

Highlands and Islands Transport Partnership

Report to Members and the Controller of Audit on the 2009/10 audit

September 2010

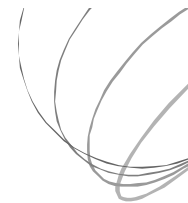


 AUDIT SCOTLAND



Contents

Key Messages	1	Future outlook - Finance	5
Introduction	2	Corporate governance	7
Financial statements	3	Overview	7
Auditor's report	3	Systems of internal control	7
Financial position	4	Performance management	8
Issues arising	4	Regional Transport Strategy (RTS)	8
Legality	4	Appendix A: Action Plan	10
Statement on the system of internal financial control (SSIFC)	5		



Key Messages

In 2009/10 we have audited the financial statements and looked at aspects of governance and performance within Highlands and Islands Transport Partnership. This report sets out our main findings.

Overall, we found the financial stewardship of Highlands and Islands Transport Partnership (the Partnership) during the year to be satisfactory. The main conclusions and outcomes from the audit are highlighted below:

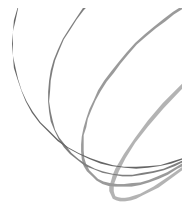
- An unqualified opinion has been issued on the financial statements for 2009/10
- The Statement on the System of Internal Financial Control included in the accounts complies with accounting requirements and is not inconsistent with audit findings.
- Final accounts preparation procedures and working papers were good and this enabled the audit to progress smoothly.
- Many aspects of a sound corporate governance framework have been adopted.

The Partnership operates the corporate financial systems of The Highland Council. As external auditor of the council, we have also been able to take assurance from our work on these systems.

The Highlands and Islands Regional Transport Strategy spans a period of 15 years (to 2022), however, the performance measures identified in support of the strategy do not cover short, medium and longer timescales. It is, therefore, difficult for the Partnership to demonstrate the effectiveness of the work it carries out and to ensure it is on track to meet the 2022 delivery date.

The UK economy is in its longest recession on record and the public sector is now facing deep and prolonged cuts in funding. It will be very challenging to maintain current levels of public services and meet new demands when resources are tight. This is further compounded by the on-going issue of funding pension liabilities. The Partnership will not be immune to these financial pressures and will need to identify ways of delivering services in light of future funding constraints.

**Audit Scotland
September 2010**



Introduction

1. The members and officers of the Partnership are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
 - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed;
 - the Partnership's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests;
 - the Partnership has adequate corporate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability; and
 - the systems of internal control provide an appropriate means of preventing or detecting material mis-statement, error, fraud or corruption.

2. This report summarises the most significant issues arising from our work during 2009/10.



Financial statements

3. The financial statements of the Partnership are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of these resources. It is the responsibility of the Partnership to prepare financial statements that provide a true and fair view of its financial position and the income and expenditure for the year.
4. In this section we summarise key outcomes from our audit of the Partnership's financial statements for 2009/10, aspects of the Partnership's reported financial position and performance to 31 March 2010, and provide an outlook on future financial reporting issues.

Auditor's report

5. We have given an unqualified opinion on the financial statements of Highlands and Islands Transport Partnership for 2009/10, concluding that the financial statements:
 - show a true and fair view, in accordance with relevant legal and regulatory requirements and the 2009 SORP, the financial position of the Partnership as at 31 March 2010 and its income and expenditure for the year then ended; and
 - have been properly prepared in accordance with the Local Government (Scotland) Act 1973.
6. The Partnership's balance sheet at 31 March 2010 shows net liabilities of £338,000. Auditing standards require auditors 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.
7. The net liability position is due to the requirements of Financial Reporting Standard 17 (retirement benefits) where there is an obligation to recognise the Partnership's full pension obligations in the year they are earned. This technical accounting requirement has had no impact on the underlying basis for meeting current and ongoing pension liabilities which will be met, as they fall due, by contributions from constituent authorities in the normal way. In common with similar authorities, the Partnership has considered it appropriate to adopt a going concern basis for the preparation of the financial statements as future actuarial valuations of the pension fund will consider the appropriate employer's contribution rate to meet the fund's commitments. The constituent authorities of the Partnership are also liable to fund the Partnership's liabilities as they fall due. We are satisfied that the process the Partnership has undertaken to consider going concern is reasonable.



Financial position

8. The Partnership's net operating expenditure for 2009/10 amounted to £218,000 (after elimination of FRS 17 pension adjustments) and was met by constituent authorities' contributions of £218,000. The Treasurer's Report to the Board contained within the financial statements summarises performance against budget.

