KPMG

INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee

Annual audit report to the members and the Controller of Audit

Year ended 31 March 2009

29 September 2009

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

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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").

This report 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 scope and objectives 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

Financial statements

We have issued unqualified opinions on the financial statements of SPT and SCTSJC.

We have provided an update on the areas of audit emphasis which were identified in our annual audit plan and interim report in addition to an explanation of the accounting treatment and audit adjustments relating to specific areas of audit emphasis identified during our final audit work. We have recommended that the Partnership establish a plan and timetable to prepare for the implementation of International Financial Reporting Standards.

Use of resources

Total expenditure in support of the capital programme amounted to £27.862 million. The capital programme was funded by £26.807 million of Scottish Government capital grant. The GARL project formally transferred to Transport Scotland on 23 May 2008. All costs incurred in 2008-09 (£0.944 million) were funded by grant from Transport Scotland and hence there was no net cost attributable to SPT.

A revenue budget of £47.642 million has been agreed for 2009-10 and performance is monitored monthly by the strategy and programmes committee with reports also presented to the Partnership. The Partnership has considered the impact of the current economic climate as part of the budget setting process for 2009-10 and 2010-11.

Financial stability proposals were presented to the Partnership at a meeting on 12 December 2008 which addressed the forecast budget deficit of £500,000 for 2009-10 and £2.5 million in 2010-11. A subsequent report by the chief executive was presented to the Partnership on 12 June 2009 and provided an update on the status of these recommendations. The report made further proposals for operational sustainability and financial stability in the context of the economic climate.

Governance and accountability

Internal audit has completed their agreed plan for the year and 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 2009.

The majority of key financial controls are designed appropriately and operating effectively.

The Partnership's governance manual was updated in November 2008. This included the procedural standing orders, contract standing orders, financial regulations, scheme of financial and non-financial delegations, codes of conduct, anti-fraud and whistle blowing policies.

The Partnership has a fraud and irregularities response plan. This sets out what to do if a fraud or any other irregularity is suspected. There were three whistle blowing allegations which were investigated by internal audit and satisfactorily resolved. There was no material instances of fraud reported during 2008-09.

Internal audit reported on their investigation of a number of National Fraud Initiative matches in the year and concluded that there were no instances of fraud or error.

Performance

During 2008-09, the internal audit department, upon request from management, completed a number of value for money audits to identify scope for improved economy, efficiency and effectiveness in relation to subway stores, travel and subsistence, procurement and an updated on the provision of a bus for subway staff.

Scope

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice* ("the *Code*"). This specifies a number of objectives for our audit.

The Accounts Commission appointed KPMG LLP as auditors of Strathclyde Partnership for Transport ("SPT") and Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC") under the Local Government (Scotland) Act 1973 ("the Act"). For the purposes of this report these bodies are referred to collectively as "the Partnership". The period of appointment is 2006-07 to 2010-11, inclusive. This document summarises our responsibilities as external auditors for the year ended 31 March 2009 and our approach to issues impacting the Partnership's activities in that year.

We carry out our audit in accordance with our statutory responsibilities under the Act and in accordance with the International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board ("APB") and the wider responsibilities embodied in Audit Scotland's *Code of Audit Practice* ("the *Code*"). Under this *Code* auditors address and comment upon a number of objectives, together with complying with a number of obligations. The *Code* also places a number of obligations on the Partnership.

Auditors' objectives in relation to the *Code* are to:

- provide an opinion whether the financial statements present a true and fair view, in accordance with applicable laws and regulations and the Code of Practice on Local Authority Accounting in the United Kingdom: a Statement of Recommended Practice ("SORP 2008") and whether the financial statements have been properly prepared in accordance with the Local Government (Scotland) Act 1973.
- review and report on (as required by relevant legislation, the *Code* and any guidance issued by Audit Scotland):
  - the Partnership's corporate governance arrangements as they relate to: its 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 arrangements to achieve Best Value
  - other aspects of the Partnership's arrangements to manage its performance, as they relate to economy, efficiency and effectiveness in the use of resources.

