

North East of Scotland Transport Partnership

2016/17 Annual Audit Report



 AUDIT SCOTLAND

Prepared for North East Scotland Transport Partnership and the Accounts Commission

18 September 2017

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Key messages

2016/17 annual accounts

- 1 Our audit opinions were all unqualified. These covered the financial statements, management commentary, remuneration report and the annual governance statement.

Financial sustainability

- 2 The partnership incurred a small overspend against budget in respect of 2016/17.
- 3 The 2017/18 budget position was approved in February 2017 on the basis that constituent councils and the Scottish Government have committed to maintain funding levels in line with previous years. This position continues to provide financial stability in the short term.

Governance

- 4 There are satisfactory internal financial controls in place. Wider governance should however be enhanced through the adoption of a local code of corporate governance including plans for an annual review of the partnership's arrangements.

Introduction

1. This report is a summary of our findings arising from the 2016/17 audit of North East of Scotland Transport Partnership (NESTRANS). The report is divided into sections which reflect our public sector audit model.

2. The scope of our audit was set out in our Annual Audit Plan presented to the board in April 2017. In accordance with Audit Scotland's Code of Audit Practice, we explained at that time that the small body clause applies to NESTRANS. The main elements of the 2016/17 audit therefore included:

- assurances to support our opinion on the annual accounts
- consideration of the appropriateness of the disclosures in the governance statement
- a review of financial sustainability.

3. The partnership is responsible for preparing annual accounts that show a true and fair view and for establishing effective arrangements for governance to enable successful delivery of objectives.

4. Our responsibilities as independent auditor are established by the Local Government (Scotland) Act 1973, the [Code of Audit Practice \(2016\)](#), and supplementary guidance, and are guided by the auditing profession's ethical guidance. The Code and supplementary guidance also provides details of management's responsibilities with regard to the accounts.

5. These responsibilities include giving independent opinions on the financial statements, the remuneration report, the management commentary and the annual governance statement.

6. 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. Also, our annual audit report contains an action plan at [Appendix 1](#). It sets out specific recommendations, responsible officers and dates for implementation.

7. Communication in this report of matters arising from the audit of the annual accounts or of risks or of weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

8. As part of the requirement to provide fair and full disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2016/17 audit fee was set out in our Annual Audit Plan and as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.

9. This report is addressed to both NESTRANS and the Accounts Commission and will be published on Audit Scotland's website www.audit-scotland.gov.uk.

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

Part 1

Audit of 2016/17 annual accounts



Main judgement

We provided unqualified audit opinions on the accounts.

Unqualified audit opinions

11. The annual accounts for the year ended 31 March 2017 were approved by the partnership on 18 September 2017. We reported, within our independent auditor's report:

- an unqualified opinion on the financial statements
- unqualified opinions on the remuneration report, management commentary and the annual governance statement.

12. Additionally, we have nothing to report in respect of those matters which we are required by the Accounts Commission to report by exception.

Submission of annual accounts for audit

13. We received the unaudited financial statements on 22 June 2017 in line with our agreed audit timetable.

14. The Treasurer is also the Head of Finance for Aberdeenshire Council and consequently, his team provides finance and accounting support to the partnership.

Risks of material misstatement

15. [Appendix 2](#) provides a description of those assessed risks of material misstatement that were identified during the planning process, how we addressed them and conclusions. Also included within the appendix are wider dimension risks.

Materiality

16. Materiality defines the maximum error that we are prepared to accept and still conclude that our audit objective has been achieved. The assessment of what is material is a matter of professional judgement. It involves considering both the amount and nature of the misstatement.

17. Our initial assessment of materiality for the annual accounts was carried out during the planning phase of the audit and was revised on receipt of the unaudited accounts. Our materiality values are summarised in [Exhibit 2](#). Specifically with regard to the annual accounts, we assess the materiality of uncorrected misstatements, both individually and collectively.

The annual accounts are the principal means of accounting for the stewardship of resources.

Exhibit 2

Materiality values

Materiality level	Amount
Overall materiality - This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It was set at 1% of gross expenditure for the year ended 31 March 2017.	£31k
Performance materiality - This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 70% of overall materiality.	£22k
Reporting threshold - We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 1% of overall materiality.	£1.5k

Evaluation of misstatements

18. In order to comply with International Accounting Standard (IAS) 19: Employee Benefits, a range of adjustments were made to the accounts which are explained in [Exhibit 3](#). The overall impact of the amendments to the accounts was to increase the deficit by £13k from £2k to £15k and to increase net liabilities by £920k from £8k to £928k.

