cutting through complexity

Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee

Annual audit report to Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee and the Controller of Audit

Audit: year ended 31 March 2014

19 September 2014

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 Strathclyde Partnership for Transport ("SPT") and Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC"), and is made available to 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 responsibilities 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.

Headlines

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

In accordance with ISA (UK and Ireland) 260: *Communication with those charged with governance,* this report summarises our work in relation to the financial statements for the year ended 31 March 2014.

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

We have completed our audit for 2013-14 of both Strathclyde Partnership for Transport ("SPT") and Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC"), together for the purposes of this report, "the Partnership".

Area	Summary observations	Analysis
Service overview		
Business issues and update	The Partnership approved the Regional Transport Strategy ("RTS") delivery plan 2014-2017 in May 2014. The delivery plan focuses on specific services, initiatives and projects that the Partnership seeks to deliver over the next three years.	Pages 6 to 7
	To meet the longer term strategy the Partnership has implemented significant changes to work practices over the last four years which have resulted in an overall decrease in employee costs and has allowed an increase in payments to bus operators and revenue contribution to the capital programme.	
	The new smartcard ticketing system was successfully introduced in November 2013. The system will be enhanced with the introduction of the park and ride element of the system; expected to be implemented in 2014.	
	The Strathclyde Concessionary Travel Scheme is operating under the same strategy as in prior years, no issues were noted during the audit process.	Page 13
Financial position	SPT achieved a broadly breakeven position, after allocating £11.5 million to the subway modernisation fund and before entries in respect of pensions, asset valuations and asset impairment charges. There was an underlying underspend of £5.8 million against the original budget. This underspend was applied to support capital expenditure (£2.1 million) and a further £3.7 million was credited to the subway modernisation fund. SPT met its financial targets through effective financial planning and management.	Pages 8 to 12
	As at 31 March 2014 the Partnership held cash and short term investments of £78.3 million.	
	Total expenditure in respect of the capital programme was £38.4 million, against an initial budget of £45.7 million. The main variance is a £5 million shortfall in respect of the re-phasing of the Fastlink project.	
	The 2014-15 budget forecasts a breakeven position, with further contributions to the subway modernisation fund of £8.1 million. The 2014-15 capital budget of £73.5 million includes planned over programming of £5.4 million.	
	SCTSJC met its financial targets. £217,000 was transferred to general reserves. The 2014-15 budget forecasts a break even position after the utilisation of £70,000 accumulated reserves.	Page 13

Headlines (continued)

Area	Summary observations	Analysis
Financial statements and accounting		
Accounting policies	The Partnership adopted IAS 19 Employee Benefits (revised), as it became effective for 2013-14, the adoption is applied retrospectively and the comparative amounts have been restated in the financial statements. There was no adjustment to the balance sheet as at 31 March 2013, the adjustments being an allocation between finance costs and other comprehensive income and expenditure. Other accounting policies have been consistently applied compared to the prior year. Following an interim revaluation of property assets as at 31 March 2014, performed by the District Valuer under instruction by the Partnership, there was a net reduction in the value of operational and investment properties of £2.1 million. We are content with the assumptions used in the valuation and the accounting entries and disclosures recognised in the financial statements.	Page 16-19
Audit conclusions	We have issued unqualified audit opinions on the 2013-14 financial statements for both SPT and SCTSJC.	Page 14-18 Appendix 1
Governance and narrative reporting		
Governance	Over-arching and supporting corporate governance arrangements provide a robust framework for organisational decision-making. We consider that the corporate governance arrangements remain appropriate for the Partnership.	Page 22-24
Control observations	Our testing, combined with that of the audit and assurance team, of the design and operation of financial controls over significant risk points confirms that controls, in the main, are operating effectively. Three minor control weaknesses were reported in our interim report with appropriate recommendations agreed with management.	Page 22-24
Performance Management		
Performance management	Financial monitoring reports are detailed and include comparison of forecast outturn against the original or revised budget, as appropriate. Management consider performance and relevant responses against Audit Scotland reports as relevant during the year, including, for example *Scotland's public sector workforce*.	Page 25-26

Scope and responsibilities

Purpose of this report

The Accounts Commission for Scotland appointed KPMG LLP as auditor of Strathclyde Partnership for Transport (“SPT”) and Strathclyde Concessionary Travel Scheme Joint Committee (“SCTSJC”) , together for the purposes of this report, “the Partnership”, under the Local Government (Scotland) Act 1973 (“the Act”). The period of appointment is 2011-12 to 2015-16, inclusive.

Our annual audit report is designed to summarise our opinion and conclusions on significant issues arising from our audit. It is addressed to both those charged with governance at Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee and the Controller of Audit. The scope and nature of our audit were set out in our audit strategy document which was presented to the audit and standards committee in our “Audit strategy, plan and interim report”.

Responsibilities

Audit Scotland’s *Code of Audit Practice* (“the Code”) sets out Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee ’s accountable officer’s responsibilities in respect of:

- preparation of financial statements;
- systems of internal control;
- prevention and detection of fraud and irregularities;
- standards of conduct and arrangements for the prevention and detection of bribery and corruption; and
- financial position.

This report reflects our overall responsibility to carry out an audit in accordance our statutory responsibilities under the Act and in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board and the Code.

The Code sets out the wider dimensions of public sector audit which involves not only the audit of the financial statements, but also consideration of areas such as financial performance and corporate governance.

An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. Weaknesses or risks identified are only those which have come to our attention during our normal audit work in accordance with the Code, and may not be all that exist. Communication by auditors of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

Under the requirements of International Standard on Auditing (UK and Ireland) (‘ISA’) 260 *Communication with those charged with governance*, we are required to communicate audit matters arising from the audit of financial statements to those charged with governance of an entity.