We outlined the framework under which we operate, under appointment by the Accounts Commission, in the audit plan overview discussed with the audit committee on 27 March 2009.

The purpose of this report is to report our findings as they relate to:

- the **financial statements** and significant accounting matters and decisions;
- **use of resources**, including financial outturn for the year ended 31 March 2009 and financial plans for 2009-10 and beyond;
- arrangements around **governance and accountability**, including risk management, systems of internal control and our consideration of the work of internal audit; and
- **performance management arrangements.**

Scope (continued)

Best Value

Audit Scotland and the Scottish Government have been committed to extending the Best Value audit regime across the whole public sector for some time now, with significant amounts of development work having taken place during the last year. Using the Scottish Executive's nine Best Value principles as the basis for audit activity, Audit Scotland selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working). Audit Scotland is developing a series of toolkits that auditors are using from 2008-09. As we reported in our audit plan overview, discussed with the audit committee on 27 March 2009, Audit Scotland has confirmed that they will not subject the Partnership to a Best Value inspection during our five-year appointment as external auditors.

Responsibilities of the Partnership and its auditors

External auditors do not act as a substitute for the Partnership's own responsibilities for putting in place proper arrangements to account for the 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 the accountable officer, to make arrangements to secure Best Value.

Action plan

This report includes an action plan containing areas for development or improvement identified during our financial statements audit fieldwork. We have not repeated recommendations raised in reports issued during our earlier work in respect of our 2008-09 audit. Responsibility for taking action and monitoring progress in response to all our recommendations lies with management.

Acknowledgement

We wish to record our appreciation of the continued co-operation and assistance extended to us by your staff during the course of our work.

Financial Statements

We have issued an unqualified opinion on the financial statements of SPT and SCTSJC.

Key issues arising from our audit of the financial statements are:

- Partick station – the redevelopment of Partick station was completed during the year at a cost of £17.3 million, including the settlement of contractor claims for additional payments. Following the audit process, the station was subject to valuation by the district valuer which resulted in a reduction in the carrying value to £11.1 million.
- Croy station – a decision was taken in January 2009 to pursue the option of a surface level car park at Croy rather than a multi-story car park. As a result of this decision £5.9 million is due to be repaid to the Partnership by the project partners.
- High Street land – land at High Street had been included in the financial statements at a market value of £5 million based on a report which SPT had received previously. Following discussion with management, it was agreed that, in the current economic climate an updated valuation was required. This resulted in a reduction in value to £3 million.
- Transport Scotland – following discussions between the Partnership and Transport Scotland a decision was taken to write-off a net creditor of £2.2 million due to Transport Scotland as at 31 March 2009, resulting in a corresponding increase to income.
- Debt rescheduling – in addition to scheduled debt repayments, it was agreed that an additional £25 million would be repaid. Associated breakage costs of £1.8 million were incurred. The Partnership has chosen to fully expense these in 2008-09 as allowed by applicable guidance. It is anticipated that future benefits, as a result of the debt rescheduling, will be utilised as part of a subway modernisation fund.

Recommendations

The action plan includes recommendations to improve the following areas.

Area for development	Action plan reference
It is important that the Partnership obtains consent to increase reserves, otherwise planned future savings may be repayable to constituent local authorities.	One
A plan and timetable is required to ensure the effective implementation of International Financial Reporting Standards.	Two

Audit opinions and key issues

Reporting arrangements and timetable

In accordance with management's timetable and the audit plan overview discussed with the audit committee on 27 March 2009, draft financial statements for SPT and SCTSJC were available for audit on 8 June 2009 on commencement of the related audit fieldwork. Management included an initial version of the accompanying narrative statements at that time.

The financial statements were substantially complete at that time.

