Scott-Moncrieff
business advisers and accountants

South East of Scotland Transport Partnership

2017/18 Annual Audit Report to members of South East of Scotland Transport Partnership and the Controller of Audit

September 2018

Contents

Key messages

Annual accounts

South East of Scotland Transport Partnership (SESTRAN) annual accounts for the year ended 31 March 2018 were approved by the Partnership on 21 September 2018.

We reported within our independent auditor's report an unqualified opinion on the annual accounts and on other prescribed matters. There are no matters which we are required to report by exception.

Our thanks go to management and staff for their assistance with our work.

Key facts

- The Partnership spent £1.608million on the delivery of services in 2017/18.
- The Partnership recorded an underspend of £16,000 against constituent council requisitions for 2017/18. At the Partnership meeting on 22 June 2018 the Partnership approved the carry forward of the underspend to 2018/19 for use on the Sustainable and Active Travel Grant Scheme.
- Operational equipment for the regional real-time passenger travel information system was purchased in the year totalling £0.177million, which was funded from Capital Funded from Current Revenue (CFCR).
- The Partnership reported an accounting surplus of £39,000.
- The Partnership has approved a balanced budget of £1.253million for 2018/19.

Wider scope

As outlined in our External Audit Plan, our annual audit work in respect of our wider scope audit responsibilities was restricted to:

- Audit work to allow conclusions to be made on the appropriateness of the disclosures in the Annual Governance Statement; and
- Consideration of the financial sustainability of the organisation and the services that it delivers over the medium and longer term.

Our conclusions and key observations are set out below:

Governance statement	• We reviewed the Partnership's 2017/18 annual governance statement and concluded that it has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016). • However, as part of our work on the systems of internal control we identified a significant governance weakness relating to approval of invoices. We requested additional disclosure in the annual governance statement outlining the issue and the actions the Partnership plans to take to address the issue.

Financial sustainability	• The Partnership has arrangements in place for short term (1 year) financial planning, with budgets aligned to its annual business plan and its 10 year Regional Transport Strategy (2015-2025). However, the Partnership has noted that there is a large degree of uncertainty over funding allocations from council requisitions and the Scottish Government, and therefore does not prepare medium to long-term financial plans. In line with our prior year recommendation, we recommend that further work is carried out to consider the long term financial priorities of the Partnership. • The Transport (Scotland) Bill was introduced to Parliament on 8 June 2018. The most significant potential impact for the Partnership is that regional transport partnerships would be given the authority to hold reserves. This would provide the Partnership with greater financial flexibility and help facilitate longer term financial planning.

Conclusion

This report concludes our audit for 2017/18. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK) and Ethical Standards.

Scott-Moncrieff
September 2018

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Introduction

This report is presented to those charged with governance and the Controller of Audit and concludes our audit of the Partnership for 2017/18.

We carry out our audit in accordance with Audit Scotland's Code of Audit Practice (May 2016). This report also fulfils the requirements of International Standards on Auditing (UK) 260: Communication with those charged with governance.

We have designated the Partnership's Performance and Audit Committee as "those charged with governance".

Introduction

1. This report summarises the findings from our 2017/18 audit of the South East of Scotland Transport Partnership ("the Partnership").

2. The scope of our audit was set out in our External Audit Plan which was presented to the Partnership in March 2018. The core elements of our audit work in 2017/18 have been:

- an audit of the 2017/18 annual accounts; and
- consideration of the Partnership's arrangements for securing financial sustainability.

3. The Partnership is responsible for preparing annual accounts that show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified in this report are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the annual accounts 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.

4. This report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding appropriate actions. We give each recommendation a grading to help the Partnership assess their significance and prioritise the actions required.

5. We would like to thank management and staff who have been involved in our work for their co-operation and assistance during our audit work.

Confirmation of independence

6. International Standards on Auditing in the UK (ISAs (UK)) require us to communicate on a timely basis all facts and matters that may have a bearing on our independence.

7. We confirm that we have complied with Financial Reporting Council's (FRC) Revised Ethical Standard (June 2016). In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way.

Adding value through the audit

8. All of our clients quite rightly demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the Partnership through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Partnership promote improved standards of governance, better management and decision-making and more effective use of resources.

Feedback

9. Any comments you may have on the service we provide, the quality of our work and our reports would be greatly appreciated at any time. Comments can be reported directly to the audit team or through our online survey: *www.surveymonkey.co.uk/r/S2SPZBX*

10. This report is addressed to both the Partnership and the Controller of Audit and will be published on Audit Scotland's website. *www.audit-scotland.gov.uk*.

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Annual accounts

The Partnership's annual accounts are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

In this section we summarise the findings from our audit of the 2017/18 annual accounts.

Annual accounts

The annual accounts for the year ended 31 March 2018 were approved by the Partnership on 21 September 2018. We reported unqualified opinions within our independent auditor's report.

The Partnership has appropriate administrative processes in place to prepare the annual accounts and the required supporting working papers.

Overall conclusion

An unqualified audit opinion on the annual accounts

11. The annual accounts for the year ended 31 March 2018 were approved by the Partnership on 21 September 2018. We reported, within our independent auditor's report:

- an unqualified opinion on the annual accounts; and
- an unqualified audit opinion on other prescribed matters.