This annual audit report to members and our presentation to the audit and standards committee, together with previous reports to that committee throughout the year, discharges the requirements of ISA 260.

Service overview

Our perspective on key business issues and the financial position of the Partnership

Key business issues

The total planned subway modernisation programme cost is approximately £290 million, of which up to £246 million will be funded by the Scottish Government.

The contribution by SPT to the subway modernisation fund for 2013-14 was £11.5 million, an increase of £3.7 million from the original budget.

In 2013-14 the total expenditure on subway modernisation projects was £11.6 million.

The smartcard ticketing system was introduced in November 2013.

Service overview

Subway modernisation

'A Catalyst for Change', The Regional Transport Strategy ("RTS") for the West of Scotland 2008-2021 was approved by Scottish Ministers in June 2008. The RTS delivery plan 2014-2017, was recently approved by the Partnership, and focuses on specific services, initiatives and projects that SPT seeks to deliver over the next three years. The strategy is based on four RTS outcomes, underpinned by eight strategic priorities, to be delivered by 15 work streams. The ability of SPT to deliver projects, services and initiatives which support the achievement of RTS outcomes is dependent on future funding and partnership working with the Scottish government, constituent councils and other public and private sector partners.

As part of this longer term strategy, SPT approved the 'modernisation case' as the best way forward for subway modernisation and the project is now underway. The total planned subway modernisation programme is approximately £290 million, of which up to £246 million will be funded by the Scottish Government with the balance met by drawing on the SPT's subway modernisation fund (created through current and future revenue savings) and borrowing as required.

The contribution to the subway modernisation fund in 2013-14 was £11.5 million, an increase of £3.7 million from the original budget. The Partnership is forecasting subway modernisation expenditure of £30.1 million for 2014-15 compared to £12.1 million in 2013-14. Expenditure will be financed by drawing down £23.5 million from the subway modernisation fund or borrowing and government grants.

Part of the subway modernisation project includes development of an integrated ticketing system. The new smartcard ticketing system was successfully introduced in November 2013. The system will be enhanced with the introduction of the subway park and ride element of the system; expected to be implemented in 2014.

Integrated ticketing system

SPT formed a joint venture, Nevis Technologies Limited, with the technology company Ecebs. Through Nevis Technologies, and subject to Transport Scotland agreement, the Partnership plans to integrate the smartcard product with the National Entitlement Card and trial it on other transport services with the ultimate aim of establishing a fully-integrated ticketing product across all public transport modes in the SPT area.

We continue to discuss accounting consequences and highlight key accounting judgements that need to be considered by management as the level of activity within the joint venture increases. The magnitude of transactions in 2013-14 was not material and consequently the Partnership has not prepared group financial statements.

Station upgrades

As in prior years, management considered the valuations of completed station upgrades in order to assess if there is a need to estimate impairments to be recognised at other stations. An impairment of £1.6 million is reflected in the 2013-14 financial statements in this respect. Having discussed with management, and reviewed supporting documentation, we are satisfied that they have been calculated on a logical and reasonable basis.

Bus operations

In 2013-14 the Partnership continued to manage socially necessary bus services, on demand-responsive bus services (MyBus) and school contracts. The Partnership committed over £11 million to secure vital bus services across Strathclyde in 2013-14. These subsidised services continue to provide an essential public transport lifeline to many local communities not served by commercial operators.

Key business issues (continued)

In 2013-14 main works commenced on Fastlink. In 2013-14 the total expenditure was £9.9 million compared to budgeted expenditure of £15 million.

To meet the longer term strategy the Partnership have implemented significant changes to work practices over the last four years which have resulted in an overall decrease in employee costs and an increase in payments to bus operators and capital contribution.

Fastlink

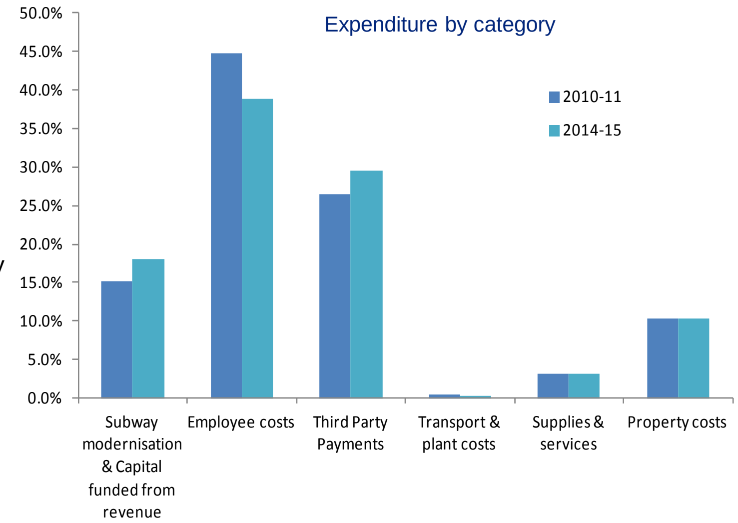
In 2013-14 the main works commenced on Fastlink, intended to improve bus services across Glasgow and surrounding areas. Glasgow City Council is responsible for the overall management of the project, with SPT acting as project sponsor. To date, progress includes completion of design works for the core route and completion of works at Anderson Quay, Lancefield Quay, ClydeArc Bridge, Pacific Drive and junction improvements in Govan.

During 2014-15 the Partnership will continue to work with Glasgow City Council to deliver the core Fastlink route to the new South Glasgow Hospital and further develop the Renfrew/Braehead extension with Renfrewshire Council. In 2013-14 Fastlink expenditure was £9.9 million compared to budgeted expenditure of £15 million. The Partnership is forecasting Fastlink expenditure of £18.3 million for 2014-15, financed primarily from the £14.7 million ring-fenced government grant, with the remainder met from ERDF funding.