Audit opinion

We have issued an unqualified opinion on the financial statements of SPT and SCTSJC for the year ended 31 March 2009.

Key issues arising during our audit of the financial statements

Our audit plan overview and interim management report identified five areas of audit emphasis, which are summarised below.

Audit issue	Conclusions
Voluntary severance	We previously discussed the voluntary severance scheme with management and understand that over 70 expressions of interest were received. The scheme closing date was 6 February 2009. Following evaluation of eligibility and acceptance of applications by management, 23 individuals were made offers of severance settlements in the year, 21 accepted and 2 withdrew. The total cost of severance was £0.5 million, including pension costs. None of the 21 employees had left the Partnership by 31 March 2009 therefore we confirmed that the total costs had been accrued and were included within staff costs for 2008-09. We understand that a requirement of the approved scheme was that staff would cease employment by June 2009. We confirmed that the majority of individuals approved had left by this deadline and the costs accrued at year end were therefore correctly calculated based on their leaving dates.
Fixed assets	*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 2008 requires that investment properties are subject to annual valuation. We met with the Partnership's internal valuer during our interim visit and confirmed that whilst no formal instructions were issued by management to the valuer, a valuation of investment properties was to be completed in accordance with SORP 2008 as at 31 March 2009. At year end we obtained the valuation report produced by the directors. This resulted in a net increase in value.

Audit opinions and key issues (continued)

Audit issue	Conclusions
Accounting for reserves	Section 3 of the Transport Scotland (Act) 2006 requires that, similar to other Regional Transport Authorities, constituent local authorities meet only the Partnership's net expenses (i.e. 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, did not agree with this interpretation of the Act and continues to press for a change to the legislation with the Scottish Government during 2009-10. For 2008-09 the Partnership has reported a reduction in the general reserve. However, following the early repayment of debt during 2008-09, which is expected to continue in 2009-10, the Partnership at their meeting on 13 February 2009 reported that the savings of £20 million achieved over the next eight years would be diverted to an earmarked subway modernisation fund. It is important that the Partnership obtains consent to increase reserves or identifies an alternative means of 'carrying' these savings. ***Recommendation one***
Assets under construction	The Croy park-and-ride and Partick station projects remained assets under construction at 31 March 2008, pending completion. *Croy park-and-ride* The strategy and programmes committee approved the option of considering a surface level car park instead of the originally proposed mutli-story car park on 30 January 2009. This resulted in the termination of the existing grant awarded to First Scotrail. As a result £5.9 million, which had been advanced for the project, is due to be repaid to the Partnership by First Scotrail. *Partick station* At Partick, the station development opened to the public on 15 March 2009. There was a contractor claim relating to the project which was subject to two adjudications. A settlement of £14.8 million was agreed between the contractor and the Partnership as the final contractor cost, compared with the original contractor budget of £12.3 which included a contractor cost of £9.8 million. We reviewed the adjudications and discussed the costs incurred with management and are satisfied that the costs have been correctly capitalised in accordance with the SORP 2008 and FRS 15. Furthermore we requested that management review the completed asset for indicators of impairment and obtain an up to date valuation as at 31 March 2009 to support the valuation in the financial statements. The district valuer reported a value as at 31 March 2009 of £11.1 million. This resulted in an impairment charge of £6.2 million.
Scottish government transactions	The Partnership received £25 million of funding from the Scottish Government in early 2009 and agreed to use these funds to redeem part of their debt with Glasgow City Council. As a result, associated breakage costs of £1.8 million were incurred. In line with relevant guidance the Partnership elected to expense these costs in full in 2008-09.

Audit opinions and key issues (continued)

We identified a number of areas of audit emphasis during our audit of the financial statements in previous years and during the current year and provide an update in respect of these areas:

Glasgow Airport Rail Link

The Glasgow Airport Rail Link ("GARL") project formally transferred to Transport Scotland on 23 May 2008. All costs incurred in 2008-09 were funded by grant from Transport Scotland and hence no net cost was attributed to SPT. No further transactions or balances are held in respect of GARL.