12. We are also satisfied that there are no matters which we are required to support by exception.

Appropriate administrative processes were in place

13. We received draft annual accounts and supporting papers of an appropriate standard, in line with our agreed audit timetable. Our thanks go to management and staff at the Partnership and City of Edinburgh Council for their assistance with our audit work.

Our assessment of risks of material misstatement

14. The assessed risks of material misstatement described in Exhibit 1 are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the audit team. Our audit procedures relating to these matters were designed in the context of our audit of the annual accounts as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the annual accounts is not modified with respect to any of the risks described in Exhibit 1 below.

Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

1. Management override

In any organisation, there exists a risk that management have the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the annual accounts. This is treated as a presumed risk area in accordance with ISA 240(UK) – *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Excerpt from the 2017/18 External Audit Plan

15. We have not identified any indications of management override in the year. We have reviewed the Partnership's accounting records and obtained evidence to ensure that transactions outside the normal course of business were valid and accounted for correctly. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.

16. During our prior year audit, we noted that there was a lack of segregation of duties in respect of posting of journals. Journals are still posted without authorisation however an additional monitoring control has been implemented in 2017 whereby the Partnership Business Manager now receives transaction listings for review. We consider the

Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

arrangements put in place to be appropriate to the organisation. Full details of our follow up work are outlined in Appendix 1.

17. We also noted, during our 2017/18 audit, that user access controls to the financial ledger could be strengthened. At present, any member of the City of Edinburgh Council finance team with ledger access could post to the Partnership's financial ledger. While any incorrect postings should be picked up through budget monitoring there is a risk that mis-postings are not detected resulting in errors in the financial statements.

Action plan point 1

2. Revenue recognition

Under ISA 240 (UK) – *The auditor's responsibilities relating to fraud in an audit of financial statements* there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the Partnership could adopt accounting policies or recognise revenue transactions in such a way as to lead to a material misstatement in the reported financial position.

Excerpt from the 2017/18 External Audit Plan

18. We have gained reasonable assurance on the completeness and occurrence of income and we are satisfied that income is fairly stated in the annual accounts. To inform our conclusion we evaluated the Partnership's key revenue streams and reviewed the controls in place over revenue accounting. We also carried out testing to confirm that the revenue recognition policy is appropriate and was consistently applied throughout the year.

3. Risk of fraud in the recognition of expenditure

In 2016, the Public Audit Forum issued Practice Note 10 "The Audit of Public Sector Financial Statements" which applies to the audit of public sector financial statements for periods commencing after June 2016. This Practice Note recognises that most public sector bodies are net spending bodies and notes that there is an increased risk of material misstatement due to improper recognition of expenditure.

Excerpt from the 2017/18 External Audit Plan

19. While we did not suspect incidences of material fraud and error, we evaluated each type of expenditure transaction and documented our conclusions. We have gained reasonable assurance on the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the annual accounts. To inform our conclusion, we carried out testing to confirm that the Board's policy for recognising expenditure is appropriate and has been applied consistently throughout the year. We did however note the following during our review:

20. The Partnership Director has been on leave since December 2017. We found during our audit work that appropriate contingency arrangements for the approval of expenditure were not in place.

21. Since its creation as a statutory body, the process to pay invoices has required that the Partnership Director sign invoices of a value greater than £2,000 and during the Partnership Director's holiday period, invoices with a value greater than £2,000 be signed by a nominated officer, in consultation with the Partnership Chair. Following the Partnership

Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

Director's absence in December 2017, it was agreed by officers that the Chair of the Partnership would provide approval of invoices above £2,000 with an officer certifying. For the 2017/18 financial year, the Chair approved and was a second signatory on total expenditure of £1.1million. This arrangement was not communicated and approved by either the Performance and Audit Committee or the Partnership Board.

22. The role of Chair should be independent to enable them to provide effective challenge and scrutiny to officers. The Audit Scotland report on *The Role of Boards*[1] notes that for a Board to be effective they should not become involved in the daily running and operation of the organisation. This is in line with other standards of good governance published by the Scottish Government and the Independent Commission on Good Governance in Public Services[2]. The Chair's approval of invoices is seen to be an operational role and presents a significant risk to the Board's ability to independently scrutinise the functions of the Partnership.

Action Plan Point 2

23. We conducted audit testing over those transactions which were approved by the Chair. We confirmed that these transactions were in the normal course of business for the Partnership.

4. Property, plant and equipment

Following auditor queries in 2016-17, a full impairment review of the Real-Time Passenger Information system was undertaken. This resulted in a prior year audit adjustment of £2.095million and an adjustment of £1.722million in the annual accounts (bringing the 2016/17 impairment to £1.918million from £0.196million in the unaudited annual accounts).

From our review of the operation of the fixed asset register we identified issues in recording and valuing assets. Assets are not individually recorded in the fixed asset register and are grouped by type. This resulted in significant issues verifying the number of assets and value per item. The Partnership has indicated that there will be significant additions in 2017/18. There is therefore a risk that the new assets are not brought into the asset register and annual accounts appropriately.

Excerpt from the 2017/18 External Audit Plan

24. The Partnership incurred £177,000 on property, plant and equipment during the year in relation to operational equipment for the regional real-time bus passenger travel information system.

25. We have gained reasonable assurance that the capital additions have been accounted for appropriately and in line with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 ('the Code').

