AUDIT SCOTLAND

South East of Scotland Transport Partnership

Annual audit report to Members and the Controller of Audit

September 2015

The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies. (www.audit-scotland.gov.uk/about/ac)

Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General. (www.audit-scotland.gov.uk)

The Accounts Commission has appointed Stephen O'Hagan as the external auditor of South East of Scotland Transport Partnershipfor the period 2011/12 to 2015/16.

This report has been prepared for the use of South East of Scotland Transport Partnership and no responsibility to any member or officer in their individual capacity or any third party is accepted.

This report will be published on our website after it has been considered by the Partnership. The information in this report may be used for the Accounts Commission's annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

Key contacts

Stephen O'Hagan, Senior Audit Manager
sohagan@audit-scotland.gov.uk

Carol Foster, Senior Auditor
cfoster@audit-scotland.gov.uk

Joan Dalgleish, Auditor

jdalgleish@audit-scotland.gov.uk

Audit Scotland
4th Floor, The Athenaeum Building
8 Nelson Mandela Place
Glasgow
G2 1 BT

Telephone: 0131 625 1500

Website: www.audit-scotland.gov.uk

Contents

Key messages

Audit of financial statements	• Unqualified independent auditor's report (audit certificate) on the 2014/15 financial statements. • Working papers were of a good standard and officers provided good support which enabled the audit team to complete fieldwork by the planned target date. • All monetary, presentation and disclosure issues, identified in unaudited accounts, corrected by management in audited financial statements.
Financial management and sustainability	• During 2014/15, the Partnership recorded a breakeven position with total outturn expenditure matching outturn income of £2.018 million.
Governance and transparency	• The Partnership had sound governance arrangements in place during 2014/15.
Outlook	• The Partnership has approved a revenue budget for 2015/16 which makes provision for £0.552 million of core service costs and £2.614 million of project expenditure. The Partnership has been successful in sourcing additional funding for projects to date. However, there is a risk around the delivery of the partnership's objectives if adequate funding cannot be sourced beyond 2015/16.

Introduction

1. This report is a summary of our findings arising from the 2014/15 audit of South East of Scotland Transport Partnership ("the Partnership").

2. The management of the Partnership is responsible for:
   - preparing financial statements which give a true and fair view
   - implementing appropriate internal control systems
   - putting in place proper arrangements for the conduct of its affairs
   - ensuring that the financial position is soundly based.

3. Our responsibility, as the external auditor of the Partnership is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.

4. An audit of financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements; this does not relieve management of their responsibility for the preparation of financial statements which give a true and fair view.

5. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures. Consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

6. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

Audit of the 2014/15 financial statements

Audit opinion	• We have completed our audit and issued an unqualified independent auditor's report.
Going concern	• The financial statements of the Partnership have been prepared on the going concern basis. We are unaware of any events or conditions that may cast significant doubt on the Partnership's ability to continue as a going concern.
Other information	• We review and report on other information published with the financial statements, including the management commentary, annual governance statement and the remuneration report. We have nothing to report in respect of these statements.

Submission of financial statements for audit

7. We received the unaudited financial statements in accordance with the agreed timetable. The working papers were of a good standard and staff provided good support to the audit team which assisted the delivery of the audit to deadline.

Overview of the scope of the audit of the financial statements

8. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Partnership in March 2015.

9. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2014/15 agreed fee for the audit was set out in the Annual Audit Plan and, as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.

10. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which had the greatest effect on the audit strategy, resources and effort. We set out in our Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance.

11. **Appendix I** sets out the audit risks identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

12. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Materiality

13. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. In addition, a misstatement or omission, which would not normally be regarded as material by amount, may be important for other reasons (for example, an item contrary to law).

14. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.

15. We summarised our approach to materiality in our Annual Audit Plan. Based on our knowledge and understanding of South East of Scotland Transport Partnership the Partnership, we set planning materiality for 2014/15 at £14,000 (1% of gross expenditure). We report all misstatements greater than £1,000. Performance materiality was calculated at £10,000, to reduce to an acceptable level the probability of uncorrected and undetected audit differences exceeding our planning materiality level.