FRS17 (amended)

The amendment to FRS 17 'retirement benefits' has been adopted in 2008-09 by the Partnership for the first time and updated disclosures have been provided as required. The amendment to FRS17 requires that quoted securities are valued at their current bid price rather than their mid-market value. No adjustment has been applied to the comparative figures as the directors consider the effect of this change not to be material to the financial statements.

Rail franchise balances

We previously reported that SPT 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. Following confirmation from Transport Scotland that no balances were now due to be paid as at 31 March 2009, management wrote this balance back with a corresponding increase to income.

Implementation of International Financial Reporting Standards

In our audit plan overview presented to the audit committee on 27 March 2009 we explained that in October 2008 CIPFA/LASAAC announced a new governance framework for the Code of Practice on Local Authority Accounting which will require financial statements to be prepared under International Financial Reporting Standards ("IFRS") for the first time in 2010-11.

CIPFA/LASAAC has now also issued the IFRS-based code of practice on local authority accounting – update 3 and an exposure draft for comment. On 23 April 2009, CIPFA/LAAP issued a bulletin which set out some key issues in respect of preparing for IFRS which advised that bodies reporting under the local government framework:

- reassess their PFI schemes in time for the revised accounting treatment to be adopted in their 2009-10 financial statements. This will involve restating the 2008-09 financial statements, and authorities may find that collecting the required information in parallel with that required to close the 2008-09 financial statements simplifies the process.
- collect information on untaken annual leave and other short-term employee benefits at 31 March 2009 as part of their 2008-09 close-down arrangements.
- collect the necessary information to allow leases to be split between land and buildings as soon as possible, bearing in mind that non-finance staff (e.g. valuers and legal staff) are likely to have an essential role in this process.
- discuss with their valuers which assets are likely to have a material difference between their current carrying value and their fair value, and ensure a programme to identify those assets is in place. It should be noted that the draft Code of Practice on Local Authority Accounting does not require separate components to be identified in the opening IFRS balance sheet and comparative figures (except where authorities have already separately identified components under the SORP). Separate components will need to be identified, where these are significant and have a different asset life to the rest of the asset, as assets and components are acquired, enhanced and revalued from 1 April 2010 onwards.

Date	Publications
3 March 2009	CIPFA/LAAP bulletin 80 sets out a detailed project plan and timetable for the implementation of IFRS.
23 April 2009	CIPFA/LAAP bulletin 81 on closure of 2008-09 accounts includes advice on preparing for implementation of IFRS
11 May 2009	CIPFA/LASAAC issued IFRS-based code of practice on local authority accounting update 3 together with draft code in respect of a number of accounting areas.
16 July 2009	CIPFA/LASAAC issued IFRS-based code of practice on local authority accounting – exposure draft

We have advised management of the need to put in place a plan and timetable to ensure the Partnership is ready for the conversion to IFRS and that key accounting judgements are considered early. This will ensure that expert advice can be taken as necessary and that any deadlines are achieved.

Recommendation two

Use of resources

The Partnership's core revenue budget was determined at a meeting of the strategy and programmes committee on 25 January 2008 as £47.230 million of which £37.306 million was financed by receipts from constituent local authorities and the remaining £9.924 million by Scottish Government grant.

The outturn for the year was in line with budget before the accelerated debt repayment and audit adjustments in respect of a net creditor of £2.2 million which was written back and the recognition of breakage costs of £1.8 million.

Total expenditure in support of the capital programme amounted to £27.862 million. The capital programme was funded by £26.807 million of Scottish Government general capital grant. The GARL project formally transferred to Transport Scotland on 23 May 2008. All costs incurred in 2008-09 (£0.944 million) were funded by grant from Transport Scotland and hence no net cost was attributed to SPT.