26. We have reviewed the steps taken by officers to improve the maintenance of the fixed asset register in 2017/18. We have observed a number of improvements in the information recorded within the asset register and have noted an increase in the number of assets that have been tagged. However, further improvements could be made to ensure a consistent level of detail is provided on the asset register for each category of assets. The asset register should include the same level of detail for each category of asset.

Prior Year Action Plan Point 2

[1] http://www.audit-scotland.gov.uk/docs/central/2010/nr_100930_role_boards.pdf
[2] https://www.jrf.org.uk/report/good-governance-standard-public-services

Our application of materiality

27. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the annual accounts.

28. Our initial assessment of materiality for the annual accounts was £28,000. We revised our assessment following receipt of the unaudited annual accounts to £16,000 and it remained at this level throughout our audit. Our assessment of materiality equates to approximately 1% of the Partnership's expenditure. We consider this to be a principal consideration for the users of the accounts when assessing the performance of the Partnership.

Performance materiality

29. Performance materiality is the amount set by the auditor at less than overall materiality for the annual accounts as a whole to reduce to an appropriately low level the probability that the aggregate of the uncorrected and undetected misstatements exceed materiality for the annual accounts as a whole.

30. We set a performance (testing) materiality for each area of work based on a risk assessment for the area and percentage application of overall materiality. We then perform audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we are performing a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are set out in the table below:

Area risk assessment	Weighting	Performance materiality
High	40%	£6,400
Medium	50%	£8,000
Low	65%	£10,400

31. We agreed with the Partnership that we would report all audit differences in excess of 5% of the overall materiality figure, as well as differences below that threshold which, in our view, warranted reporting on qualitative grounds. We would also report to the Partnership on disclosure matters that we identified when assessing the overall presentation of the annual accounts.

Audit differences

32. We identified one material adjustment to the annual accounts in relation to the estimates applied in calculating the defined benefit pension liability and associated movements. We identified one additional adjustment of £12,000 was made in relation to the treatment of assets under construction. This adjustment did not impact on the figures disclosed within the primary statements.

33. These adjustments have been discussed with management and are reflected in the final set of annual accounts.

Adjustment to the defined benefit pension liability

34. The timing of the request for actuarial reports means that actuaries produce IAS 19 actuarial reports using estimated figures.

35. The validity of the information provided to the actuary has been compared with the actual information reported by the Partnership and Lothian Pension Fund. This review highlighted a risk of material misstatement arising from difference between the figures relating to asset values.

36. We requested that management instruct the actuary to update its calculations based on year end results; the results of which have been incorporated into the annual accounts.

37. The difference between actual and estimated figures for investment returns resulted in a reduction of £34,000 to the net pension liability with an associated increase to total comprehensive income and expenditure.

38. This adjustment has been discussed with management and is detailed within an appendix to the letter of representation.

39. We confirm there were no unadjusted differences to the accounts.

40. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual accounts.

41. We have requested that a signed representation letter be presented to us at the date of signing the annual accounts. This letter is to be signed by the Treasurer.

An overview of the scope of our audit

42. The scope of our audit was detailed in our External Audit Plan, which was presented to the Partnership in March 2018. The plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the Partnership. This ensures that our audit focuses on the areas of highest risk. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.

43. At the planning stage we identified the significant risks that had the greatest effect on our audit. Audit procedures were then designed to mitigate these risks.

44. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical review. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit management team. In performing our work, we have applied the concept of materiality, which is explained earlier in this report.

Other matters identified during our audit

45. During the course of our audit we noted the following:

Pension Liability

46. As at 31 March 2018 the net pension liability was £0.662million, an increase of £0.355milion in comparison to the net pension liability as at 31 March 2017 (£0.307million).

47. Due to the significant movement in comparison with the prior year, the Partnership sought further clarification from the Actuary.

48. The movement is primarily as a result of the triennial valuation of the Lothian Pension Fund (carried out as at 31 March 2017). The actuarial valuation for the 31 March 2018 is the first year that the results of the triennial valuation are taken into account. In the interim years between triennial valuations, actuarial valuations are based on rolled forward data rather than a full valuation.

49. As a small employer, the Partnership can experience significant movements in its pension asset/liability if employees transfer in to the scheme or retire. This is represented through the 'other experience' movement through the Comprehensive Income and Expenditure Statement (2017/18 £0.499million).

Going concern

50. As at 31 March 2018, the Partnership reported a net liability position of £0.247million.

51. In line with the Transport Scotland Act 2005, the Partnership does not hold useable reserves. The balance on the unusable reserves reduced to a net liability position of £0.247million. This is due to the net pension liability of £0.662million as at 31 March 2018.

52. In the Partnership's opinion, the organisation will be able to continue for the foreseeable future. The Partnership has adequate budget to meet the ongoing employer contributions required by Lothian Pension Fund.

The Local Authority Accounts (Scotland) Regulations 2014

53. As part of our audit, we reviewed the Partnership's compliance with the Local Authority Accounts (Scotland) Regulations 2014, in particular with respect to regulations 8 to 10[3] as they relate to the annual accounts. Overall, we concluded that appropriate arrangements are in place to comply with these Regulations.

Management commentary

54. We are satisfied that the information given in the management commentary is consistent with the financial statements and has been prepared in accordance with the statutory guidance issued under the Local Government Scotland Act 2003.

Remuneration report

55. Our independent auditor's report confirms that the part of the remuneration report to be audited has been properly prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014.