19. There were no unadjusted misstatements which require to be reported.

Significant findings

20. International Standard on Auditing (UK and Ireland) 260 requires us to communicate to you significant findings from the audit. These are summarised in [Exhibit 3](#).

Management commentary, annual governance statement and remuneration report

21. The *Code of Audit Practice 2016* requires bodies to prepare and publish, along with their financial statements, an annual governance statement, management commentary and a remuneration report that are consistent with the disclosures made in the financial statements. From 2016/17, in giving an unqualified audit opinion, we are also confirming that these statements have been prepared in accordance with relevant regulations and/or guidance.

22. During the audit process, additional performance information was added to the management commentary and an action plan was added to the annual governance statement to reflect work to be undertaken as a result of revised guidance contained in the CIPFA/SOLACE 'Delivering Good Governance in Local Government: Framework'.

Exhibit 3

Significant findings from the audit of the financial statements

Issue	Resolution
<p>1. Accounting for Pension Costs in accordance with IAS19 (Employee Benefits)</p> <p>In the past, the partnership accounted for pension contributions to the Local Government Pension Scheme as if it were a defined contribution scheme. This meant that only the pension contributions paid during the year were reflected in the accounts. Consequently, the liability to pay for future pensions of current staff was not recognised on the balance sheet as required by IAS19. In addition, the comprehensive income and expenditure account (CIES) does not reflect pension expenses on an actuarial basis.</p> <p>Historically, the actuary only identified the assets and liabilities of the smaller admitted bodies in the North East Scotland Pension Fund on an aggregate basis which meant they were part of a pooled valuation. This however changed sometime ago and the actuary routinely provides separate information to each body on request.</p>	<p>Resolution</p> <p>In order to reflect the pension liability on the balance sheet, 2015/16 comparative figures have been restated to include a pension liability and pension reserve of £538k. Due to a change in the discount rate during the year, the pension liability increased to £920k at 31 March 2017. The CIES has also been amended to reflect additional pension costs on an actuarial basis of £13k (2015/16 £19k).</p> <p>In accordance with ISA 620: using the work of an expert, we regard the actuary as an expert we can place reliance on when considering the findings and conclusions from actuarial valuations.</p> <p>We are satisfied with the accounting treatment, amounts reflected in the audited accounts and changes in account policy adopted following the implementation of IAS19 requirements in respect of pension costs and liabilities.</p>
<p>2. Service analysis</p> <p>The CIES in the draft accounts was presented in line with the Service expenditure reporting code of practice as in previous years.</p> <p>With effect from 2016/17, the Code requires bodies to present the service analysis on the basis of the organisational structure under which they operate and report. Bodies are no longer required to follow the service expenditure analysis in the Service expenditure reporting code of practice.</p>	<p>Resolution</p> <p>The revised accounts have been amended to reflect the 2016/17 Code requirements.</p>
<p>3. Going concern</p> <p>Auditors are required to consider an organisation's ability to continue as a going concern when forming an opinion on the financial statements. One of the indicators that may give rise to going concern considerations is an excess of liabilities over assets.</p> <p>The partnership is an admitted body of North East Scotland Pension Fund. As explained at item one in this Exhibit, following the implementation of IAS 19, the partnership has recognised net pension liabilities of £920k in the balance sheet resulting in a net liabilities position of £928k at 31 March 2017. This accounting requirement has no impact on the underlying basis for meeting current and on-going pension liabilities which will be met, as they fall due, by contributions from the constituent authorities.</p>	<p>Resolution</p> <p>We agree with management's view that it is appropriate to prepare the 2016/17 annual accounts on a going concern basis.</p>

Objections

23. The Local Authority Accounts (Scotland) Regulations 2014 (2014 Regulations) require a local authority body to publish a public notice on its website that includes details of the period the unaudited accounts are available for public inspection and the process for making an objection to the accounts. The notice must remain on the website throughout the statutory 3 week inspection period.

24. NESTRAN's accounts were not made available for inspection online as required. Following audit notification, this was rectified during the inspection period and the period of inspection was extended to ensure the unaudited accounts were publicly available for a 3 week period.

Part 2

Financial sustainability



Main judgement

With funding levels maintained, there is financial stability in the short term.

Financial planning

25. The partnership achieved a small overspend against budget in 2016/17 which was broadly consistent with the original budget. The partnership set its 2016/17 budget in February 2016 with planned funding from constituent councils and the Scottish Government being maintained at the same level as the previous year.

26. Similar to 2016/17, the agreed budget for 2017/18 has been set assuming that funding will continue to be held at the level of previous years. This continues to provide a degree of financial stability in the short term.