16. On receipt of the financial statements and following completion of audit testing we reviewed our materiality levels and set materiality for 2014/15 at £26,000. We report all misstatements greater than £1,000. Performance materiality was calculated at £18,000. The change in materiality levels is mainly due to increased depreciation charges affecting the Partnership's financial statements as a result of new assets becoming operational.

Evaluation of misstatements

17. Officers have amended all identified misstatements exceeding our misstatement threshold.

18. We identified a number of presentational and monetary adjustments within the financial statements during the course of our audit. These were discussed with relevant officers who agreed to amend the unaudited financial statements. These adjustments have reduced both the cost of services gross income and gross expenditure by £219,000. The effect on the balance sheet was to reduce the general fund reserve balance and increase the capital adjustment account by £675,000. There is no effect on the net cost of services or net assets. A prior year re-statement was also made to reduce the prior year cost of services gross income and gross expenditure by £201,000. The net effect on the prior year net cost of services is nil.

Significant findings from the audit

19. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit, including:

- The auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures.
- Significant difficulties encountered during the audit.
- Significant matters arising from the audit that were discussed, or subject to correspondence with management.
- Written representations requested by the auditor.
- Other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process.

20. The following table contains a summary of the significant findings that, in our view, require to be communicated to you in accordance with ISA260.

Significant findings from the audit

Issue	Resolution
ERDF Funding Debtor: The financial statements include debtors of £446,000 in respect of ERDF funding for Bus Improvement projects, which has been outstanding since 31 March 2014. There is a risk that this amount may not be received in full, resulting in a write-off being required.	Management Assurances have been provided in respect of the recoverability of this debtor and it has been included in the ISA 580 Letter of Representation.
Salaries Recharge Journal: The unaudited financial statements included an adjustment to re-charge salary costs to projects. However the credit side of the adjustment had been processed incorrectly, resulting in both cost of services gross income and gross expenditure being overstated by £190,230. A similar adjustment was also made in 2013/14 and the effect was to overstate both income and expenditure by £187,000. There is no effect on the net cost of services or net assets.	The audited financial statements have been adjusted to correct this error.
Adjustment between Accounting Basis and Funding Basis: No depreciation charge adjustment has been made in the Movement in Reserves Statement. This has resulted in the general fund being overstated by £675,000 and the Capital Adjustment Account being understated by the same amount. There is no effect on the net cost of services or net assets.	The audited financial statements have been adjusted to correct this error.

Issue	Resolution
Budget Underspend: The unaudited financial statements included an adjustment to increase expenditure in respect of the amount of underspent requisitions, instead of reducing income. This resulted in both income and expenditure being overstated by £29,000. A similar adjustment was also made in 2013/14 and the effect was to overstate both income and expenditure by £14,000.	The audited financial statements have been adjusted to correct this error.
Remuneration Report disclosure: The unaudited remuneration report omitted disclosure of one officer with remuneration over £50,000.	The audited remuneration report has been amended to include this disclosure.
Performance Reporting in Management Commentary: The unaudited financial statements include a management commentary as required by the Local Authority Accounts (Scotland) Regulations 2014. However this does not include an analysis of non financial performance indicators as required by the regulations	The management commentary has been amended to include information about non financial performance.

Future accounting and auditing developments

Revisions to the Code of Practice

21. The financial statements of the Partnership are prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code) which interprets and adapts International Financial Reporting Standards (IFRS) to the local authority context. There are no significant changes to accounting requirements introduced by the 2015/16 Code which are likely to impact on the financial statements of the Partnership.

Financial management and sustainability

Financial management

22. As auditors we need to consider whether bodies have established adequate financial management arrangements. We do this by considering a number of factors, including whether:
    - the officer responsible for finance has sufficient status to be able to deliver good financial management
    - standing financial instructions and standing orders are comprehensive, current and promoted within the body
    - reports monitoring performance against budgets are accurate and provided regularly to budget holders
    - monitoring reports do not just contain financial data but are linked to information about performance
    - members provide a good level of challenge and question budget holders on significant variances.

23. The main financial management arrangements for the Partnership have been set down in the financial regulations and based on our accumulated knowledge and our review of relevant papers we conclude that the Partnership has made appropriate financial management arrangements.