A revenue budget of £47.642 million has been agreed for 2009-10 and performance is monitored monthly by the strategy and programmes committee with reports also presented to the Partnership. The Partnership has considered the impact of the current economic climate as part of the budget setting process for 2009-10 and 2010-11.

Financial stability proposals were presented to the Partnership at a meeting on 12 December 2008 which addressed the forecast budget deficit of £500,000 for 2009-10 and £2.5 million in 2010-11. A subsequent report by the chief executive was presented to the Partnership on 12 June 2009 and provided an update on the status of these recommendations. The report made further proposals for operational sustainability and financial stability in the current economic climate

Recommendations

We did not identify any significant recommendations for development of the Partnership's arrangements to manage its use of resources.

Financial management

Financial position

The Partnership core revenue budget was determined at a meeting of the strategy and programmes committee on 25 January 2008 and subsequently approved by the Partnership as £47.230 million of which £37.306 million was financed by receipts from constituent local authorities and the remaining £9.924 million by Scottish Government grant. It is set at a high level and monitored throughout the year in order to manage any significant under / over spends by the strategy and programmes committee.

A significant increase in the Scottish Government grant income to £33.070 million was as a result of accelerated funding. Management agreed with the Scottish Government that this would be primarily used to redeem debt which is managed on behalf of the Partnership by Glasgow City Council. It was agreed that an additional £25 million would be repaid in respect of 2008-09 with associated breakage costs of £1.8 million.

The outturn for the year was in line with budget before the accelerated debt repayment and audit adjustments in respect of a net creditor of £2.2 million which was written back and the recognition of breakage costs of £1.8 million.

Income and Expenditure account	£'000
Net cost of services	38,600
Interest payable and similar charges	4,270
Interest receivable	(1,426)
Pension cost and expected return on assets	(747)
Net operating expenditure	**40,697**
Funding received from constituent councils	(37,306)
Funding from Scottish Government	(33,070)
Deficit / (surplus) for the year	**(29,679)**

Statement of movement on the General Fund Balance	£'000
Deficit / (surplus) for the year	**(29,679)**
Net additional amount required by statute to be debited or credited to the general fund balance for the year	30,759
Decrease in general fund balance for the year	1,080
General fund balance brought forward	(13,607)
General fund balance carried forward	**(12,527)**

Capital programme

Total expenditure in support of the capital programme amounted to £27.862 million. The programme was funded by £26.807 million of Scottish Government grant and Transport Scotland specific grant of £0.944 million in support of the Glasgow Airport Rail Link (GARL). A funding arrangement of £3.689 million with other Regional Transport Partnerships was entered into in 2007-08. In 2008-09 £1.8 million was returned with £1.889 million still outstanding by SPT at 31 March 2009. This will be returned at a time agreed between the respective bodies.

As noted in 2007-08, the GARL project formally transferred to Transport Scotland on 23 May 2008. All costs incurred in 2008-09 (£0.944 million) were funded by grant from Transport Scotland, with no net cost attributable to SPT. A related purchase of a private company, Airlink Security Park Limited, took place in 2007-08. The company was liquidated in 2008-09 with no transactions occurring under SPT's stewardship.

Financial management (continued)

Financial planning

Financial planning

A revenue budget of £47.642 million has been agreed for 2009-10 and performance is monitored monthly by the strategy and programmes committee with reports also presented to the Partnership. The 2009-10 operating plan outlines SPT's goals and strategic priorities and reflects the Regional Transport Strategy. The plan also highlighted SPT's key performance indicators and tracking indicators together with appropriate targets and measures, taking into account resources available for deliverability.

Current economic climate

The Partnership has considered the impact of the current economic climate as part of the budget setting process for 2009-10 and 2010-11. Financial stability proposals were presented to the Partnership at a meeting on 12 December 2008 which addressed the forecast budget deficit of £500,000 for 2009-10 and £2.5 million in 2010-11. The key drivers behind these increased costs were explained to be increased power costs, pensions and bus operating costs as a result of fuel prices. At the same time it was recognised that there was a decrease in the level of investment income due to falling interest rates.

