



**South East of
Scotland Transport
Partnership
(SEStran)
Annual Audit Plan
2014/15**

Prepared for South East of Scotland Transport Partnership

February 2015



Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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Summary

Introduction

1. Our audit is focused on the identification and assessment of the risks of material misstatement in the South East of Scotland Transport Partnership's financial statements.
2. This report summarises the key challenges and risks facing South East of Scotland Transport Partnership (SEStran) and sets out the audit work that we propose to undertake in 2014/15. Our plan reflects:
 - the risks and priorities facing SEStran
 - current national risks that are relevant to local circumstances
 - the impact of changing international auditing and accounting standards
 - our responsibilities under the Code of Audit Practice as approved by the Auditor General for Scotland
 - issues brought forward from previous audit reports.

Summary of planned audit activity

3. Our planned work in 2014/15 includes:
 - an audit of the financial statements and provision of an opinion on whether:
 - they give a true and fair view of the state of affairs of SEStran as at 31 March 2015 and its income and expenditure for the year then ended
 - the accounts have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2014/15 Code of Practice on Local Authority Accounting in the United Kingdom (the Code)
 - a review and assessment of the Partnership's governance and performance arrangements in a number of key areas including a review of the adequacy of internal audit and the governance statement.

Responsibilities

4. The audit of the financial statements does not relieve management, or the Partnership as the body charged with governance, of their responsibilities.

Responsibility of the appointed auditor

5. Our responsibilities, as independent auditor, are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.
6. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements set in place by the audited body to ensure the proper conduct of its financial affairs and to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

Responsibility of the Treasurer

7. It is the responsibility of the Treasurer, as the appointed "proper officer", to prepare the financial statements in accordance with relevant legislation and the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). This means:

- maintaining proper accounting records
- preparing financial statements which give a true and fair view of the state of affairs of SEStran as at 31 March 2015 and its expenditure and income for the year then ended.

Format of the accounts

8. The financial statements should be prepared in accordance with the Code which constitutes proper accounting practice.

Audit Approach

Our approach

9. Our audit approach is based on an understanding of the characteristics, responsibilities, principal activities, risks and governance arrangements of SEStran. We also consider the key audit risks and challenges in the local government sector generally. This approach includes:
- understanding the business of SEStran and the risk exposure which could impact on the financial statements
 - assessing the key systems of internal control, and considering how risks in these systems could impact on the financial statements
 - identifying major transaction streams, balances and areas of estimation and understanding how SEStran will include these in the financial statements
 - assessing and addressing the risk of material misstatement in the financial statements
 - determining the nature, timing and extent of the audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements give a true and fair view.
10. We have also considered and documented the sources of assurance which will make best use of our resources and allow us to focus audit testing on higher risk areas during the audit of the financial statements. The main areas of assurance for the audit come from planned management action and reliance on systems of internal control. Management action being relied on for 2014/15 includes:
- Comprehensive closedown procedures for the financial statements accompanied by a timetable issued to all relevant staff (SEStran utilises the financial systems of the City of Edinburgh Council and follows the closedown procedures and timetables of the council)
 - clear responsibilities for preparation of financial statements and the provision of supporting working papers
 - delivery of unaudited financial statements to agreed timescales with a comprehensive working papers package
 - completion of the internal audit programme for 2014/15.
11. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carry out an early assessment of the internal audit function. Internal audit is provided by the internal audit section within the City of Edinburgh Council. Overall, we concluded that the internal audit service operates in accordance with Public

Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place.

12. We plan to place formal reliance on aspects of the work of internal audit in the following areas, to support our audit opinion on the financial statements:
- City of Edinburgh Council systems operated on behalf of the Partnership, specifically accounts payable
 - audit work carried out in support of the Annual Governance Statement for inclusion with the financial statements.

Materiality

13. International Standard on Auditing 320 provides guidance on the concept of materiality. We consider materiality and its relationship to audit risk when planning the nature, timing and extent of our audit and conducting our audit procedures. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
14. Based on our knowledge and understanding of SEStran we have set our planning materiality at 1% of gross expenditure. For 2014/15 planning materiality is £14,000.
15. We set a lower level, known as performance materiality, when defining our audit procedures. This level depends on

professional judgement and is informed by a number of factors including:

- extent of estimation and judgement within the financial statements
 - nature and extent of prior year misstatements
 - extent of audit testing coverage.
16. For 2014/15 performance materiality has been set at £10,000. We will report, to those charged with governance, all misstatements greater than £1,000.
17. In addition, an inaccuracy which would not normally be regarded as material in terms of monetary value may be important for other reasons (for example the failure to achieve a statutory requirement, or an item contrary to law). In the event of such an item arising, its materiality has to be viewed in a narrower context; such matters would normally fall to be covered in an explanatory paragraph in the independent auditor's report.