Annual governance statement

56. We have reviewed the annual governance statement and have found that it is consistent with the accounts and has been prepared in accordance with the Delivering Good Governance in Local Government Framework (2016).

57. The Treasurer of the Partnership has confirmed that in their opinion, reasonable assurance can be placed upon the adequacy and effectiveness of the systems of internal financial control.

58. We considered the content of the governance statement in the unaudited annual accounts and noted that there was no disclosure of the arrangements put in place while the Partnership Director was absent from service from 8 December 2017 to 31 March 2018. We raised this with management and additional disclosures have been added to the governance statement.

59. We noted a significant governance weakness as part of our testing of expenditure (Paragraph 21). We requested that the governance statement was updated to reflect the issue and the actions that the Partnership would take to address this and the other governance weaknesses identified in 2017/18.

60. We further observed that the Chair acted as a temporary Chair of the Performance and Audit Committee in the absence of the appointed Chair. It is not best practice[4] for the Chair to act in this role as it reduces their ability to effectively challenge the Performance and Audit Committee at Board meetings. We recommend a review of governance arrangements is considered to identify a suitable deputy for the Performance and Audit Committee.

Action Plan point 3

Internal audit

61. The Partnership's internal audit function is provided by City of Edinburgh Council's Internal Audit service. We have taken cognisance of the work of internal audit in forming our opinion on the appropriateness of the disclosures in the annual governance statement.

62. Internal audit provided an 'amber' rated finding reflecting that the Partnership's control environment and governance and risk management frameworks are generally adequate which is reflected in the overall certification.

Accounting and internal control systems

63. The Partnership has systems in place to record, process, summarise and report financial and other relevant data. We have identified areas for improvement with respect of user access to the financial ledger and the approval of invoices. We outline the issues identified and our recommendations at Appendix 1.

64. In addition we have followed up on progress in implementing actions raised in the prior year. We have concluded that while progress has been made in year in implementing our recommendations, a number are still to be fully implemented. Full details of our findings are included in Appendix 1.

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[3] Regulations 8 to 10 relates to the preparation and publication of unaudited accounts, notice of public right to inspect and object to the accounts and consideration and signing of the audited accounts.

[4] https://www.cipfa.org/policy-and-guidance/publications/a/audit-committees-practical-guidance-for-local-authorities-and-police-2018-edition-online

Legality

65. We planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual accounts. Our audit procedures include the following:

- Reviewing minutes of relevant meetings;
- Enquiring of senior management and the Partnership's solicitors the position in relation to litigation, claims and assessments; and
- Performing detailed testing of transactions and balances.

66. We are pleased to report that we did not identify any instances of concern with regard to the legality of transactions or events.

Cyber security

67. In May 2017, a number of public sector bodies across Scotland were impacted by the Wannacry global ransomware attack. In response to this the Scottish Government launched 'A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017/18'.

68. The action plan outlines a number of requirements that public sector bodies should be taking forward. This includes an action for public sector bodies to achieve Cyber Essentials Plus certification by the end of October 2018.

69. The Partnership has presented regular updates to the Board and Performance and Audit Committee on the progress in achieving the Cyber Essentials Plus Certification. In June 2018, the Performance and Audit Committee approved that the Cyber Essential Plus accreditation is pursued.

70. We understand that the Partnership is on track to achieve the accreditation in line with the deadlines.

General Data Protection Regulations

71. The General Data Protection Regulations (the Regulations) came into force in the UK on 25 May 2018. The Regulations replace the Data Protection Act 1998 and as well as strengthening existing Regulations, the Act has brought in new legislative duties for the Partnership. The Regulations bring significant potential penalties for non-compliance.

72. Partnership staff attended GDPR awareness training during 2017/18 and the role of data protection officer is being fulfilled by the Partnership Business Manager. The Partnership's revised privacy statement was published on the website in May 2018.

73. Compliance with the Regulations is an ongoing process, which we will monitor as part of our annual audit procedures. We have not identified any significant issues at this stage.

Qualitative aspects of accounting practices and financial reporting

74. We have considered the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the annual accounts. Our findings are summarised in the following table:

Qualitative aspect considered	Audit conclusion
The appropriateness of the accounting policies used.	The accounting policies, which are disclosed in the annual accounts, are considered appropriate to the Partnership and are in line with the (the Code).
The timing of the transactions and the period in which they are recorded.	We did not identify any concerns over the timing of transactions or the period in which they were recognised.
The appropriateness of the accounting estimates and judgements used.	We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the annual accounts. Estimates have been made in relation to property, plant and equipment and pensions. We consider the estimates made, and the related disclosures, to be appropriate to the Partnership. Pension estimates have been informed by advice from qualified, independent experts. We evaluated the competence, objectivity and capability of managements' experts in line with the requirements of ISA (UK) 500.
The appropriateness of the going concern assumption	We have reviewed the detailed financial forecasts for 2018/19. Our understanding of the legislative framework and activities undertaken provides us with sufficient assurance that the Partnership will continue to operate for at least 12 months from the signing date.
The extent to which the annual accounts have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed.	From the testing performed, we identified no significant unusual transactions in the period.
Apparent misstatements in the management commentary or material inconsistencies with the annual accounts.	The management commentary contains no material misstatements or inconsistencies with the accounts.
Any significant annual accounts disclosures to bring to your attention.	There are no significant annual accounts disclosures that we consider should be brought to your attention. All the disclosures required by relevant legislation and applicable accounting standards have been made appropriately.
Disagreement over any accounting treatment or annual accounts disclosure.	While disclosure and presentational adjustments were made during the audit process there was no material disagreement during the course of the audit over any accounting treatment or disclosure.
Difficulties encountered in the audit.	There were no significant difficulties encountered during the audit.

