



cutting through complexity

Strathclyde Partnership for Transport and Strathclyde Concessionary Travel Scheme Joint Committee

Audit strategy and interim report

Year ending 31 March 2016

26 February 2016

For Audit and Standards Committee consideration on

18 March 2016

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About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the Code").

This report is for the benefit of Strathclyde Partnership for Transport ("SPT") and Strathclyde Concessionary Travel Scheme Joint Committee ("SCTSJC") is made available to Audit Scotland and the Controller of Audit (together "the Beneficiaries"). This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report. We have prepared this report for the benefit of the Beneficiaries alone. Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scoping and purpose section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.

Complaints

If at any time you would like to discuss with us how our services can be improved or if you have a complaint about them, you are invited to contact Andy Shaw, who is the engagement leader for our services to the Partnership, telephone 0131 527 6673 email: andrew.shaw@kpmg.co.uk who will try to resolve your complaint. If your problem is not resolved, you should contact Alex Sanderson, our Head of Audit in Scotland, either by writing to him at Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2EG or by telephoning 0131 527 6720 or email to alex.sanderson@kpmg.co.uk. We will investigate any complaint promptly and do what we can to resolve the difficulties. After this, if you are still dissatisfied with how your complaint has been handled you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN.

SIGNIFICANT RISKS AND OTHER MATTERS

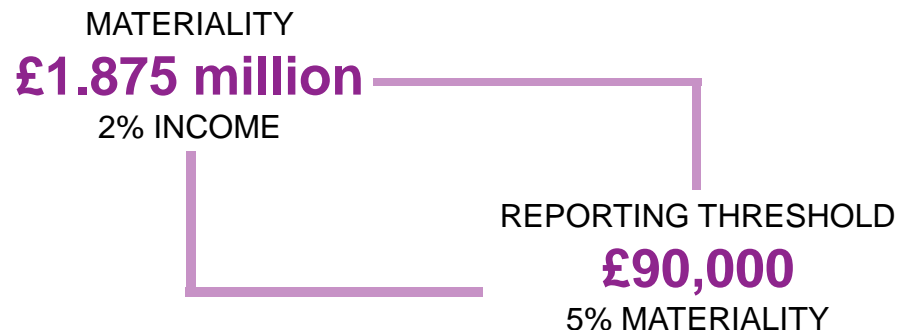


From discussions with management, from our knowledge of the partnership and review of risk registers, we have considered areas of risk and audit focus. We have identified one significant risk as fraud risk from management override of controls.

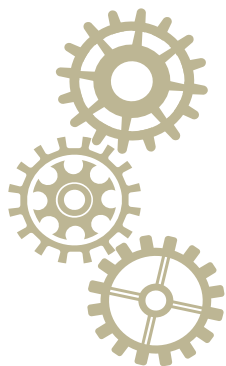
Other focus areas have been identified as:

- recognition of income and expenditure;
- property, plant and equipment;
- retirement benefits; and
- transport infrastructure assets.

MATERIALITY



WIDER SCOPE REQUIREMENTS



The audit will consider other areas:

- Audit Scotland's Code of Audit Practice ("the Code") and the audit dimensions set out in the 2016 code (in consultation)
- National Fraud Initiative
- Code of Practice on Local Authority Accounting in the United Kingdom disclosure
- Targeted follow up

KPMG TEAM



The leadership team benefits from strong continuity at a senior level:

- Andy Shaw – engagement director
- Michael Wilkie – senior manager
- Carol Alderson – engagement manager
- Laura Nelson – audit in-charge

We will harness the expertise of our valuation and pension specialists to support our audit work where necessary.

Scope definition

The Accounts Commission has appointed KPMG LLP as auditor of Strathclyde Partnership for Transport (“SPT”) under the Local Government (Scotland) Act 1973 (“the Act”). The period of appointment is 2011-12 to 2015-16, inclusive. For the 2015-16 audit our appointment includes the audit of the Strathclyde Concessionary Travel Scheme Joint Committee (“STCSJC”).

Purpose

This document summarises our responsibilities as external auditor for the year ending 31 March 2016 and our intended approach to issues impacting The Partnership’s activities in the year.

KPMG’s planned audit work in 2015-16 will include:

- an audit of the financial statements and provision of an opinion on whether the financial statements:
 - give a true and fair view in accordance with applicable law and the 2015-16 Code of the state of the affairs of the body as at 31 March 2016 and of the income and expenditure of the body for the year then ended;
 - have been properly prepared in accordance with IFRS as adopted by the European Union, as interpreted and adapted by the 2015-16 Code, the requirements of the Local Government (Scotland) act 1973, the Local Authority Accounts (Scotland) Regulations 2014 and the Local Government Scotland Act 2003.
- a review and assessment of SPT’s governance arrangements including: a review of the adequacy of internal audit and review of the governance statement;
- a review of National Fraud Initiative arrangements; and
- a review of arrangements for preparing and publishing statutory performance information.