Reporting arrangements

18. The Local Authority Accounts (Scotland) Regulations 2014 require that the unaudited annual accounts are submitted to the appointed external auditor no later than 30 June each year. The Partnership Board (or a committee whose remit includes audit or governance) is required to consider the unaudited annual accounts at a meeting by 31 August.

19. The Partnership must publish the unaudited accounts on their website and give public notice of the inspection period.
20. The 2014 regulations require the Partnership Board (or a committee whose remit includes audit or governance) to meet by 30 September to consider whether to approve the audited annual accounts for signature. Immediately after approval, the annual accounts require to be signed and dated by specified members and officers and then provided to the auditor. The Controller of Audit requires audit completion and issue of an independent auditor's report (opinion) by 30 September each year.
21. The Partnership is required to publish on its website its signed audited annual accounts, and the audit certificate, by 31 October. The annual audit report is required to be published on the website by 31 December.

An agreed timetable is included at Exhibit 1 below which takes account of submission requirements and planned Audit Committee dates:

Exhibit 1: Financial statements audit timetable

Key stage	Date
Planned Board approval of unaudited financial statements	19 June 2015
Submission of unaudited financial statements with working papers package	30 June 2015
Progress meetings with lead officers on emerging issues	As required during audit
Latest date for final clearance meeting with Treasurer	28 August 2015
Agreement of unsigned financial statements for Performance and Audit Committee agenda, and issue of combined ISA 260 report to those charged with governance and Annual Audit Report.	4 September 2015
Performance & Audit Committee date	11 September 2015
Independent auditors report signed	By 30 September 2015

22. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to Partnership Director to confirm factual accuracy. Responses to draft reports are expected within three weeks of submission. A copy of all final agreed reports will be sent to the Partnership Director, the Treasurer, internal audit and Audit Scotland's Performance Audit and Best Value Group.
23. We will provide an independent auditor's report to SEStran and the Accounts Commission that the audit of the financial statements has been completed in accordance with applicable statutory requirements. As part of streamlining our audit approach, the Annual Audit Report will be combined with the ISA 260 report.
24. All annual audit reports produced are published on Audit Scotland's website: (www.audit-scotland.gov.uk).
25. Planned outputs for 2014/15 are summarised at Appendix I.

Quality control

26. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice issued by Audit Scotland and approved by the Accounts Commission. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews and has been subject to a programme of external reviews by the Institute of Chartered Accountants of Scotland (ICAS).

27. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We do, however, welcome feedback at any time and this may be directed to the engagement lead, Stephen O'Hagan.

Independence and objectivity

28. Auditors appointed by the Accounts Commission must comply with the Code of Audit Practice. When auditing the financial statements, auditors must also comply with professional standards issued by the Auditing Practices Board (APB) and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. The arrangements are overseen by the Assistant

Auditor General, who serves as Audit Scotland's Ethics Partner.

29. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of the Partnership.

Audit issues and risks

Audit issues and risks

30. Based on our discussions with staff, attendance at committee meetings and a review of supporting information, we have identified the following main financial statements risk areas for your organisation.
31. **Income:** Auditing standards (ISA 240 *The auditor's responsibility to consider fraud in an audit of financial statements*) requires auditors to presume a risk of fraud where income streams are significant. The Partnership receives a significant amount of funding from the Scottish Government, however £200,000 is received from its constituent councils, and other sources, including the European Union. The complexity of income means there is an inherent risk that income could be materially misstated. However, this is the nature of SEStran's daily operations and therefore our audit procedures are already tailored to address this risk.
32. **Management override of controls:** ISA 240 states that audit procedures should be responsive to risks related to management override of controls. We will design and perform audit procedures to address these risks within the Partnership.
33. **Receipt of European Funding:** The financial statements of the Partnership include a number of debtor balances relating to grant funding for specific projects. In 2013/14 the Partnership was notified that common management costs associated with one project, managed by another partner, had increased, and this would reduce the grant settlement due. The Partnership has a number of European grant claims in the process of being settled and 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.
34. **Depreciation Policy:** With the exception of RTPPI, all of SEStran's assets are now fully depreciated in accordance with existing policies on depreciation and useful asset lives. However these assets continue to be in operational use. There is a risk that assumptions in the existing depreciation policy do not reflect the actual lifespans over which the benefits of the asset are realised.
35. **Accommodation:** SEStran shared its accommodation with SESplan until December 2014 when SESplan moved out. SESplan has paid its share of the remaining rent, however going forward, SEStran will need to meet the full rental costs from within its existing budget, unless alternative tenants are found. This presents an increased financial pressure on operating costs of the Partnership. We will consider the impact