Resourcing strategy

The Partnership approved a two year budget plan in December 2013, including in principle 2015-16, complementing SPT's longer term strategy. The key elements of the strategy are to ensure service levels are maintained and increased resources are available to ensure socially necessary bus services are protected, whilst providing funding to support the subway modernisation project and local authority capital projects. This is to be achieved by savings generated across all aspects of SPT and without increase to local authority requisition levels.

Since the approval of the plan in 2010 there has been a 28% decrease in headcount, following significant changes to the organisational structure and review of work practices. The graph opposite sets out the changes in the distribution of expenditure in the 2014-15 budget compared to 2010-11.



Source: *Partnership committee 13 December 2013*

Employee costs as a percentage of total expenditure have decreased by 6%, whilst the percentage allocated to third party payments (which includes bus operator payments) increased by 3% in cash terms. Contributions to subway modernisation and local authority capital projects (capital funded from revenue) also increased by 3% in cash terms.

Strathclyde Concessionary Travel Scheme

The Strathclyde Concessionary Travel Scheme is still operating under the same strategy as in prior years, no issues were noted during the audit process.

Financial position

SPT met its financial targets, through effective financial planning and management.

An underlying underspend of £5.8 million against the original budget arose during 2013-14, of which £2.1 million was used to support capital expenditure and £3.7 million was credited to the subway modernisation fund.

Financial position

The table opposite reconciles the budgeted outturn to actual outturn for 2013-14. The original 2013-14 budget forecast a breakeven position; the core revenue expenditure budget was £38.4million. Of this, £37.4 million was financed through requisition from constituent local authorities, together with £1 million funded by the Scottish Government.

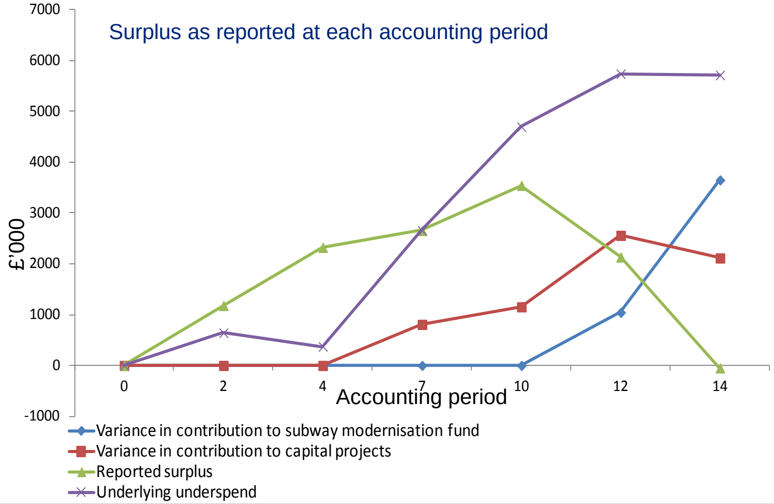
Requisitions from the constituent local authorities were in line with budget. Expenditure was below budget in a number of areas including employee costs (£1.7 million) and bus operator payments (£1.3 million). There were also increases in subway income (£1.8 million), and bank interest and other finance income (£0.3 million). The increase in subway income is attributable to a fare increase introduced in January 2014 and increased patronage in the latter part of 2013-14. Savings arose as a result of staff restructuring and reduced overtime payments, management of bus operator payments and close control of all expenditure lines.

The savings were offset by an increase in the contribution to capital funded from revenue (£2.1 million), to continue to support the general capital programme.

The original budget, approved by the Partnership, included a forecast contribution to the subway modernisation fund of £7.8 million. As a result of the revenue savings and additional income which arose during 2013-14, an additional contribution of £3.7 million was made to the subway modernisation fund to bring the cumulative total amount to £29.6 million.

There is an underlying underspend of £5.8 million as shown in the graph opposite. The increase in subway modernisation fund contribution reflects the continuing funding programme as detailed in the subway modernisation outline business case. The business case details the requirement to contribute revenue savings to assist in the overall funding package throughout the life of the project.

Surplus on provision of services reconciled to budgeted outturn	£'000
Budget outturn	**0**
Variations in respect of:	
Employee costs	1,692
Property costs	200
Supplies and services	58
Transport and plant costs	(129)
Third party payments	1,370
Financing costs	(125)
Subway income	1,824
Additional income	641
Contribution to capital financed from revenue	(2,115)
Contribution to subway modernisation	(3,654)
Surplus on provision of services as at 31 March 2014	(238)



Financial position (continued)

As at 31 March 2014 the Partnership had liquid cash balances of £78.3 million.

Cash balances

As at 31 March 2014 the Partnership had liquid cash balances (cash and short term investments) of £78.3 million. We have noted in prior years that this is a relatively high balance for a public body, although we noted that there is expected to be a significant reduction in 2014-15 when the contract for the provision of new subway rolling stock is signed, as a result of a substantial initial payment. However a decision on whether to utilise cash or borrow to meet these costs is still to be taken by SPT.

Financial position (continued)

The 2014-15 budget forecasts a breakeven position, with further contributions to the subway modernisation fund of £8.05 million. In line with the approved plan.

Revenue budget

A revenue budget of £38.4 million for 2014-15 was agreed at the partnership meeting on 13 December 2013. This budget was set on the basis that the level of requisition from the constituent local authorities will be maintained, in cash terms (with inflation factors and service cost pressures being absorbed by SPT). Similar to prior years, performance is monitored regularly by the strategy and programmes committee, with reports also presented to partnership meetings. A summary of the budget and variances to the previous years' budget is shown opposite.