Auditors and audited bodies’ responsibilities are set out in Audit Scotland’s Code of Audit Practice (“the Code”). This Code states the responsibilities in relation to:

- the financial statements;
- corporate governance and systems of internal control;
- prevention and detection of fraud and irregularities;
- standards of conduct and arrangements for the prevention and detection of bribery and corruption;
- arrangements for preparing and publishing statutory performance information;
- financial position; and
- Best Value, uses of resources and performance.

These responsibilities are outlined in appendix four.

Financial position

- Original forecast net revenue expenditure was £38.4 million, with a break-even outturn. Planned requisitions from constituent local authorities were maintained in cash terms at 2011-12 levels (£37.4 million) and contributions from Scottish Government were budgeted at £1 million.
- The period nine revenue monitoring report shows a forecast full year surplus of £2 million. This is primarily due to higher subway income from increased patronage. Higher bus operations income has been received through funding from Glasgow City Council for hospital bus services, however this is offset by additional contract costs. Expenditure is below budget, primarily in staff costs due to vacancies.
- The capital expenditure budget for 2015-16 was initially forecast as £78.4 million. Budget changes made during the period increased the approved budget to £81.2 million. The key change was an additional £2.1 million for subway modernisation.

Key developments

- Prior to 31 March 2016, Buchanan Street and St Enoch station upgrades are anticipated to be completed.
- During 2015-16 the contract for the replacement of the ramps and turnouts was awarded, and work is due to start in Summer 2016. The replacement of the tunnel lining and pumps and sumps has been ongoing during 2015-16.
- Other developments to be considered during the 2015-16 audit and included within our annual audit report include:
 - progress with the Fastlink project;
 - any further transactions as a result of moving to a new head office;
 - Audit Scotland's new best value approach for 2015-16 onwards; and
 - progress against the capital and revenue budgets.

Audit dimensions – as they develop we will consider the wider scope Audit Dimensions as set out in the Code of Audit Practice 2016 (in consultation). The audit dimensions put Best Value at the core.

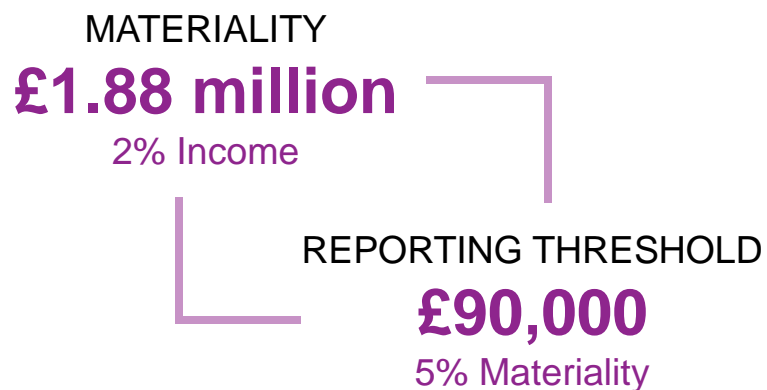
| Financial sustainability | Financial management | Governance and transparency | Value for money |
|--|---|--|---|
| Financial sustainability looks forward to the medium and longer term to consider whether the Partnership is planning effectively to continue to deliver its services or the way in which they should be delivered. | Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. | Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information. | Value for money is concerned with using resources effectively and continually improving services. |

We consider quantitative and qualitative factors in setting materiality and in designing our audit procedures.

Audit differences will be presented to the Audit and Standards Committee if they are material in size or material in nature. For 2015-16 we consider individual or aggregated financial statement errors of over £1.88 million (2014-15: £1.90 million) to be material.

To the extent that we identify misstatements above £90,000 (2014-15: £95,000) we report them to the Audit and Standards Committee and assess whether the misstatement is indicative of a significantly deficient or materially weak control environment.

We recognise that matters can be important because of their nature regardless of their size, for example misstatements to key disclosures such as remuneration and related parties, and we will also report these to Audit and Standards Committee.



DETERMINING MATERIALITY

We consider materiality by reference to SPT's total income, which is forecast to be approximately £94 million in 2015-16.

Audit Scotland guidance typically puts this percentage at not higher than 2% of the chosen gross metric (total Income).

We consider SPT's total income of 2014-15 along with the expectation for 2015-16 and consider the use of a materiality of £1.88 million, representing 2% of 2015-16 forecast income to be appropriate.