of this alongside other financial pressures when reviewing the budget setting process for 2015/16.

Summary assurance plan

36. Within these identified risk areas there is a range of more specific risks and these are summarised at Appendix II. In most cases, actions to manage these risks are either planned or already underway within the organisation. Details of the sources of assurance that we have received for each of these risks and any audit work we plan to undertake are also set out in Appendix II. In the period prior to the submission of the unaudited financial statements, we will liaise with senior officers on any new or emerging issues.

Fees and resources

Audit fee

37. Over the past four years, Audit Scotland has reduced audit fees by 23.5% in real terms, exceeding our 20% target. Due to further refinement of our audit approach we have been able to restrict the increase in audit fees for 2014/15 to 1% which, in real terms, represents a 0.6% reduction at 2014 price levels.
38. In determining the audit fee we have taken account of the risk exposure of SEStran, the management assurances in place, and the level of reliance we plan to take from the work of internal audit. We have assumed receipt of a complete set of unaudited financial statements and comprehensive working papers package by 30 June 2015.
39. The agreed audit fee for the 2014/15 audit of SEStran is £9,535. Our fee covers:
- the costs of planning, delivering and reporting the annual audit including auditor's attendance at committees
 - your organisation's allocation of the cost of national performance audits and statutory reports by the Accounts Commission
 - a contribution towards functions that support the local audit process (e.g. technical support and coordination of

the National Fraud Initiative), support costs and auditors' travel and subsistence expenses.

- 40. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Audit team

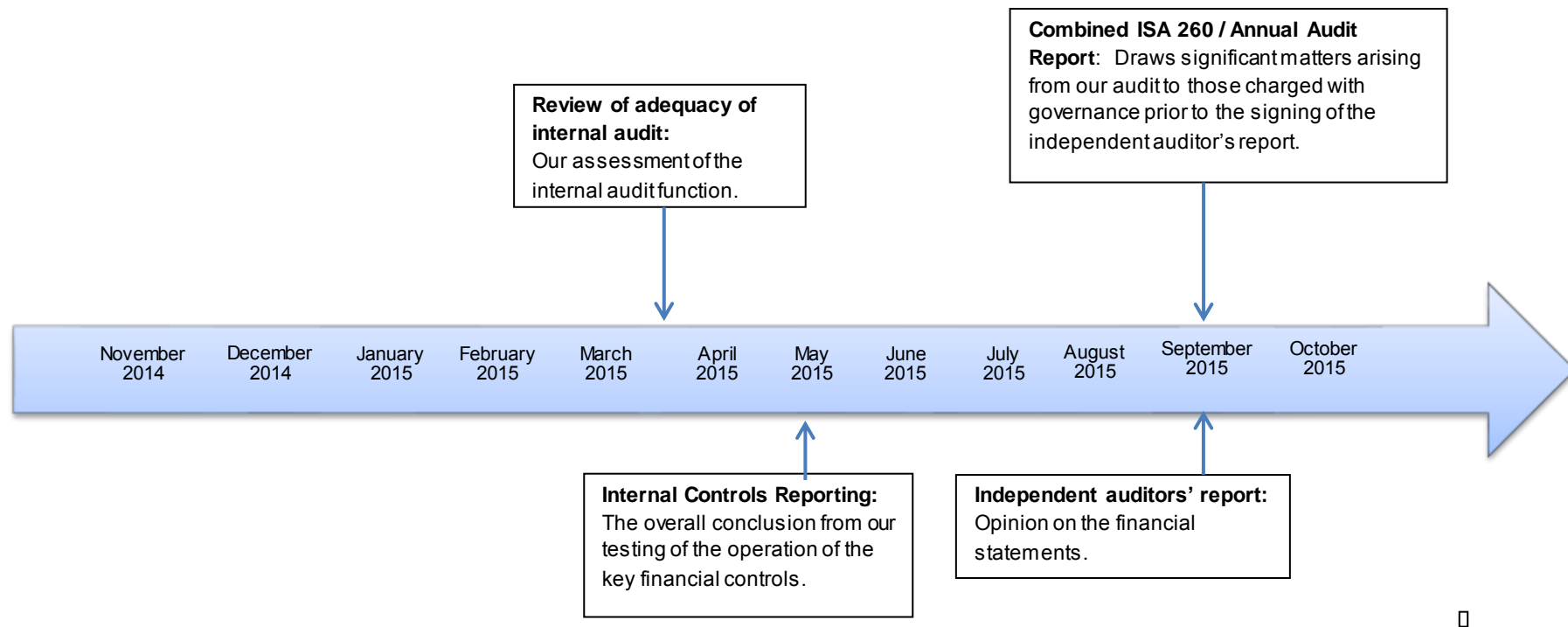
- 41. Stephen O'Hagan, Senior Audit Manager, Audit Services is your appointed auditor. The local audit team will be led by Carol Foster, who will be responsible for day to day management of the audit and who will be your primary contact. Details of the experience and skills of our team are provided in Exhibit 2. The core team will call on other specialist and support staff as necessary.