The key changes in the 2014-15 budget, compared with 2013-14 are:

- reduction in employee costs of £0.7 million (3%) – reflecting changes in headcount, revised shift patterns and a reduction on strain on funds costs.
- increase in property costs by £0.2 million (3.8%) as a result of increased rates for the new Hamilton bus station; and
- other third party payments increased by £0.1 million (3.7%), reflecting increases in computer maintenance contracts and provision for ticketing marketing.

	Budget 2013-14 (£'000)	Budget 2014-15 (£'000)	Variance (£'000)
Chief executive's department	601	617	16
Operations	19,914	20,161	247
Corporate	3,888	3,505	(383)
Business support	3,674	3,585	(89)
Contribution to subway modernisation fund	7,841	8,050	209
Contribution to capital funded from revenue	2,500	2,500	-
Net expenditure	**38,418**	**38,418**	**-**
Requisitions	(37,381)	(37,381)	-
Revenue grant	(1,037)	(1,037)	-
Reserves	0	0	-
Funding	**38,418**	**38,418**	**-**
(Surplus) / deficit	**-**	**-**	**-**

Source: Partnership committee 13 December 2014

Financial position (continued)

Total expenditure in support of the capital programme was £38.4 million against an initial budget of £45.7 million, the main variance is a £5.1 million underspend to date in respect of re-phasing of the Fastlink project.

Capital programme

The table below summarises capital programme expenditure in 2013-14 against budget. Total expenditure in support of the capital programme was £38.4 million against an initial budget of £45.7 million, approved by the partnership on 15 February 2014. The main variance in the delivery of the capital plan related to the re-phased Fastlink project. £5 million pounds of Fastlink funding was used to support subway modernisation in 2013-14, this transaction will be reversed in 2014-15 ensuring that funding for Fastlink is available at the time expenditure is incurred.

Capital Project	Actual 2013-14 (£'000)	Original Budget 2013-14 (£'000)	Variance (£'000)
Subway modernisation	11,563	11,650	(87)
Fastlink	9,891	15,000	(5,109)
Local Authority grants	7,334	9,335	(2,001)
Dalmarnock station	2,860	2,860	0
Bus station and shelter upgrade	1,581	1,600	(19)
Other	5,144	5,280	(136)
Total	**38,373**	**45,725**	**(7,352)**

Source: *P13 capital monitoring report*

A number of projects were carried forward into 2014-15. The capital programme was mainly funded by known Scottish Government grant funding (£15.3 million), EDRF specific grants (£3.5 million), Fastlink grant (£15 million) and a contribution from revenue (£4.6 million).

Throughout the year there was a continued focus on capital programme monitoring. Updates on the delivery of the capital programme were presented to all strategy and programmes committee meetings during 2013-14.

Financial position (continued)

SPT approves a higher level of capital expenditure relative to available funding, as a number of projects may be subject to in-year delays and slippage.

The 2014-15 capital budget of £73.5 million includes over programming of £5.4 million.

Capital budget

SPT regularly plans a higher level of capital expenditure relative to available funding to allow for flexibility in the capital programme. The 2014-15 capital budget, approved on 21 February 2014, includes £73.5 million of projects. Indicative budgets include amounts planned in respect of the subway modernisation programme and the Fastlink programme. The budget for 2014-15 compared to 2013-14 is shown below:

Capital budget	2013-14 £'000	2014-15 £'000
Capital budget	45,725	73,520
Funded by:		
Scottish Government capital grant	9,337	16,500
Subway modernisation (ring-fenced)	6,000	6,000
Contribution subway modernisation fund/borrowing requirement	-	23,491
Fastlink funding	15,000	14,713
ERDF grant	2,860	4,212
Other capital grants	-	722
Capital funded from revenue	2,500	2,500
Variance	**10,028**	**5,382**

Source: Partnership committee 21 February 2014

Scottish Government general funding available in 2014-15 is £22.5 million. The core capital grant award from the Scottish Government includes £6 million ring-fenced for subway modernisation and it is therefore important that management continues to monitor capital expenditure against these projects as part of the monthly monitoring to ensure the terms of the capital grant are met.

SPT has put considerable efforts into seeking additional funding, and has been successful in securing additional specific and European grants to support the Fastlink project and a contribution to the subway modernisation.

The 2014-15 Subway Modernisation budget was set at £30.1 million, with funding provided by a draw down of the subway modernisation fund, borrowing to support subway modernisation plans of £23.5 million, government grants of £6 million and £0.6 million ERDF grant.

Rolling stock represents the most significant investment in subway modernisation. The project team have undertaken the reference and manufacturing site visits in order to assess the suppliers experience and ability in the technical, operational and management aspects of the delivery of similar projects for new trains and signalling and control systems. The outcomes of the site visits will contribute to the assessment required in the next stage of the procurement process (Invitation to Submit Detailed Solutions) and have assisted in preparing the organisation for the delivery and on-going operation of the new system.

Strathclyde Concessionary Travel Scheme Joint Committee

SCTSJC met its financial targets. £217,000 was transferred to general reserves.

The 2014-15 budget forecasts a break even position after the utilisation of £70,000 accumulated reserves.

The Strathclyde Concessionary Travel Scheme ("the Scheme") covers the twelve local authorities in the partnership area. The cost of the Scheme is mainly funded by requisitions from the constituent local authorities together with planned utilisation of reserves.

The table below highlights the 2013-14 surplus of £217,000 which was transferred to reserves, compared with a budget to break even. The payment to operators was £517,000 less than budget following an increase in the basic concessionary fare of 10p on all modes of transport and a renegotiation of the rate of reimbursement to operators.