3

Financial sustainability

Financial sustainability looks forward to the medium and longer term to consider whether the Partnership is planning effectively to continue to deliver its services or the way in which they should be delivered.

Financial sustainability

The Partnership operated within budget in 2017/18 and has presented a balanced budget for 2018/19.

The Partnership does not have financial plans in place for the medium to long term due to uncertainty around funding. There is a risk that long term priorities are not planned for appropriately due to a focus on short term financial pressures.

The Transport (Scotland) Bill was introduced to Parliament on 8 June 2018. The most significant potential impact for the Partnership is that regional transport partnerships would be given the authority to hold reserves.

Significant audit risk

75. As outlined in our audit plan, we considered there to be a significant risk to the wider scope of our audit in relation to financial sustainability:

Exhibit 2: Key audit risk: financial sustainability

Financial sustainability

The Partnership produced a Regional Transport Strategy (2015-2025) and a supporting business plan for 2017-18. While the strategy sets out the long-term objectives of the Partnership, revenue funding is generally only confirmed for the forthcoming financial year. This therefore challenges the Partnership's ability to agree detailed long-term plans and objectives.

In addition, the review of the Transport (Scotland) Bill may result in changes to the operation of the Partnership, which cannot currently be reflected in long-term financial planning.

Excerpt from the 2017/18 External Audit Plan

76. In line with our findings in 2016/17 there has been no financial planning for the medium to longer term.

77. The Partnership has made expenditure decisions on an annual basis based on the level of funding available. There is therefore a risk that long term priorities are not appropriately planned for as the Partnership focuses on addressing short term financial pressures.

78. The Partnership receives annual allocations both from Scottish Government and constituent councils and therefore finds it difficult to plan further ahead. However, in recent years, both funding sources have remained generally consistent with only minor reductions observed with respect of council requisitions.

79. The Transport (Scotland) Bill was introduced to Parliament on 8 June 2018. The Bill is currently in the call for evidence period, which is due to end in September 2018. The most significant potential impact for the Partnership is that regional transport partnerships would be given the authority to hold reserves. This would provide the Partnership with greater financial flexibility and help facilitate longer term financial planning.

Prior Year Action Plan Point 6

Exhibit 2: Key audit risk: financial sustainability

80. We will continue to monitor the outcome of the call for evidence period on the Transport (Scotland) Bill and consider the impact on long term financial planning in 2018/19.

The Partnership's financial performance in 2017/18

81. The Comprehensive Income and Expenditure Statement for 2017/18 shows that the Partnership spent £1.608million on the delivery of services, resulting in an accounting surplus of £0.39million. However, the accounting surplus includes certain elements of income and expenditure that need to be accounted for to comply with the Code of Practice on Local Authority Accounting in the United Kingdom (the 2017/18 Code), and which are subsequently adjusted to show their impact on reserves.

82. Taking account of these adjustments, the Partnership reported a breakeven position.

2017/18 outturn position

83. The Partnership reduced expenditure in year on both core service and revenue projects which resulted in a £0.016million underspend against budget. This was matched by a reduction in the income giving an overall breakeven position.

Exhibit 3: Revenue performance against budget

	Revised Budget £'000	Actual £'000	Variance £'000
Core	487	444	(43)
Projects	839	1,154	315
Interest	1	-	(1)
Total Expenditure	**1,327**	**1,598**	**271**
Government grant	(782)	(782)	-
Constituent council requisitions	(190)	(174)	16
Other income	(355)	(642)	(287)
Total Income	**(1,620)**	**(1,598)**	**(271)**
Total	**-**	**-**	**-**

Source: *Annual accounts for the year ended 31 March 2018*

84. While the Partnership achieved a breakeven position, there was a significant overspend of £0.315million against the revenue projects budget. The Partnership however secured additional income from EU grants and SUStrans in the year to ensure the breakeven position was achieved.

85. The Partnership recorded an underspend of £16,000 against constituent council requisitions for 2017/18. At the Partnership meeting on 22 June 2018 the Partnership approve the carry forward of the underspend to 2018/19 for use on the Sustainable and Active Travel Grant Scheme

Financial planning

Indicative 2018/19 budgets

86. The Partnership has set a balanced budget for 2018/19. This is based on a reduction of income in 2018/19 of 6% reducing from £1.327million to £1.253million. The Partnership's budget is funded through Scottish Government funding of £0.782million and Council requisitions of £0.190million alongside external funding of £0.281million from EU grants and other sources.

87. The reduction in income for 2018/19 has been offset by a reduction in Real Time Passenger Information (RTPI) expenditure of £0.231million. The reduction of RTPI expenditure largely related to a decrease maintenance costs. This is as a result of a small number of bus providers using alternative systems.

88. There are increases in core and project expenditure respectively of £0.053million, relating to increases in employee costs and £0.104million, predominantly relating to the Surflogh project, which is EU funded.