Issues arising

9. The Partnership's financial statements were submitted to the Controller of Audit by the deadline of 30 June. Final accounts preparation procedures and working papers were good and this enabled the audit to progress smoothly.
10. Local authorities in Scotland are required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). No major changes were introduced by the 2009 SORP that affected the Partnership accounts. Overall, we were satisfied that the Partnership had prepared the accounts in accordance with the revised SORP.
11. Audited accounts were finalised prior to the target date of 30 September 2010 and are now available for presentation to the Partnership and for publication. The financial statements are an essential means by which the Partnership accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.

Legality

12. Each year we request written confirmation from the Treasurer that the Partnership's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of members and officials of Highlands and Islands Transport Partnership, the financial transactions of the Partnership were in accordance with the relevant legislation and regulations governing its activities.
13. There are no additional legality issues arising from our audit which require to be brought to members' attention.



Statement on the system of internal financial control (SSIFC)

14. Scottish authorities are required by the local authority SORP to include a statement on the system of internal financial control with their statement of accounts. The 2009/10 financial statements include a Statement on the System of Internal Financial Control which highlights the Treasurer's view that the Partnership can place reliance upon the effectiveness of the Partnership's financial systems.
15. The SSIFC included in the accounts highlighted the role of The Highland Council's Internal Audit and Risk Management department for reporting on management and performance issues. During 2009/10, the internal audit department carried out work on the council's financial systems which are used by the Partnership but no specific work was done on financial controls operated by the Partnership. The SSIFC therefore overstated the level of assurance available to the Treasurer. This was amended to more accurately reflect the role of internal audit within the Partnership. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.
16. The SORP states that authorities *may choose* to include a wider statement of internal control in place of a statement of internal financial control. The CIPFA framework document *Delivering good governance in local government* recommends that the review of the effectiveness of the system of internal control should be reported in an annual governance statement. LAAP bulletin 71 *The Annual Governance Statement* clarifies that authorities are encouraged (but not required) to include an annual governance statement with their accounts. The Partnership may wish to consider moving to an Annual Governance Statement in future years.

Future outlook - Finance

National economic conditions

17. The UK economy is in its longest recession on record and the public sector is now facing deep and prolonged cuts in funding. At a UK level, real term reductions of 2.3 per cent each year are projected for Departmental Expenditure Limit (DEL) budgets between 2011 and 2014. Current forecasts are that any real term growth in public spending over the next two spending review periods (2011 to 2018) will continue to be constrained and will not return to the levels seen over the last decade.
18. Whilst the Scottish Government has implemented an economic recovery programme to support the economy through this period of decline, demand for public services continues to rise adding to the on-going strain on public sector resources. The Partnership will not be immune to these financial pressures and will need to identify ways of delivering services in light of future funding constraints.



Pension liabilities

19. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. In accounting for pensions, Financial Reporting Standard 17 (Retirement of Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in a very large future liabilities being recognised on the face of annual accounts.
20. The Partnership participates in the Local Government superannuation Scheme (Highland Pension Fund), a defined benefits scheme administered by The Highland Council. Note 6 to the Core Financial Statements highlights that the Partnership's scheme net liabilities at 31 March 2010 are £1,065,000, an increase of £486,000 from the previous year largely as a result of a significantly lower discount rate (based on corporate bond rates) being applied this year.
21. The actuary is required to make a 3-year assessment of the contributions that should be paid by the employing authorities as from April 2009 to maintain the solvency of the fund. The current 3-year assessment set budgeted contributions, expressed as a percentage of employees' contribution rates at 275% for 2009/10 and 290% for the next two years.
22. The actuary makes a number of assumptions in calculating pension costs. However, we are not aware of the Partnership, or the administering authority undertaking any confirmation that the assumptions applied are appropriate to local circumstances. We would highlight that actuarial reports are only advisory and the Partnership should confirm it is satisfied with the assumptions/rates used in these reports.

Key risk area 1

International Financial Reporting Standards Adoption

23. Local government will move from UK Generally Accepted Accounting Principles to International Financial Reporting Standards (IFRS) with effect from 2010/11. A comparative balance sheet as at 1 April 2009 will be required as well as at 31 March 2010 and 2011. We have been advised that work is on-going to restate the required figures for inclusion in the 2010/11 accounts.



Corporate governance

24. In this section we comment on key aspects of the Partnership's governance arrangements during 2009/10.

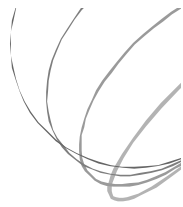
Overview

25. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. The Partnership has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.

26. The Partnership has adopted a number of aspects of a sound corporate governance framework in place within the Highland Council for its own purposes, for example, financial regulations and arrangements for the prevention and detection of fraud and corruption.