There have been a number of measures established since 2010-11 to ensure the long-term sustainability of the Scheme and the joint committee highlights that the fare increase has helped manage overall payments to operators from the Scheme and that despite fare increases, patronage levels have been maintained.

At 31 March 2014, the accumulated reserves of £1.6 million were higher than anticipated as the planned utilisation of reserves was not required.

	Actual 2013-14 (£'000)	Budget 2013-14 (£'000)	Variance (£'000)
Payments to operators	3,738	4,279	(541)
Administration & overheads	332	309	23
Interest received	(29)	(30)	1
Net operating expenditure	4,041	4,558	(517)
Funded by:			
Requisition	**(4,258)**	(4,258)	-
Use of reserves	-	(300)	300
(Surplus) / deficit	**(217)**	**-**	**217**

The budget for 2013-14 estimates £4.6 million net operating expenditure, funded by £4.3 million requisition income from the constituent local authorities and utilisation of £0.3 million reserves.

The budget reflects forecast patronage and reduced operator reimbursement levels. It was designed to sustain the continued operation of the scheme within levels affordable to the constituent local authorities together with prudent use of accumulated reserves, however SCTSJC has no control over the fare levels set by operators or patronage.

	Budget 2013-14 (£'000)	Budget 2014-15 (£'000)	Variance (£'000)
Payments to operators	4,279	4,042	(237)
Administration & overheads	309	311	2
Total expenditure	4,588	4,353	(235)
Interest received	(30)	(25)	5
Net operating expenditure	4,558	4,328	(230)
Funded by:			
Requisition	(4,258)	**(4,258)**	**-**
Use of reserves	(300)	(70)	(230)
(Surplus) / deficit	**-**	**-**	**-**

Source: SCTSJC February 2014

Financial statements and accounting

Our perspective on the preparation of the financial statements and key accounting judgements made by management

Audit conclusions

We have issued unqualified audit opinions on the financial statements.

International Standards on Auditing require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk and that management override of controls is a significant risk.

We have satisfactorily carried out audit work to address these risks.

Audit conclusions

Following approval of the financial statements by the Partnership, we have issued unqualified opinions on the financial statements of both Strathclyde Partnership for Transport (“SPT”) and Strathclyde Concessionary Travel Scheme Joint Committee (“SCTSJC”). There are no matters identified on which we are required to report by exception.

In gathering the evidence for our opinion we have:

- performed a mixture of substantive and controls testing to ensure an efficient approach that covers all the key risks;
- liaised with the audit and assurance team and reviewed their reports to ensure all key risk areas having a potential financial statements impact have been considered;
- reviewed and challenged the assumptions and judgements made by management and considered these for appropriateness;
- considered if the financial statements may be affected by fraud through discussions with senior management and audit and assurance team to gain a better understanding of their work in relation to prevention and detection of fraud with the potential to impact on the financial statements; and
- attended the audit and standards committee to communicate our findings to those charged with governance, but also to update our understanding of the key governance processes and obtain key stakeholder insights.

Audit focus areas

Income recognition	The Partnership receives significant income in the form of requisitions from the constituent local authorities, Scottish Government grants and operating income associated with the subway. Associated with the complexity of arrangements surrounding some aspects of income, there is a risk over its recognition in the financial statements. To address this risk, we reviewed the treatment of significant elements of income, including building an expectation of subway income taking into account patronage numbers and fare changes occurring in the year. We have obtained sufficient evidence that the risk of fraud or error in income recognition is within materiality levels and did not identify any errors that required adjustment in the financial statements.

Audit conclusions (continued)

We have considered the other areas of focus as noted in the audit strategy and plan:

- income recognition
- subway modernisation
- voluntary severance
- revaluation of assets
- pensions liability

Audit focus areas	
Subway modernisation	The Partnership approved the 'modernisation case' as the best way forward in respect of the requirement to significantly upgrade the subway system. The final business case was approved by the Scottish Government in March 2011. The overall programme is underpinned by five work streams comprising; rolling stock and signalling, infrastructure, ticketing, stations and human resources. There is a delivery risk associated with this project which could inhibit the realisation of the Partnership's strategy. There is also a risk to the financial statements relating to the recognition of expenditure and the valuation of the assets that have been subsequently recognised. To address this risk, we reviewed management's approach to calculation of impairments and underlying assumptions and have agreed the valuation of assets to the independent valuer's report and confirmed that management had adopted a similar approach to prior year. During 2013-14, expenditure of £2.2 million was incurred in respect of enhancements at Kelvinhall station and preparatory work for other stations as part of the subway modernisation programme. An impairment of £1.7 million was recognised against the related assets as the value of the station was assessed as increased by £0.5 million. The station is particularly space-constrained and the required expenditure was higher as a result, without a corresponding value benefit. We concur with management's assertions in respect of impairment and the treatment in the financial statements.
Voluntary severance	During 2013-14, 15 members of staff left the organisation through the voluntary severance arrangements, as part of the Partnership's rationalisation of headcount. We reviewed the contents of the remuneration report against the requirements of the regulations and confirmed that information related to the departure of senior staff and voluntary severance payments was accurately disclosed in line with current guidance. We also tested a sample of voluntary severance payments made in the year to ensure they had been calculated correctly and were in line with policy. Our work did not identify any matters that required adjustment in the financial statements or which require to be brought to your attention.