EU withdrawal

89. One of the Partnership's primary funding sources is through the European Union grants. EU grants funding received was £0.280million in 2017/18 compared to £0.111million in 2016/17. This accounted for 44% of project income in the year and 17% of income on provision of services. The Partnership is continuing to explore other funding opportunities as well as regular engagement with EU partners. There has been regular reporting around the impact of EU Withdrawal on funding to the Partnership Board and also features on the Partnership's risk register.

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Appendices

Appendix 1: Management action plan

Our action plan details the control weaknesses and opportunities for improvement that we have identified during our audit.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist. The weaknesses or risks identified are only those which have come to our attention during our normal audit work, and may not be all that exist.

Communication of the matters arising from the audit of the annual report and accounts 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.

Action plan grading structure

To assist the Partnership in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated. The rating structure is summarised as follows:

Grade 5	Very high risk exposure – major concerns requiring Partnership attention
Grade 4	High risk exposure – material observations requiring senior management attention
Grade 3	Moderate risk exposure – significant observations requiring management attention
Grade 2	Limited risk exposure – minor observations requiring management attention
Grade 1	Efficiency / housekeeping point

Action plan point	Issue, Risk & Recommendation	Management Comments
1. User access controls **Rating** **Grade 3** **Paragraph ref** **17**	**Issue** Our review of the journals environment identified that all City of Edinburgh Council staff with access to Oracle journal input function in the financial ledger system, have the ability to post to the Board's financial ledger. **Risk** There is a risk that incorrect or fraudulent postings could be made without detection by the Board's officers. **Recommendation** While our audit review in respect of the 2017/18 financial year did not identify any indications of user access being manipulated, we recommend that Partnership officers in conjunction with City of Edinburgh Council review user access controls for the financial ledger.	**Responsible officer:** Treasurer/Partnership Director **Implementation date:** Immediate The City of Edinburgh Council is undertaking an investigation into the technical requirements and cost implications of introducing additional user access controls for journal entry input to the financial ledger.

Action plan point	Issue, Risk & Recommendation	Management Comments
2. Authorisation of invoices **Rating** **Grade 5** **Paragraph ref** **22**	**Issue** The Partnership Director has been absent since December 2017. In the interim, an arrangement was put into place where the Chair of the Board would approve invoices greater than £2,000 before passing to City of Edinburgh Council finance for payment. This arrangement was not reported to the Board or Performance and Audit Committee and does not demonstrate good governance. **Risk** There is a risk that the Chair cannot provide effective challenge or scrutiny to officers due to involvement in operational decision making. **Recommendation** The Partnership should ensure that all invoices that were approved by the Chair are reported to the Performance and Audit Committee and Board. Moving forward, the schedule of Certifying Officers and Limits of Authority should be revised to require two officer signatures.	**Responsible officer:** Treasurer **Implementation date:** Immediate Since its creation as a statutory body, the process to pay Partnership invoices has required that the Partnership Director sign invoices of value greater than £2,000 and during the Partnership Director's holiday period, invoices with a value greater than £2,000 be signed by a nominated officer, in consultation with the Partnership Chair. Once relevant signatures are obtained by the Partnership, invoices are passed to the Finance Team in the City of Edinburgh Council for scrutiny by a Principal Accountant and Accountant, before being passed to the Council's invoice Payment Team. The Invoice Payment Team review invoices to ensure the supplier is an approved supplier, before payment is processed. Scrutiny of all payments is made as part of the quarterly financial performance reporting to the Partnership Board. In addition, any invoice payment subject to European grant funding is subject to review by external auditors who are appointed as part of the EU grant funding process. A report will be presented to the Partnership's Performance and Audit Committee on 7th September 2018, detailing all invoice payments signed by the Partnership Chairperson, during the Partnership Director's absence. A report will be presented to the Partnership Performance and Audit Committee on 7th September 2018 detailing changes to the schedule of Certifying Officers and Limits of Authority, to revise this to require two officer signatures. During any absence of the Partnership Director, any invoice payment requests in excess of £2,000 will be counter-signed by a Principal Accountant of the City of Edinburgh Council; this in addition to signature by two officers of the Partnership.

Action plan point	Issue, Risk & Recommendation	Management Comments
3. Governance Scheme **Rating** **Grade 3** **Paragraph ref** **60**	**Issue** During 2017/18, a number of independent members' terms of appointment came to an end including the Chair of the Performance and Audit Committee. For a single meeting, the Chair of the Board acted as Chair of the Performance and Audit Committee until a permanent Chair could be appointed by the Partnership Board to the Committee. Audit Committees: Practical Guidance for Local Authorities and Police (CIPFA, 2018) states that organisations 'should adopt a model that establishes the committee as independent and effective.' Best practice recommends that the Chair should not be permitted to be a member of the Performance and Audit Committee. **Risk** There is a risk that the Performance and Audit Committee is not operating independently and could not provide effective scrutiny and challenge to officers. **Recommendation** The Partnership has reviewed their Governance Scheme following a recommendation from internal audit. We recommend that a further review is conducted specifically considering whether the Chair of the Partnership should be entitled to substitute for any member of the committee. CIPFA have recently published a reviewed Audit Committee guide and we further recommend that the Committee performs a self-assessment against the guide.	**Responsible officer:** Head of Programmes **Implementation date:** First part complete, second part by end December 2018 Ministerial approval for the appointments of the new Non-Councillor Members was not granted within the expected timeframe, resulting in the Performance and Audit Committee not having full Non-Councillor Member representation, or a Chair, for the June 2018 meeting. There were concerns that the meeting would not be quorate and as the Governance Scheme states that the Chair of the Partnership is entitled to substitute for any member of the Committee, it was considered appropriate, as an emergency measure, for him to Chair a one-off meeting. At the 22 June Partnership Board meeting, appointments to the Performance and Audit Committee were made, including a permanent Chair. In respect of the Chair being able to substitute for any member of the committee, a further review of the Governance Scheme will be carried out and reported to the December Partnership Board.