Systems of internal control

27. It is the responsibility of the council's management to maintain adequate financial systems and associated internal controls. The Partnership's financial transactions are processed through Highland Council's corporate financial systems, namely: ResourceLink for payroll and the Oracle financial management system for all other income and expenditure. As external auditors of the council we have been able to take assurance from our work on these systems. We also undertook audit testing focussing on the high level controls applied by the Partnership in relation to the financial management system. Overall, there were no material issues of concern in relation to the operation of the main financial systems.



Performance management

28. As part of our planned work this year, we held discussions with Partnership officers about the arrangements put in place to measure the performance of the Partnership against the Regional Transport Strategy for the Highlands and Islands.
29. In this section we comment on the Partnership's approach to performance management

Regional Transport Strategy (RTS)

30. The RTS is part of a number of strategies and plans for improving transport links. These include the National Transport Strategy, National Planning Framework, and national economic and sustainable development strategies. Successful delivery of these transport strategies and plans will require effective partnership working between a wide range of bodies and funders including Scottish Government, local authorities and health boards.
31. The Partnership is striving towards developing a fit for purpose, multi-modal transport system for its area. Its primary objective is "to improve the interconnectivity of the whole region to strategic services and destinations in order to enable the region to compete and support growth" (RTS page 1). This is a complex challenge as the area covered by the RTS for the Highlands & Islands is diverse, ranging from remote rural and island communities to dense urban neighbourhoods.
32. The overall objective is supported by four further objectives designed: to enable people to participate in everyday life; to improve the safety and security of travel; to improve people's health; and to manage impacts on our environmental assets. In addition a package of policies and measures have been developed under a number of horizontal themes which apply across the region.
33. A framework has been set up to monitor the overall success of the Partnership in delivering the RTS. This framework sets out performance indicators against the following five headings which match the strategic objectives outlined in the Strategy:
 - Economy – improve interconnectivity;
 - Accessibility – enable participation in everyday life;
 - Environment – manage the impact on environmental assets;
 - Safety – improve safety and security of travel; and
 - Health – improve people's health



34. The performance indicators have been tiered to measure the high level strategic outcomes which cascade through to intermediate outputs and transport indicators. Significant effort has been made to collect the baseline data for these measures. This is a good starting point for measuring the effectiveness of the work of the Partnership in delivering the Strategy.

35. However, the RTS spans a period of 15 years (to 2022) and the performance measures identified do not cover short, medium and longer timescales. It will, therefore, be difficult for the Partnership to demonstrate the effectiveness of the work it carries out over this timescale and to ensure it is on track to meet the 2022 delivery date.

Action point 2



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Risk Identified	Planned Management Action	Responsible Officer and Target Date
1 Ref para 22	<p>In accounting for pensions, Financial Reporting Standard 17 (Retirement of Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in a very large future liabilities being recognised on the face of annual accounts. An actuarial calculation of the FRS17 impact is provided to the Partnership each year however no review of the assumptions or rates applied by the actuary is carried out to ensure the Partnership is satisfied that these are appropriate to local circumstances.</p> <p>Risk: FRS 17 pension costs, assets and liabilities are based on inaccurate or inappropriate assumptions.</p>	<p>Actuaries request and are provided fund specific information on which to base their FRS 17 estimates.</p> <p>The Pensions team within Highland Council will in future conduct a high level check of the FRS 17 reports for assurance where possible that the reports are broadly consistent with the fund specific data provided.</p> <p>However it will not be possible to conduct a detailed review all of the actuarial assumptions and consequent outcomes.</p>	<p>Finance manager</p> <p>May 2011</p>
2 Ref para 35	<p>The Regional Transport Strategy spans a period of 15 years from inception. Although there are performance measures in place these are not split into short, medium and longer term and therefore the Partnership is unable to measure its effectiveness in delivering on its performance measures on an on-going basis. There is, therefore a risk that the Partnership will not be alerted to problems in meeting the 2022 delivery date.</p> <p>Risk: the Partnership will not be able to deliver the RTS on time.</p>	<p>The Partnership recognizes the challenges in monitoring and evaluating the success of HITRANS and its partners in delivering the RTS within the prescribed timescale, and has established a Framework for this purpose.</p> <p>HITRANS officers and Permanent Advisors will develop interim and final targets for the key Transport Indicators included in the Framework. These will be established with assessment dates of 2013, 2018, and the end of 2022, and presented to the HITRANS Board for their consideration at their Meeting in December 2010.</p> <p>The Board will subsequently, subject to its agreement, be provided with updates on progress towards achieving these targets in the Partnership's Annual Reports, and periodically review the effectiveness of the focus of the Partnership's actions and the RTS in achieving its aims.</p>	<p>Partnership director</p> <p>December 2010</p>