Audit conclusions (continued)

We have considered the other areas of focus as noted in the audit strategy and plan:

- **income recognition**
- **subway modernisation**
- **voluntary severance**
- **revaluation of assets**
- **pensions liability**

Audit focus areas	
Revaluations of assets	The last full valuation of the Partnership's property plant and equipment was in 2010-11. The Code requires valuations to be carried out with sufficient regularity to ensure that the balances are not materially misstated, and at least every five years. In line with good practice, SPT carried out an interim valuation and engaged the District Valuer to perform the valuation. As a result of the valuation there was a net reduction in the value of operational properties of £2.1 million. In the financial statements, a downward revaluation movement of £4.4 million is recognised against the deficit on provision of service and the revaluation reserve balance increased by £2.3 million. The value of investment property increased by £0.5 million following the annual valuation at 31st March 2014 by the District Valuer. In the financial statements a credit was recognised against the deficit on provision of service. We reviewed the valuation reports, the basis upon which they were prepared, related accounting entries and disclosures. We are satisfied with the assumptions applied by the valuer and are satisfied that the valuations were carried out by suitably qualified valuers and that the valuers' instructions were in line with the requirements of the Code. From our audit testing, we concur with the amounts presented in the financial statements, related accounting entries and disclosures.
Pensions liability	The majority of the Partnership's employees are members of the local government pension scheme, this is a defined benefit scheme and as such is dependent on the actuarial assumptions and calculations. We reviewed the assumptions used by the actuary in calculating the pension deficit. The assumptions are within the acceptable range of the guideline assumptions that KPMG considers are appropriate, having consulted with KPMG's actuaries. Overall, the assumptions are considered to represent a balanced approach to valuation of the net pension deficit. We provide further information on the next two pages. Our work did not identify any matters that required adjustment in the financial statements or which require to be brought to your attention and we concur with the amounts presented in the financial statements including disclosures.

Audit conclusions - employee benefits

Each of the assumptions used to value the Partnership's net pension deficit are within an acceptable range of KPMG's expectations.

We are of the view that this therefore represents a reasonable and balanced approach, in accordance with the requirements of IAS 19.

Defined benefit pension liability		
Value (£000s)		
2013-14	2012-13	KPMG comment
(30,143)	(24,978)	In line with our established practice and in advance of the audit fieldwork, our actuarial specialists reviewed the approach and methodology of the actuarial assumptions used in the IAS19 pension scheme valuation. Details of key actuarial assumptions are included in the table, along with our commentary.

Assumption	Partnership	KPMG central	Comment
Discount rate	4.1%	4.1%	Acceptable
RPI inflation	3.4%	3.4%	Acceptable
CPI inflation	2.6% RPI - 0.8%	2.4% RPI – 1%	Acceptable – the Partnership's assumption is more prudent (higher liability) than KPMG's central rate, and is within the acceptable range.
Salary growth (long term)	4.9% 1.5% above RPI	0-1.5% above RPI/CPI inflation	Acceptable – the Partnership's assumption reflects the extension of the public sector pay freeze to 2016, followed by a long term assumption of RPI plus 1.5%.

The overall assumptions applied by management are considered to be reasonably balanced for a scheme with a liability duration of around 17 years.

The closing deficit increased by £5 million from 2012-13, primarily due to the application of an updated discount rate. A reconciliation from opening to closing deficit is included on the next page.

Audit conclusions - employee benefits (continued)

The table opposite shows the reconciliation of the movement in the balance sheet.

The main elements of volatility are in respect of the discount rate, which drives the valuation of the liabilities.

	£000	Deficit / loss	Surplus / gain	Impact	Volatility	Commentary
	Opening deficit			**(24,978)**	-	The opening IAS19 deficit for the Scheme at 31 March 2013 was £24.978 million, this agrees to the 2012-13 financial statements
I & E	Service cost			(3,764)	●	The scheme is open to accrual. The service cost represents the value of new benefits built up over the year.
I & E	Curtailments			(243)	●	This represents the loss on curtailment in 2013-14
I & E	Net interest charge			(1,133)	●	This is the difference between the expected return on assets of £7.586 million and the interest on the defined benefit obligation of £8.719 million.
Cash	Contributions			3,191	●	The Partnership made cash contributions of £3.191 million.
TCIE	Change in assumptions gain/(loss)			(3,216)	●	This represents an actuarial loss due to changes in assumptions, primarily due to the reduction in the discount rate.
	Closing deficit			**(30,143)**	-	

Key: ● Low ● Medium ● High

Source: KPMG analysis of scheme valuation movements. Volatility assessment based on KPMG's market experience.

I&E – impacts on surplus /(deficit)
Cash – cash-flow impact
TCIE – charged through total comprehensive income and expenditure

Accounting framework; application of accounting policies

There have been no substantive changes to the financial reporting framework as set out in the Code of practice on Local Authority Accounting in the United Kingdom 2013-14 ("the Code") .

As required, the Partnership adopted IAS 19 *(revised)* in 2013-14. All other accounting policies have been applied consistently.

The financial statements have been prepared on a going concern basis; we concur that this is appropriate.