Follow up of prior year audit recommendations

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
1. Authorisation of journals **Rating** **Grade 3**	**Observation** Our review of the journals environment found that there was a lack of segregation of duties over the posting of journals. Journals are prepared and posted without any secondary review or authorisation. Journals can be used to override controls and create fraudulent errors therefore, it is essential appropriate controls are in place **Recommendation** While our audit review in respect of the 2016/17 financial year did not identify any indications of management override we recommend that a review process is put in place for the preparation and posting of journals to the ledger.	**Action owner:** Treasurer **Due Date:** Immediate Expenditure and Income monitoring reports are prepared in full consultation with officers of the Partnership for reporting to the Partnership Board on a quarterly basis, in line with the Financial Regulations of the Partnership. Any exceptional or unanticipated expenditure or income created by journal entry would be identified through this process. To enhance control, Partnership officers will receive a monthly report to include details of all journal entries processed, for review. Strict separation of financial controls, segregation of duties and authorisation levels exist for all actual expenditure transactions of the Partnership.	**Action Complete** While segregation of duties has not been introduced, an additional control has been implemented whereby monthly reports detailing all ledger transaction are provided by the Partnership officers.

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
2. Asset recording and tagging **Rating** **Grade 4**	**Observation** Assets within the asset register are not allocated a unique reference number and are instead grouped by type. In addition to this the physical assets are not individually labelled. It is therefore not possible to undertake a physical verification of assets from the register to the floor (or vice versa). There has been significant issues verifying the number of assets held and the value per item in year **Recommendation** To ensure assets are accounted for appropriately and prevent against the possible misappropriation of assets, we recommend that new assets acquired, across all sites are: • brought into the fixed asset register with sufficient detail to allow each unit to be individually identifiable including purchase date and value per item; and • appropriately labelled when brought into use to create a direct link between the fixed asset register and the physical assets.	**Action owner:** Partnership Director **Due Date:** 31 March 2018 The Partnership Director has instructed that the Projects team oversee the creation of a full and comprehensive asset register for the Partnership.	**Action partially complete** While significant work has been undertaken by officers to improve the asset register. For example, information on the different types of asset are not recorded in the same manner. We would recommend that as a minimum the asset register includes: • Asset number • Asset category • Asset description • Asset location • Date of addition • Asset gross book value • Depreciation Charge • Asset Net book value **Management comments:** SEStran appreciates the acknowledgement that significant work has been done, to date and that the presentation of the information can be improved. Accordingly, work will continue to complete the Fixed Asset Register, ensuring that all necessary information is included and that it is presented in a consistent manner. **Responsible officer:** Head of Programmes **Implementation date:** 31 December 2018

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
3. Registers of Interest **Rating** **Grade 3**	**Observation** From our review of the Registers of Interests of members it was found that a number of the declarations forms had not been updated since 2014. Upon further review we identified an undisclosed related party transaction of £0.086million relating to an undeclared related party for Edinburgh and Lothians Greenspace Trust. The annual accounts have been updated to reflect the appropriate disclosures. **Recommendation** The Partnership should ensure registers of interest are updated on at least an annual basis	**Action owner:** Partnership Director **Due Date:** 31 December 2017 All members of the Partnership Board are reminded and have been in Summer 2017 of the provision of regulations which provide for Board Members to give notice of registerable interests as outlined in the Partnership Code of Conduct and all members of the Board at the first meeting of the new session has been reminded of their Code of Conduct responsibilities. Keeping entries in the Register of Interests up to date is ultimately the responsibility of individual Members. The Secretary of the Partnership is the proper officer for these purposes. We should stress that they receive an annual reminder	**Action partially complete** We again noted that two members have not disclosed their role as a trustee of Edinburgh and Lothians Greenspace Trust. In 2017/18, there was again a material transaction with this organisation which officers have disclosed within the accounts. Members should ensure their register of interests is both up-to-date and accurately completed. **Management comments:** The members concerned have been advised of the omissions and the necessary interests have now been recorded. Code of Conduct training is arranged for 21 September 2018. **Responsible officer:** Secretary to the Partnership **Implementation date:** 21 September 2018

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
4. Reconciliation of holding accounts **Rating** **Grade 2**	**Observation** The City of Edinburgh Council maintains a holding account on behalf of the Partnership. The holding account is reconciled on an annual basis. There is a risk that any errors in the allocation of items to the holding account are not discovered timeously. **Recommendation** The holding account should be reconciled with the Partnership records on a regular basis to reduce the risk of significant error.	**Action owner:** Treasurer **Due Date:** 31 December 2017 The indebtedness between the City of Edinburgh Council and the Partnership, as reflected in the holding account balance, was reconciled a number of times during 2016/17. The frequency of reconciliation will be formalised such that reconciliations will be undertaken on a quarterly basis.	**Action complete** The frequency of the holding account reconciliation has been formalised and we did not identify any issues during audit work with respect of the holding account balance.