The Partnership agreed a number of actions to address the budget shortfall in 2009-10 and proposals for reviews to identify savings and efficiencies for 2010-11. A subsequent report by the chief executive was presented to the Partnership on 12 June 2009 which provided an update on the status of these recommendations. (Progress is summarised below).

The report made further proposals for operational sustainability and financial stability in the current economic climate. SPT currently requisitions £38.3 million from constituent local authorities to deliver its services with further funding from the Scottish Government. In addition, £33.7 million is requisitioned to cover the cost of agency services delivered on behalf of local authorities such as school travel. A further £30 million is due in 2009-10 to fund capital expenditure which is expected to reduce to £20 million in 2010-11.

A number of financial and operational pressures were identified:

- a reduction in income from patronage on the Subway and increasing rolling stock maintenance costs;
- a pay award and associated employer costs in 2010-11 consistent with prior years would increase costs by £1.2 million; and
- ongoing pressure to deliver more subsidised bus services.

To address each of these pressures, a number of actions were proposed to ensure the longer term financial and operational capability of the organisation in the current economic environment. These included:

- a freeze on vacancies;
- a review of all temporary staffed posts;
- investigating and developing a business case to support future borrowing for replacement of the subway rolling stock with a modern equivalent which would reduce the level of maintenance costs;
- continued and focussed consultation with trade unions on a review of the terms and conditions of all staff to ensure they are modern, flexible, and are able to deliver the needs of the public;
- further development of the use of the capital funding to support 'spend to save' initiatives consistent with the recent bus fleet procurement; and
- active engagement with partners on the shared service agenda.

Financial management (continued)

Action Agreed December 2008	Status at 12 June 2009
Introduction of a voluntary severance scheme	Complete
General freeze on recruitment	Completed with only essential appointments being approved
Subway efficiency plan and review of operations and spares	In progress
Review of ferry opening hours and savings from new vessels	In progress
Bus restructuring and précis process	In progress
Review of travel centres	Complete
Review of capital project staffing and charging	Complete
Secure early capital receipts	On hold due to current market conditions
Reduction in communications budget	Complete
Review of advertising contract	In progress
Review of HR and OD structure to generate £50k	Due 1 April 2010
Review affordability of diversity champion	Complete (reduction from full-time to part-time agreed)
Technology solutions to deliver an efficiency plan	Early fixes implemented. Longer term developments to be included in future capital plan
Second internally to full posts	Complete
Agree travel planning capability	Complete (reduced from 3 FTE to 2 FTE)
Reduction in all supply lines	In progress
Finance – capture benefits from procurement review	In progress (corporate-wide procurement policy introduced)
Efficiency savings of 1 FTE as a result of new FMS implementation	Due 1 April 2010
Review of special projects unit	In progress
Increase zonecard scheme administration fee	Due as part of 2010/11 budget process

Source: Strathclyde Partnership for Transport

Governance and accountability

The statement on internal control does not disclose any significant weaknesses. The content of the statement is consistent with our understanding of the Partnership.

Internal audit has completed their agreed plan for the year and 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 2009.

The majority of key financial controls are designed appropriately and operating effectively.

The governance manual was updated in November 2008. This included the procedural standing orders, contract standing orders, financial regulations, scheme of financial and non-financial delegations, codes of conduct, anti-fraud and whistle blowing policies.

The Partnership has a fraud and irregularities response plan. This sets out what to do if fraud or any other irregularity is suspected. There were three whistle blowing allegations which were investigated by internal audit and satisfactorily resolved. There was no material instances of fraud reported during 2008-09.

Internal audit reported on their investigation into a number of National Fraud Initiative matches in the year and concluded that there were no instances of fraud or error.

Recommendations

We did not identify any significant recommendations for development in respect of the Partnership's governance and accountability arrangements.