Financial reporting framework	■ The partnership prepared the financial statements in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013-14 ("the Code") which is based upon International Financial Reporting Standards ("IFRS"). ■ Under previous IAS 19, the interest cost and the expected return on plan assets were recognised in the comprehensive income and expenditure statement. Under IAS 19R, these two amounts have been replaced by a single measure called 'net interest' calculated on the net defined benefit liability. If the standard had been adopted early in 2012-13, the estimated change to finance costs would have be £1.47 million, this has been recognised as a restatement to the comparative results. There is no change to the balance sheet. ■ Other changes to the code include: - accounting for allowances in respect of the Carbon Reduction Commitment Energy Efficiency Scheme; - amendments to the Comprehensive Income and Expenditure Statement as a result of changes to IFRS; - clarification of the treatment of overdrafts on the balance sheet and cashflow statement; - augmentation to pensions on service concession arrangements; - a number of clarifications and augmentations as a result of the CIPFA/LASAAC post implementation review. ■ We are satisfied that the accounting policies adopted remain appropriate to the Partnership.
Impact of revised accounting standards	■ No other newly effective accounting standards are considered to have a material impact on the Partnership's financial statements in the coming year. Appropriate disclosure to this effect is included within the accounting policies note to the financial statements.
Going concern	■ The financial statements of the Partnership have been prepared under the assumption that the organisations are a going concern. ■ SPT has net assets as at 31 March 2014 of £157.8 million. The Partnership's main sources of funding are government grants, funding from constituent local authorities and subway generated income. Government grants and local authority requisitions are agreed in advance of 2014-15 and therefore there is reasonable certainty over those sources of income. ■ We are satisfied that it is appropriate for the Partnership to prepare the financial statements under the going concern assumption

Financial statements preparation and other matters

The financial statements were made available on a timely basis and were accompanied by high quality working papers.

Our testing of the design and operation of financial controls over significant risk points confirmed these were operating effectively.

Financial statements preparation	Preparation of the financial statements ■ Throughout the course of the year we have had regular correspondence with the Partnership's finance team on key accounting issues. For example, we attended discussions prior to the final audit visit to discuss the proposed impairments and the valuations of non-current assets that had been completed during 2013-14. We found this approach beneficial and it supported an accelerated completion of the audit process. ■ High quality working papers and full draft financial statements were provided at the start of the audit fieldwork on 2 June 2014. This included the remuneration report, explanatory foreword and governance statement. We provided observations on the draft financial statements which have been incorporated by management. ■ In advance of our audit fieldwork, we issued a 'prepared by client' request setting out a list of required analyses and supporting documentation. The standard of documentation was very good and there was evidence of accountability and ownership of working papers across the finance department.
Internal controls	■ The Partnership is responsible for designing and implementing appropriate internal control systems. Our testing, combined with that of the audit and assurance team, of the design and operation of financial controls over significant risk points confirms that controls relating to financial systems and procedures are designed appropriately and operating effectively. ■ In our interim audit report, we raised two 'grade three' recommendations over review of bank reconciliations and authorisation of payments which were accepted by management and have now been implemented and one 'grade two' recommendation over journal authorisation which has been accepted by management and will be implemented from September 2014.
Other matters	■ Mandatory communications required by International Standards on Auditing are given in Appendix one. There are no significant matters in respect of (i) audit differences; (ii) auditor independence and non-audit fees; and (iii) management representation letter content.

Governance and narrative reporting

Our overall perspective on your narrative reporting, including the remuneration report and annual governance statement

Update on controls findings from our audit

Corporate governance arrangements

The Partnership maintains an integrated governance framework to provide an appropriate structure for maintaining decision-making, accountability, control and behaviour.

Annual governance statement and governance arrangements	
	SCTSJC, as a separate legal entity maintains its own governance arrangements which are appropriate for its size and complexity, however due to the administrative relationship between SCTSJC and SPT, there are a number of shared systems between the two bodies. The corporate governance and financial control frameworks that govern SCTSJC are also that of SPT. The annual governance statement for 2013-14 outlines the governance and risk management arrangements in operation in the financial year. It provides detail on the governance framework, the system of internal control, internal audit, internal financial controls and risk management arrangements and analyses the effectiveness of these elements of the framework. It describes a number of sources of assurance for the accountable officer. The statements, which are made by the Assistant Chief Executive (Business Support) (SPT) or Treasurer (SCTSJC), consider the effectiveness of the system of internal control based on information provided by the audit and standards committee and the audit and assurance team. The statements identify that there have been no significant risk-related matters. The Partnership maintains an integrated governance framework to provide an appropriate structure for maintaining decision-making, accountability, control and behaviour. The Partnership is supported by four other committees, with meetings of the partnership receiving the minutes from each of the other committees. The Corporate Risk Register is considered on a monthly basis by the strategy group and updated as required, it was last updated in May 2014 and reviewed by the audit and standards committee in June 2014. The strategy group has responsibility for overseeing the implementation of the Partnership's risk management policy and strategy. The audit and assurance team operated in accordance with the Public Sector Internal Audit Standards (PSIAS). We have considered the work of internal audit to inform our risk assessment and consider the work as appropriate. Our testing, combined with that of the audit and assurance team, of the design and operation of financial controls over significant risk points confirms that controls are designed appropriately and operating effectively. However, during our interim review we noted minor control observations, with recommendations agreed with management to address these matters. We have reviewed the governance statements and have confirmed that they are in line with guidance and reflect our understanding of the Partnership. We have updated our understanding of the governance framework and documented this through our overall assessment of the Partnership's risk and control environment. This work has formed part of our assessment of the Partnership's annual governance statements.