27. The partnership has an important role to play in the development of the £250m agreed with the UK and Scottish Governments for a City Region Deal. As detailed plans become clear on the specific projects to be funded through the City Region Deal, the partnership board has been advised that existing NESTRANS projects and budget plans may need to be reviewed and updated in consultation with partners.

Reserves strategy

28. The partnership is required to achieve a break-even position year on year in accordance with the requirements of the Transport (Scotland) Act 2005 for Regional Transport Partnerships. The Act requires that the net expenses of a Transport Partnership for each year are paid by its constituent councils. This means that any surplus be returned to the constituent councils through a reduction in requisitions, and any deficit is funded by increased contributions from constituent authorities.

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

Part 3

Governance



Main judgement

While there are satisfactory internal financial controls in place, governance should be enhanced through the adoption of a local code of corporate governance including plans for an annual review of the partnership's arrangements.

Governance arrangements

29. The NESTRANS partnership is constituted under the Transport (Scotland) Act 2005 as one of seven transport partnerships set up to provide a co-ordinated approach to transport planning and delivery between different local authority areas. NESTRANS area covers Aberdeen City Council and Aberdeenshire Council.

30. The board has 12 members, four each from Aberdeenshire and Aberdeen City Councils and the final four are non-council appointments made by the Minister for Transport.

31. The board met on six occasions during 2016/17, roughly every two months. We review minutes of board meetings to assess their effectiveness and periodically observe meetings for a greater insight into proceedings.

Financial regulations

32. In line with good practice, Financial Regulations are regularly updated, most recently in February 2015. We note however that they should be updated to reflect the requirements of the 2014 Regulations in respect of published accounts and review of internal control.

33. The existing Financial Regulations require the audited accounts to be submitted to the board within two months of being certified. This practice was replaced in the 2014 Regulations by the requirement for the board to consider the audited accounts and to approve them for signature prior to 30 September each year. Thereafter, audited accounts and the auditor's annual report require to be published on the partnership's website.

34. The 2014 Regulations also require the partnership to review its system of internal control on an annual basis prior to its approval of the annual governance statement. The Financial Regulations require the partnership to have an effective system of internal control in place and they also provide for 'periodic' reviews by internal audit. There is scope for the financial regulations to be reviewed to ensure the requirements of the 2014 Regulations have been addressed.

Governance is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information.

Local Code of corporate governance

35. Through a service level agreement the partnership uses the financial systems of Aberdeenshire Council to process its transactions. These systems are subject to a continuous internal audit by the council's chief internal auditor. In our Annual Audit Plan, we acknowledged that the partnership is a small body and as such it is appropriate that it uses and takes assurance from council systems. Through the audit process, revised wording was agreed with the Treasurer for inclusion in the annual governance statement to confirm the partnership's reliance on council systems and to clarify the level of assurance provided by the council's chief internal auditor in respect of those systems.

36. With effect from 2016/17, the CIPFA/SOLACE 'Delivering Good Governance: Framework (2016)' applies to all local government bodies. It has been acknowledged that an annual review against the framework will meet the requirements of an effectiveness review under the 2014 Regulations.

37. The framework sets out a range of core and sub principles for good governance including behaviour, openness and transparency, leadership capacity, decision making and risk and internal control. While the partnership should continue to take assurance from the council in respect of financial systems and internal controls, the framework is wider and extends to the vision, leadership and operation of the partnership board. It is therefore appropriate that the partnership adopts a local code of corporate governance in response to the framework and puts plans in place to conduct an annual review.

Recommendation 2

Internal audit

38. The partnership's internal auditor is Aberdeenshire Council's Chief Internal Auditor. In respect of 2016/17, he concluded that reasonable assurance could be taken from the financial controls the partnership has in place based on his programme of work on council systems.

39. As external auditors for the council, we concluded that internal audit operated in accordance with Public Sector Internal Audit Standards (PSIAS) and has sound documentation, standards and reporting procedures in place.

Financial management

40. Financial management is about financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. It is the partnership's responsibility to ensure that its financial affairs are conducted in a proper manner.

41. As auditors, we need to consider whether audited bodies have established adequate financial management arrangements. We do this by considering a number of factors, including whether:

- the Treasurer has sufficient status to be able to deliver good financial management
- financial regulations and standing orders are comprehensive, current and promoted within the partnership
- reports monitoring performance against budgets are accurate and provided regularly to budget holders.

42. Overall financial management within the partnership is considered to be satisfactory, with appropriate monitoring reports being regularly submitted to the board for scrutiny.