Financial outcomes

24. The main financial objective for the Partnership is to ensure that the financial outturn for the year is within the resource budget allocated.

25. The Partnership's outturn total expenditure exceeded its budgeted total expenditure for 2014/15 however the Partnership achieved a breakeven position, with its outturn income matching the actual expenditure incurred as detailed in Table 1 below.

Table 1: Resource Budget

	Final Budget (£'000)	Actual Outturn (£'000)	(Under) / Over spend
Core Service	465	453	(12)
Revenue Projects	730	662	(68)
Capital Project	628	902	274
Interest	4	1	(3)
Total Expenditure	**1,827**	**2,018**	**191**
Government Grant	(782)	(782)	0

	Final Budget (£'000)	Actual Outturn (£'000)	(Under) / Over spend
Constituent Councils Requisitions	(200)	(171)	29
Other Income - Revenue Projects	(346)	(327)	19
Other Income - Capital Projects	(487)	(690)	(203)
Other Income - SESplan	(12)	(48)	(36)
Total Income 2014/15	**(1,827)**	**(2,018)**	**(191)**

Source: SEStran unaudited financial statements 2014/15

26. Capital expenditure of £0.902 million was incurred on the Real Time Passenger Information (RTPI) project. This expenditure was funded principally by income from the bus operators, the Bus Investment Fund and by using the underspend which was carried forward from the Partnership's revenue budget for 2013/14.

27. The Partnership recorded an underspend of £29,000 against its revenue budget for 2014/15. The normal practice is for the Partnership Board to vote to carry forward any underspend into the following year. The Board will make a decision on the use of the 2014/15 underspend following approval of the audited accounts.

28. The Partnership has no usable reserves at the year end as it holds no statutory powers to operate this type of reserve. Unusable reserves decreased by £76,000 mainly due to the net effect of adjustments through the Capital Adjustment Account and Pension Reserve.

2015/16 and beyond

29. In March 2015 the Partnership agreed a balanced budget for 2015/16 which made provision for £0.552 million of core service costs and £2.614 million of project expenditure in support of Regional Transport Strategy projects. The 2015/16 budget is based on confirmed Scottish Government and council funding for a one year period.

30. The Partnership has been successful in sourcing additional funding for projects to date. However there is a risk around the delivery of the Partnership's objectives if adequate funding cannot be sourced to support new projects beyond 2015/16.

31. In the absence of confirmed budget allocations for local government beyond 2015/16, longer-term funding assumptions remain subject to considerable uncertainty. Those projections that are available, however, point to a tightening of the overall fiscal position and potential cash-reductions in funding provided through the Scottish Block grant over the following two years. The Partnership intends to develop a revenue budget proposal for 2016/17 for consideration by the Partnership Board in the autumn of 2015.

Governance and transparency

Corporate governance

32. Members and management of the Partnership are responsible for establishing arrangements to ensure that its business is conducted in accordance with the law and proper standards, that public money is safeguarded and for monitoring the adequacy and effectiveness of these arrangements.

33. The Partnership Board comprises elected members from the eight constituent authorities and non-councillor members and is responsible for overseeing key aspects of governance. In addition there are a number of standing committees overseeing specific aspects of governance.

34. In previous years we have raised an issue with regard to the Performance and Audit Committee (PAC) achieving a quorate for meetings. We note that all PAC meetings took place during 2014/15.

35. From our work undertaken during the year, we have concluded that the Partnership has effective overarching and supporting governance arrangements which provide an appropriate framework for organisational decision making.

Accounting and Internal control systems

36. While auditors concentrate on significant systems and key controls in support of the opinion on the financial statements, their wider responsibilities require them to consider the financial systems and controls of audited bodies as a whole. However, the extent of this work should also be informed by their assessment of risk and the activities of internal audit.

37. A number of key financial systems of the Partnership are provided through City of Edinburgh Council (CEC), and our consideration of the internal control environment for the Partnership is informed by our CEC audit work. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

38. During our financial statements testing of creditors, we identified an instance where a VAT invoice had not been passed on to finance officers, resulting in VAT of £401 not being reclaimed from HMRC.