Corporate governance arrangements

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 its 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:

- the Partnership's 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.

Governance framework

The Regional Transport Strategy, 'A Catalyst for Change 2008-2021' was approved and provided to the Scottish Government by 31 March 2008 as required by the Transport (Scotland) Act 2005. It forms the basis of the Partnership's activity. The Partnership appoints between seven and nine of the executive board members with the permission of the Scottish Government with a further 20 elected members appointed from the 12 constituent local authorities. This is in line with the standing orders of the Partnership and Transport (Scotland) Act 2005.

At a meeting on 14 November 2008, the Partnership approved a number of policies which form its governance manual. This included the procedural standing orders, contract standing orders, financial regulations, scheme of financial and non-financial delegations, codes of conduct, anti-fraud and whistle blowing policies. The updated scheme of delegation took account of the revised operational structure of the Partnership following the changes in 2007-08. The governance manual, once approved, was provided to all members, directors and senior managers and is available to all other staff through the intranet.

The financial regulations include guidance on how to contribute to a positive control environment, procedures for identifying risks and responsibilities for establishing adequate controls and procedures to mitigate those risks.

The Partnership also approved the terms of reference for the following committees:

- chairs committee;
- strategy and programmes committee;
- operations committee;
- personnel appeals sub-committee;
- audit and standards committee; and
- personnel committee.

We have considered the corporate governance arrangements, which, combined with the work of internal audit, has allowed us to concluded that the corporate governance framework has been designed and implemented appropriately.

Corporate governance arrangements (continued)

Systems of internal control

Statement of systems of internal financial control

The statement for 2008-09 provides details of the internal control environment and risk management and control framework. Management highlights that the system of internal control is based on a framework of guidance and regular management information, financial regulations, administrative and authorisation procedures, management supervision and a system of delegation and accountability. The statement identifies that it is informed by officers throughout SPT and the audit and standards committee as the scrutiny committee and by the work of internal and external audit.

SCTSJC utilises the systems and controls of SPT 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 SPT's statement.

Internal audit

Our planned audit approach seeks, wherever possible, to place reliance on the work completed by internal audit to minimise duplication of effort and ensure maximum benefit from the combined audit resource. In accordance with our audit plan overview we placed reliance on the following areas of work audited internally;

- treasury management;
- rental and subway income;
- other income;
- procurement; and
- regularity and value for money audits.

We also visited a travel centre and subway station with internal audit to understand their inspection role.

Internal audit's annual report, submitted to the audit and standards committee at their meeting on 12 June 2009 noted that liaison with KPMG allowed us to place continued reliance on the work of internal audit. In respect of the Partnership's control environment it 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 2009'.*

Corporate governance arrangements (continued)

Internal controls

Our interim management report submitted to the audit and standards committee on 12 June 2009 reported that

- in respect of organisation-wide controls:
  - six previously made IT recommendations were either partially implemented or had yet to be implemented; and
  - one new recommendation in respect of user administration procedures was made.
- in respect of key financial controls:
  - we made 12 recommendations – the key theme of our recommendations focused on the need for management to make improvements in the evidencing of management review of controls. One of these recommendations was graded as 'significant'.

Our testing, combined with that of internal audit, over the design and operation of controls over significant risk points confirms that, with the exception of some minor weaknesses, controls are designed appropriately and operating effectively.

Corporate governance arrangements (continued)

Corporate risk register

The corporate risk register was developed by the risk management group in 2007. It is regularly updated by responsible officers forming part of the risk management group and updates are presented at least quarterly to the audit and standards committee. Key risks added during 2008-09 include the global financial crisis, staff morale as a result of the voluntary severance scheme and the impact of the swine flu pandemic.