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
5. Income and expenditure controls **Rating** **Grade 3**	**Observation** While income and expenditure testing did not identify any misstatements to the annual accounts, we did identify a number of errors relating to income and expenditure invoice processing. Income and expenditure invoices are sent to City of Edinburgh Council alongside a cover sheet that details the VAT coding, ledger coding and supplier/customer details. We found that the details on cover sheets were often incorrect which resulted in credit notes being raised on numerous occasions. Income invoices were also found to have a number of errors in year which resulted in an under declaration of output tax of £12k (disclosed in the accounts as a debtor and creditor). A voluntary disclosure to HMRC was made in relation to this. As part of our review we found that there were weaknesses in the review and authorisation of invoices. **Recommendation** The Partnership should ensure all invoices are subject to rigorous checks and are appropriately authorised prior to submitting for processing by City of Edinburgh Council officers.	**Action owner:** Partnership Director/Treasurer **Due Date:** immediate A new protocol/guidelines have been obtained from City of Edinburgh Council around the declaration of VAT and have been put in place. This processing change is continuing to be embedded across the organisation. Controls on authorisation and review of invoice payments have been updated.	**Action complete** No issues were identified with respect of income and expenditure controls during our 2017/18 audit testing.

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
6. Longer term financial planning **Rating** **Grade 4**	**Observation** The Partnership develops a budget for one financial year which is aligned to the annual business plan and Regional Transport Strategy. There is a risk that funding is used to support short term need rather than long term strategic priorities**.** **Recommendation** In order to ensure financial sustainability the Partnership should develop medium to long term financial plans on a 3 to 5 year basis. This would assist the Partnership in highlighting risks to its sustainability and ensure funding is allocated in line with the long term strategic aims of the Regional Transport Strategy.	**Action owner:** Partnership Director **Due Date:** 31 December 2017 The removal of capital funding in 2009/10 means there is a difficulty for long-term strategic funding of RTS projects. The Director continues to monitor and advocate for investment by stakeholders in strategic priorities and for the return of long-term significant funding to RTPs through the second National Transport Strategy review process. However, given our main funder Transport Scotland has only been able to issue one year funding settlements in recent years, this has limited our ability to take a long-term budgetary approach to investment.	**Action incomplete** The Partnership continues to set a one year budget and no medium to long term financial plans are in place. **Management comments** The Transport (Scotland) Bill, currently out to consultation, includes a proposal to allow RTPs to carry forward reserves. If approved, this may assist with financial planning over a time period longer than one year. However, as Transport Scotland continues to issue one-year funding settlements, there is limited scope to take a long-term approach to financial planning. Within the scope of funding information available, a plan shall be developed, which will seek to align to the Business Plan and Regional Transport Strategy, **Responsible officer:** Partnership Director/Treasurer **Implementation date:** 31st March 2019

Appendix 2: Respective responsibilities of the Partnership and the Auditor

Responsibility for the preparation of the annual accounts

The Partnership is required to make arrangements for the proper administration of its financial affairs and to secure that one of its officers has the responsibility for the administration of those affairs. The Treasurer has been designated as that officer.

The Treasurer is responsible for the preparation of the annual accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom (the Code).

In preparing the annual accounts, the Treasurer is responsible for:

- selecting suitable accounting policies and applying them consistently;
- making judgements and estimates that are reasonable and prudent;
- complying with legislation; and
- complying with the Code.

The Treasurer is also responsible for:

- keeping proper accounting records which are up to date; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor responsibilities

We audit the annual accounts and give an opinion on whether:

- they give a true and fair view in accordance with applicable law and the 2017/18 Code of the state of the affairs of the body as at 31 March 2018 and of the its income and expenditure for the year then ended;
- they have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code;
- they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014 and the Local Government in Scotland Act 2003;
- the part of the Remuneration Report to be audited has been properly prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014;
- the information given in the Management Commentary is consistent with the financial statements and has been prepared in accordance with statutory guidance issued under the Local Government Scotland Act 2003; and
- the information given in the Annual Governance Statement is consistent with the financial statements and has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016).

We are also required to report, if in our opinion:

- adequate accounting records have not been kept; or
- the financial statements and the part of the Remuneration Report to be audited are not in agreement with accounting records; or
- we have not received all the information and explanations we require for our audit; or
- there has been a failure to achieve a prescribed financial objective.

Wider scope of audit

The special accountabilities that attach to the conduct of public business, and the use of public money, mean that public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance, not only on the financial statements, but providing audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

The Code frames a significant part of our wider scope responsibilities in terms of four audit dimensions: financial sustainability; financial management; governance and transparency; and value for money. The Code recognises that full application of its requirements may be impractical or inappropriate due to the nature or size of the audited body.

We have concluded that the full application is not appropriate due to the size of the organisation. As part of our annual audit we consider and report against:

- appropriateness of the disclosures in the governance statement; and
- financial sustainability of the body and the services that it delivers over the medium to longer term.

Independence

We are required by International Standards on Auditing in the UK (ISAs (UK)) to communicate on a timely basis all facts and matters that may have a bearing on our independence. We can confirm that we have complied with the Ethical Standards. In our professional judgement the audit process has been independent and our objectivity has not been compromised. In particular, there have been no relationships between Scott-Moncrieff, the Partnership Board and its Board members or senior management that may reasonably be thought to bear on our objectivity and independence.

Scott-Moncrieff
business advisers and accountants