Appendix 3 – action plan point 1

Internal audit

39. Internal audit provides members and management of the Partnership with independent assurance on risk management, internal control and corporate governance processes. We are required by international auditing standards to make an assessment

of internal audit to determine the extent to which we can place reliance on its work. To avoid duplication, we place reliance on internal audit work where possible.

40. Our review established that the work of internal audit is of a good quality allowing us to place reliance on their work on the annual governance statement. We had planned to place reliance on internal audit's work in relation to accounts payable however, due to the scope of internal audit work carried out, we were unable to place reliance on it for this area and we modified our procedures accordingly.

Arrangements for the prevention and detection of fraud

41. Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. Auditors review and report on these arrangements.

42. There were no instances of fraud or corruption reported by the Partnership in 2014/15.

43. We assessed the arrangements for the prevention and detection of fraud during the planning phase of our audit. The Partnership's anti-fraud and corruption and anti- bribery policies provide a framework for deterring and preventing fraud and also dealing with any frauds which may occur.

44. We concluded that there are effective arrangements for the prevention and detection of fraud, although it should be noted that no system can eliminate the risk of fraud entirely.

Arrangements for maintaining standards of conduct and the prevention and detection of corruption

45. Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and have proper arrangements in place for implementing and monitoring compliance with standards and codes of conduct, standing orders and financial instructions. Auditors consider whether bodies have adequate arrangements in place. No issues have been identified by us for inclusion in this report.

Best Value and performance

46. Best value is a key factor to consider when planning policies, programmes and projects, and when taking any spending decisions. The Partnership should have systems and processes to ensure that it can demonstrate that it is delivering best value by assessing and reporting on the economy, efficiency, effectiveness and equality in service provision.

Performance management

47. The aims of the Partnership are set out in the Regional Transport Strategy. During 2014/15, the Partnership has been working on refreshing the strategy previously approved by the Scottish Government in 2008. A revised strategy was approved by the Partnership Board in March 2015 and by the Scottish Government in July 2015.

48. The annual Business Plan sets out the levels of capital and revenue expenditure approved by the Board and the projects and activities that will be taken forward by the Partnership in the year.

49. Progress towards the achievement of the Partnership's objectives is monitored on an annual basis, with the results reported in an Annual Report. In addition, progress on Projects is reported to the Board on a quarterly basis.

Overview of performance targets in 2014/15

50. A key project within the Partnership's Business Plan is Real Time Passenger Information (RTPI). The March 2015 Projects Report notes that the Partnership has obtained funding of £5.3 million for this project to date however a significant change was required to the project as a result of Stagecoach Fife taking the decision to implement its own RTPI system instead of the SESTRANs system. Following discussions with Stagecoach, it was agreed that data from the Stagecoach system will be fed into the SESTRANs system, which will enhance the system, although it has not been possible to develop the necessary interface by the end of March 2015.

51. The following deliverables were agreed with Transport Scotland :

- 31 buses in the First fleet would be equipped and commissioned by the end of March 2015
- Development of the system interface to accept data from Stagecoach and smaller operators would commence and be approximately 50% complete by the end of March 2015.

52. The June 2015 Projects report notes that, other than the transfer of on-bus units from Stagecoach to First, the timetable for which is determined by Stagecoach, the installation of equipment on First vehicles would be complete by July 2015.

53. The quarterly Projects reports also outline progress made for a range of other projects, including Sustainable Travel Awareness, Urban Cycle Networks and a project to improve accessibility to the SESTRAN ports and linkages to Europe.