Corporate governance arrangements (continued)

Annual report, including the explanatory foreword	The financial statements form part of the annual report of the Partnership for the year ended 31 March 2014. We are also required to consider the explanatory foreword for consistency with the financial statements. We are satisfied that the information contained within the explanatory foreword is consistent with the financial statements.
Remuneration report	Scottish Statutory Instrument 2011 number 64, *The Local Authority Accounts (Scotland) Amendment Regulations 2011 amended the Local Authority Accounts (Scotland) Regulations 1985* added the requirement for local authority bodies to prepare a remuneration report. The remuneration report was provided at the commencement of the audit, and supported by good quality information in respect of the disclosures given. We considered the contents of the remuneration report and reviewed this against the requirements of the regulations. We have reviewed the exit packages awarded to confirm they are correctly stated and in line with SPT's policy. We have in prior years recommended that the Partnership include the remuneration report as a statement in its own right, in line with local government guidance. SPT continues to include the remuneration report after the primary statements and notes, at the back of the financial statements. While not out of line with some other local authorities, we remain of the view that it is inconsistent with our experience of good practice in other sectors and Scottish Government guidance. We suggested a number of minor amendments to disclosures and additional disclosure requirements to be carried put in order to meet with regulations.
Internal audit	As set out in our audit plan and strategy, we liaised with the audit and assurance team to maintain an understanding of their approach to ensure duplication of effort was minimised. We also reviewed internal audit reports to inform our risk assessment and to better understand the key audit issues. The audit and assurance team has completed their agreed plan and their annual report concludes that "reasonable assurance can be placed upon the adequacy and effectiveness of the Partnership's framework of governance, risk management and control in the year to 31 March 2014". The general programme of work was reviewed for significant issues to support our general work in assessing the corporate governance statements and statements of system of internal financial controls.

Corporate governance arrangements (continued)

Prevention and detection of fraud	Procedures and controls related to fraud are designed and implemented effectively. The Partnership has appropriate arrangements to prevent and detect fraud, inappropriate conduct and corruption, including policies and codes of conduct for staff and partnership members. These are supported by a fraud prevention policy and response plans, part of the overall counter fraud strategy. Management has confirmed that no significant fraud or irregularities have been identified during the year. As may be expected given the activities of the Partnership, minor customer frauds do occur and are reported to the strategy group and audit and standards committee.
National Fraud Initiative (“NFI”)	The National Fraud Initiative (“NFI”) is a data matching exercise which compares electronic data within and between participating bodies in Scotland to prevent and detect fraud. This exercise runs every two years and provides a secure website for bodies and auditors to use for uploading data and monitoring matches. Audit Scotland required auditors of local authorities to conduct a review of audited bodies participation and engagement with the National Fraud Initiative (“NFI”) exercise. We liaised with internal audit and reviewed the Partnership's progress in the investigation of data matches and submitted our response to Audit Scotland in December 2013. The audit and standards committee reviewed progress of the NFI data matching exercise during the year. Overall, we are satisfied with the Partnership's participation in the NFI exercise and have no recommendations to make in this regard.

Performance management

Our perspective on the performance management arrangements, including follow up work on Audit Scotland reports

Performance management

The Partnership's Best Value and performance management arrangements remain largely unchanged and we did not identify any issues which require to be brought to your attention.

Best Value and local response to national studies	In April 2002 the Scottish Ministers introduced a non-statutory duty on accountable officers to ensure there are arrangements designed to secure Best Value. Audit Scotland is committed to extending the Best Value audit regime across the whole public sector. Using the Scottish Government's nine Best Value principles as a basis for audit activity, Audit Scotland previously selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working). Audit Scotland periodically undertakes national studies on topics relevant to the performance of central government bodies. To ensure that added value is secured through the role of Audit Scotland and its appointed auditors, auditors will continue to ensure that audited bodies respond appropriately to reports from Audit Scotland's programme of national performance audits. The Partnership's internal audit and assurance function completed reviews of four Audit Scotland national reports: Scotland's public finances: Addressing the challenges; Responding to challenges and changes: An overview of local government in Scotland 2013; Scotland's public sector workforce and Managing early departures from the Scottish public sector. The reviews were reported to the audit and standards committee throughout the year and outlined the background to the report and the Partnership's response, including key recommendations in the report compared to the current practice at SPT. Areas for improvement were identified and a number of recommendations have been agreed and will be implemented by departmental management.
Performance management	Financial performance of the Partnership is monitored via revenue and capital monitoring reports presented to the strategy and programmes committee. Operational performance relating to transport services is reported to the operations committee. Ultimately, both of the above areas are reported to meetings of the Partnership. Financial monitoring reports are detailed and include comparison of forecast outturn against the original or revised budget as appropriate. Actions required to be taken in response to significant variances are summarised within the reports.

Appendices

Mandatory communications

There were no audit adjustments required to the core financial statements and there are no unadjusted audit differences.

Area	Key content	Reference
Adjusted audit differences Adjustments made as a result of our audit	There were no audit adjustments required to the draft financial statements of SPT or SCTSJC	
Unadjusted audit differences Audit differences identified that we do not consider material to our audit opinion	We are required by ISA (UK and Ireland) 260 to communicate all uncorrected misstatements, other than those which are trivial, to you. There are no unadjusted audit differences.	-
Confirmation of Independence Letter issued by KPMG to the Audit Committee	We have considered and confirmed our independence as auditors and our quality procedures, together with the objectivity of our audit director and audit staff.	Appendix two
Schedule of Fees Fees charged by KPMG for audit and non-audit services	There were no non-audit fees in 2013-14	
Draft management representation letter Proposed draft of letter to be issued by the Partnership to KPMG prior to audit sign-off	There are no changes to the standard representations required for our audit from last year.	-

Auditor independence and non-audit fees

Auditing standards require us to consider and confirm formally our independence and related matters in our dealings with the Partnership.

We have appropriate procedures and safeguards in place to enable us to make the formal confirmation in our letter included opposite.

Auditor independence

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

We have considered the fees paid to us by the Partnership and its related entities for professional services provided by us during the reporting period. We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the APB Ethical Standards. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Regular communications
- Internal accountability
- Risk management
- Independent reviews

Please inform us if you would like to discuss any of these aspects of our procedures in more detail.

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

Confirmation of audit independence

We confirm that as of 19 September 2014, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This letter is intended solely for the information of the audit and standards committee and should not be used for any other purpose.

Yours faithfully

KPMG LLP

KPMG

cutting through complexity