Prevention and detection of fraud and irregularity

The financial regulations approved by the audit and standards committee on 14 November 2008 state that;

'The Assistant Chief Executive (Business Support) must ensure the Partnership has an effective ant-fraud and corruption policy. It should be backed up by a culture that does not tolerate fraud or corruption'; and

'The Assistant Chief Executive (Business Support) must ensure that the Partnership has effective whistle blowing procedures'.

An anti-fraud strategy is in place. This sets out what to do if fraud or any other irregularity is suspected. The strategy forms part of the Partnership's procedures for handling suspicions, allegations or evidence of fraud or other irregularities. It includes a fraud response plan.

There is a formal whistle blowing policy governing the procedures to be followed in the event of a fraud or suspected fraud. We have considered the policy against the Public Interest Disclosure Act requirements and the Public Concern at Work: Best Practice notes and not identified any significant variations.

Any significant frauds arising are reported to the audit and standards committee. During 2008-09 there were three whistle blowing allegations which were investigated by internal audit.

There were no material instances of fraud reported during 2008-09.

National Fraud Initiative

The National Fraud Initiative brings together data from councils, health bodies, police and fire and rescue boards and other agencies, to help identify and prevent a wide range of frauds against the public sector. These include, occupational pension fraud and payroll fraud.

Participating for a second year, the Partnership provided payroll and trade creditors data for the exercise and an NFI report listing eight employee matches and 360 creditor matches was provided and investigated by internal audit.

In their report to the audit and standards committee on 12 June 2009, internal audit reported that they had considered all employee matches and approximately 50% of the creditor matches. They intend to continue to review the lower risk matches.

The work completed by internal audit did not identify any evidence of fraud or error.

Performance

During 2008-09, internal audit, upon request from management, completed a number of value for money audits to identify scope for improved economy, efficiency and effectiveness in relation to subway stores, travel and subsistence, procurement and an updated on the provision of a bus for subway staff.

Audit Scotland has confirmed that they will not subject the Partnership to a Best Value inspection during our five-year appointment as external auditors.

Recommendations

We did not identify any significant recommendations for development in performance management arrangements.

Performance management

Performance management

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.

During 2008-09, internal audit, upon request from management, completed a number of value for money audits to identify scope for improved economy, efficiency and effectiveness in relation to subway stores, travel and subsistence, procurement and an updated on the provision of a bus for subway staff. These reports resulted in a number of recommendations relating to the scope for improved value for money through performance indicators and revision of policies and procedures.

Best Value

The Local Government in Scotland Act (2003) established Best Value and Community Planning as statutory duties for local authorities. In response to these duties, the Accounts Commission introduced specific arrangements for the audit of Best Value and Community Planning. Audit Scotland has confirmed that they will not subject the Partnership to a Best Value inspection during our five-year appointment as external auditors.

Appendix one – action plan

Priority rating for recommendations		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the Partnership or systems under consideration. The weakness may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the controls to meet their objectives in any significant way. These are less significant observations than grades one and two, but we still consider they merit attention.

No.	Issue and recommendation	Management response	Officer and due date
1	For 2008-09 the Partnership has reported a reduction in its general reserve. However, following the early repayment of debt during 2008-09, which is expected to continue in 2009-10, the Partnership at their meeting on 13 February 2009 reported that savings of £20 million achieved over the next eight years would be diverted to an earmarked subway modernisation fund. It is important that the Partnership obtains consent to increase reserves or identifies an alternative means of 'carrying' these savings. (*Grade one*)	Agreed. SPT will continue to press for a change to the legislation to allow SPT to manage reserves in accordance with the SORP.	Assistant Chief Executive (Business Support) 31 March 2010
2	It is recommended that a plan and timetable is established to ensure the effective implementation of International Financial Reporting Standards. This will allow the consideration of key accounting judgements on a timely basis. This will ensure that expert advice can be taken as necessary and that deadlines are achieved. (*Grade one*)	Agreed. Consideration of IFRS has begun and a plan will be developed by end of September 2009 for implementation.	Director of Finance 30 September 2009