Exhibit 2: Audit team

Name	Experience
Stephen O'Hagan, CPFA Senior Audit Manager	Stephen has over 18 years experience of public sector audit with Audit Scotland, covering local government, central government, health and the education sector. Prior to joining Audit Scotland, Stephen worked in local government finance for 5 years.
Carol Foster, ACA Senior Auditor	Carol has over 9 years experience of public sector audit with Audit Scotland, covering local and central government. Previously Carol has worked in internal audit in a Scottish local authority and the private sector on a range of public and private sector audits.
Joan Dalglish Auditor	Joan has over 12 years experience of public sector audit with Audit Scotland, covering local government, central government and health.

Appendix I: Planned audit outputs

The diagram below shows the key outputs planned for SEStran in 2014/15.



Appendix II: Significant audit risks

We undertake a risk-based audit whereby we focus on those areas where we have identified a risk of material misstatement in the accounts. This section shows how our audit approach focuses on the risks we have identified through our planning procedures. ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment* defines a significant risk as “an identified and assessed risk of material misstatement that, in the auditor’s judgement, requires special audit consideration.”

In this section we identify a range of risks facing SEStran, the related source of assurance received and the audit work we propose to undertake to secure additional assurance. The management of risk is the responsibility of SEStran and its officers, with the auditor’s role being to review the arrangements put in place by management. Planned audit work, therefore, will not necessarily address all residual risks.

Audit Risk	Source of assurance	Assurance procedure
<i>Audit risk of material misstatement in financial statements</i>		
<p>Income</p> <p>SEStran receives a significant amount of income in addition to SG funding.</p> <p>The complexity of income means there is an inherent risk of fraud in accordance with ISA240.</p>	<ul style="list-style-type: none"> Existing control arrangements, internal audit review. 	<ul style="list-style-type: none"> Detailed substantive testing of revenue transactions focusing on the areas we consider to be of greatest risk.

Audit Risk	Source of assurance	Assurance procedure
<p>Management override of controls</p> <p>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.</p>	<ul style="list-style-type: none"> N/A 	<ul style="list-style-type: none"> Detailed testing of journal entries Review of accounting estimates for bias Evaluating significant transactions that are outside the normal course of business.
<p>Receipt of European funding</p> <p>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.</p>	<ul style="list-style-type: none"> Review of central management costs will be undertaken prior to finalisation of projects. 	<ul style="list-style-type: none"> Substantive testing of grant funding debtors as part of financial statement programme.
<p>Depreciation Policy</p> <p>With the exception of the RTP1 assets, all of SEStran 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.</p>	<ul style="list-style-type: none"> Review of existing assets, and consideration of current depreciation policy. 	<ul style="list-style-type: none"> Consideration of appropriateness of revised asset lives. Detailed testing of fixed assets.