Prevention and detection of fraud and irregularity

43. Through its Financial Regulations, the partnership had adopted the fraud and whistleblowing policies of Aberdeenshire Council. While this is an appropriate arrangement, as the council's external auditors, we recommended that the fraud strategy which currently dates from 2012 be refreshed to reflect current good practice and once updated, it should be re-issue and widely promoted.

Appendix 1

Action plan 2016/17



Page/
para
no.

Issue/risk

Recommendation

Agreed management
action/timing

11/34	<p>The Financial Regulations have not been updated to reflect the requirements of the 2014 Regulations e.g. consideration and approval of audited accounts, responsibility for annual review of internal controls</p> <p>Risk: the partnership does not comply with statutory requirements.</p>	<p>Review and update the Financial Regulations to reflect the requirements of the 2014 Regulations.</p>	<p>Financial Regulations will be reviewed and revised during 2017/18.</p>
12/37	<p>Assurances on the effectiveness of partnership's governance arrangements focus on the council's financial systems and internal controls. Wider governance arrangements around the operation of the partnership board have not been reviewed.</p> <p>Risk: the partnership does not meet the expectations of the Delivering Good Governance Framework.</p>	<p>The partnership should adopt a local code of corporate governance including plans for annual review.</p>	<p>A review of working arrangements will be carried out in early 2018 to take into account the CIPFA "Delivering Good Governance in Local Government: Framework (2016) and a local code adopted thereafter.</p>

Appendix 2

Significant audit risks identified during planning

The table below sets out the audit risks we identified during our planning of the audit and how we addressed each risk in arriving at our conclusion. The risks are categorised between those where there is a risk of material misstatement in the annual accounts and those relating to our wider responsibility under the [Code of Audit Practice 2016](#).

Audit risk	Assurance procedure	Results and conclusions
Risks of material misstatement in the financial statements		
<p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<ul style="list-style-type: none"> Samples of journals and accruals/prepayments were reviewed and accounting estimates were considered. No issues were identified.
<p>2 Changes in accounting requirements</p> <p>The 2016/17 Code of Practice on Local Authority Accounting (the Accounting Code) introduced a number of changes in the presentation of the financial statements including a new expenditure and funding analysis and changes in the governance statement. There is a risk the financial statements will not comply with the Code and/or contain a material misstatement.</p>	<ul style="list-style-type: none"> The Finance team are alert to the Accounting Code changes and the impact on the financial statements. 	<ul style="list-style-type: none"> A detailed review of relevant working papers was carried out against the requirements of the Accounting Code. Amendments were made to the annual accounts to meet the requirements of the revised code.
<p>3 New Payroll System</p> <p>Financial services including payroll administration are provided to NESTRANS by Aberdeenshire Council. The council introduced a new payroll system with effect from 1 April 2016. As with many new systems, there were issues during implementation. There is a risk that payroll is not functioning correctly and staff</p>	<ul style="list-style-type: none"> Assurances from Aberdeenshire over services provided Budget monitoring arrangements. 	<ul style="list-style-type: none"> Assurances drawn from internal and external audit activity in Aberdeenshire Council. Sample checks of partnership employees' pay were satisfactory.

Audit risk	Assurance procedure	Results and conclusions
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costs are misstated.

Risks identified from the auditor's wider responsibility under the Code of Audit Practice

<p>4 Financial management</p> <p>NESTRANS approve an annual budget but have an indication of likely funding proposals for future years. With public sector financial pressures, and a number of projects which are longer than one year in duration, there is a risk that short term planning would not be sufficiently alert to funding shortfalls</p>	<ul style="list-style-type: none"> • The board has adopted the development of a 5 year funding plan • Projects are regularly matched with funding • Mechanisms are in place to give an indication of future years' funding • Good partnership working between NESTRANS, partner councils, community planning partnerships and the City Region Deal joint committee. 	<ul style="list-style-type: none"> • Commentary in our Annual Audit Report.
<p>5 Risk management</p> <p>While the 2015/16 governance statement reported ongoing progress in respect of risk management, the risk register is out of date and we understand that it has not been considered by the board since 2008. Risk management is part of all decision making activities and along with internal controls, is central to good governance arrangements. In the absence of an effective risk management process, there is a risk that the board has not considered its appetite for risk and may not be fully aware of all relevant factors and the impact of failure when making decisions.</p>	<ul style="list-style-type: none"> • Review undertaken to support annual governance statement • Internal audit's annual report • Alert to risk factors when developing the budget. 	<ul style="list-style-type: none"> • An action to review and update the risk register has been highlighted within the annual governance statement.

Aberdeenshire North East of Scotland Transport Partnership

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