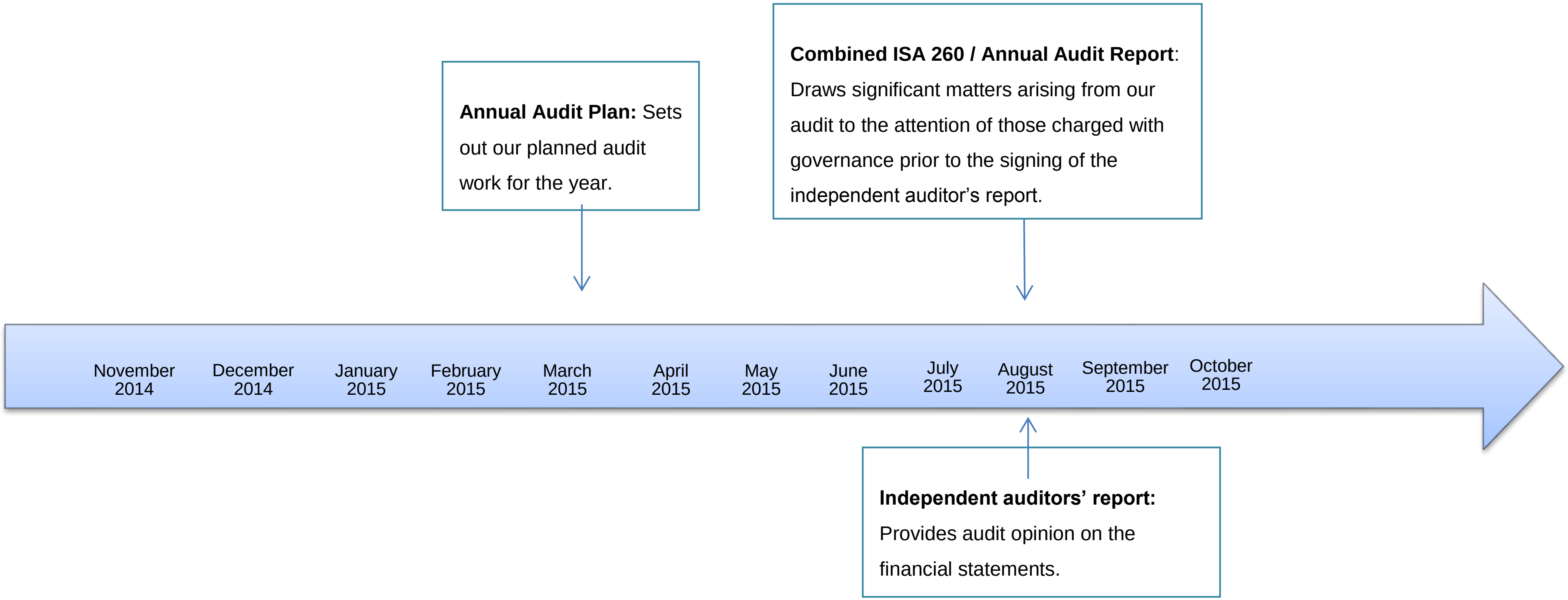
Appendix 1 – Audit risks

The table below sets out the financial statement audit risks we identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

Audit Risk	Assurance procedure	Results and conclusions
Risk of material misstatement		
Income SEStran receives a significant amount of income in addition to SG funding. The complexity of income means there is an inherent risk of fraud in accordance with ISA240.	• Detailed substantive testing of revenue transactions focusing on the areas we consider to be of greatest risk.	• No fraud identified from substantive testing performed.
Management override of controls As stated in ISA 240, management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.	• Detailed testing of journal entries • Review of accounting estimates for bias • Evaluating significant transactions that are outside the normal course of business.	• No issues identified from testing performed.
Receipt of European funding There is a risk that budgets will not be achieved if future settlements from Europe include significant common management costs which have not been provided for within the budget.	• Substantive testing of grant funding debtors as part of financial statement programme.	• No specific issues re. management costs identified however an issue re. recoverability of ERDF debtor has been raised.

Audit Risk	Assurance procedure	Results and conclusions
Depreciation Policy With the exception of the RTPI assets, all of SEStrans assets have been fully depreciated but are still in use. There is a risk that the existing depreciation policy does not fully reflect the consumption of economic benefit of assets.	• Consideration of appropriateness of revised asset lives. • Detailed testing of fixed assets.	• No issues identified from testing performed.

Appendix 2 – Summary of local audit reports 2014/15



Appendix 3 – Action plan

No. Page/para	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
1 **13/38**	**VAT not reclaimed:** During testing of creditors, we identified an instance where a VAT invoice had not been passed on to finance officers, resulting in VAT of £401 not being reclaimed from HMRC. **Risk:** The Partnership may not recover VAT paid **Recommendation:** Relevant officers are reminded of the correct procedures for dealing with VAT invoices.	Officers of the Partnership have been reminded of invoice payment procedures to ensure all VAT costs are correctly recovered.	Treasurer and Office Manager	30 September 2015