors, however, the Partnership should ensure that the arrangements in place are appropriate.

During 2007-08, the internal audit department, upon request from management, completed three value for money audits to identify scope for improved economy, efficiency and effectiveness in relation to catering, cycle lockers and provision of a bus for subway staff. These reports resulted in a number of recommendations to management relating to the formal contracts and reviews of the services. The head of organisational development has been charged with co-ordinating a number of Best Value initiatives going forwards.

Efficient government

The efficient government initiative is a five-year programme with the aim of tackling waste, bureaucracy and duplication in Scotland's public sector. No specific requirements have been made of the Partnership and management are considering how best to embrace the efficient government agenda and establish a clear programme for delivering efficiency savings. We understand that in response to the council tax freeze and other financial pressures on the constituent local authorities that a 2% efficiency target has been set for future revenue budgets.

Appendix 1 – action plan

Priority rating for performance improvement observations raised		
Grade 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.	**Grade 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.	**Grade 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 be of benefit to you if introduced.

No.	Issue and performance improvement observation	Management response	Officer and due date
1	The Partick station and Croy park-and ride projects remained Assets Under Construction at 31 March 2008 pending completion. Management should ensure that independent valuations are obtained on a periodic basis for major capital projects to ensure that any volatility in the value reflected within the financial statements is minimised and that such major fixed asset additions are valued in accordance with the SORP upon completion. *(Grade two)*	Such valuations have been regularly obtained for the Partick station project. This practice will be extended to other significant capital projects undertaken by the Partnership	Director of Finance / Director of Operations Immediate
2	At 31 March 2008 the Partnership held investment properties with a value of £10.2 million. These include a number of concessions within subway and bus stations and units within Consort House. The SORP requires that investment properties are valued on an annual basis. The Partnership should ensure that arrangements are established to obtain appropriate valuations in accordance with the requirements of the SORP. *(Grade two)*	Agreed.	Director of Property and Asset Management 31 March 2009

No.	Issue and performance improvement observation	Management response	Officer and due date
3	Currently a CIPFA/LASAAC working group on infrastructure accounting is discussing the future accounting treatment of infrastructure assets, the outcome of which may impact on future financial statements of the Partnership. The Partnership should ensure that it continues to monitor the progress of these discussions and adopts any changes to the required accounting treatment on a timely basis and in liaison with its external auditors. *(Grade two)*	Agreed.	Director of Finance Immediate
4	At 31 March 2008, the Partnership held a net liability of £2.2million due to Transport Scotland from transactions previously entered into by Strathclyde Passenger Transport Executive, some of them over a decade ago. These amounts have been outstanding for a number of years and are yet to be settled. Management have assured us that these balances are valid and that the liability will be settled during 2008-09. The Partnership should ensure that these are addressed and settled within the current financial year. *(Grade two)*	The Partnership will engage with Transport Scotland to seek settlement of these balances in 2008-09.	Director of Finance 31 March 2009
5	In accordance with good corporate governance practice and the terms of reference of the audit and standards committee, management should ensure that the Partnership 's financial statements and associated documentation are subject to consideration by the audit and standards committee prior to review and approval at a formal meeting of the Partnership. *(Grade one)*	Agreed.	Director of Finance 30 September 2009

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