We consider quantitative and qualitative factors in setting materiality and in designing our audit procedures.

Audit differences will be presented to the Audit and Standards Committee if they are material in size or material in nature. For 2015-16 we consider individual or aggregated financial statement errors of over £85,000 (2014-15: £85,000) to be material.

To the extent that we identify misstatements above £4,000 (2014-15: £4,000) we report them to the Audit and Standards Committee and assess whether the misstatement is indicative of a significantly deficient or materially weak control environment.

We recognise that matters can be important because of their nature regardless of their size, for example misstatements to key disclosures such as remuneration and related parties, and we will also report these to Audit and Standards Committee.

MATERIALITY

£85,000

2% Income

REPORTING THRESHOLD

£4,000

5% Materiality

DETERMINING MATERIALITY

We consider materiality by reference to SCTSJC's total operating expenditure which was £4.3 million in 2014-15.

Audit Scotland guidance typically puts this percentage at not higher than 2% of the chosen gross metric (total expenditure).

We consider SCTSJC's total expenditure of 2014-15 along with the expectation for 2015-16 and consider the use of a materiality of £85,000, representing 2% of 2014-15 expenditure to be appropriate.

International Standard on Auditing (UK and Ireland) 315: *Identifying and assessing risks of material misstatement through understanding the entity and its environment* requires the auditor to determine whether any of the risks identified as part of risk assessment are significant risks and therefore requiring specific audit consideration.

In determining whether a risk is significant, judgement is applied in respect of whether, for example, the risk is associated with the complexity of transactions, the degree of subjectivity involved in the measurement of financial information, whether the associated transactions are outside the normal course of business or whether there is an associated risk of fraud. We have set out our assessment of significant risks, along with other audit focus areas, in terms of the comprehensive income and expenditure statement and the balance sheet.

| COMPREHENSIVE INCOME AND EXPENDITURE | |
|---|------------------|
| CAPTION | 2014-15 £'000 |
| Gross income | (24,391) |
| Gross expenditure | 85,807 |
| Financing and investment income and expenditure | 665 |
| Taxation and non-specific grant income | (66,138) |
| Other comprehensive income and expenditure | 5,941 |
| Total comprehensive income and expenditure | 1,884 |

Recognition of income and expenditure

Property, plant and equipment

Transport infrastructure assets

Retirement benefits

| BALANCE SHEET | |
|-------------------------------|------------------|
| CAPTION | 2014-15 £'000 |
| Property, plant and equipment | 126,341 |
| Other long term assets | 6,673 |
| Short term debtors | 30,152 |
| Cash and cash equivalents | 46,611 |
| Other current assets | 178 |
| Short term investments | 52,131 |
| Short term creditors | (44,769) |
| Provisions | (741) |
| Long term liabilities | (21,714) |
| Pension asset/ liability | (38,987) |
| Useable reserves | (69,466) |
| Unusable reserves | (86,409) |

Key

Significant audit risk

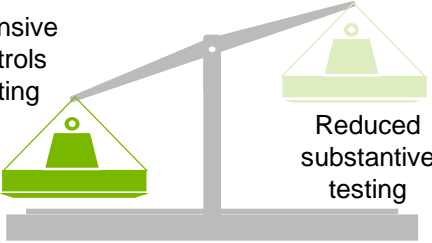
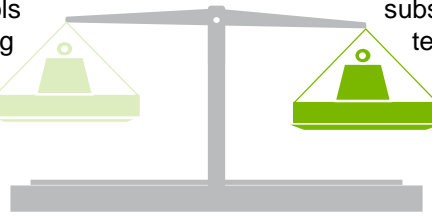
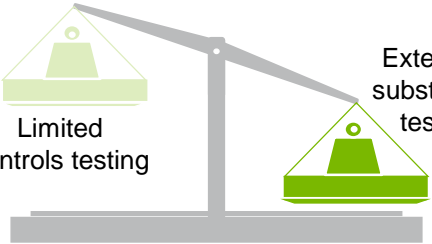
Other focus area

| RISK | WHY | AUDIT APPROACH |
|---|--|---|
| <p>Fraud risk from management override of controls</p> | <p>Professional standards require us to communicate the fraud risk from management override of controls as a significant risk; as management is typically in a unique position to perpetrate fraud because of its 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"> ■ Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to the audit of SPT. ■ Strong oversight of finances by management provides additional review of potential material errors caused by management override of controls. ■ In line with our methodology, we will carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the organisation's normal course of business, or are otherwise unusual. |

| FOCUS AREA | WHY | AUDIT APPROACH |
|---|---|--|
| <p>Recognition of income and expenditure</p> | <p>Professional standards require us to make a rebuttable presumption that the fraud risk from income recognition is a significant risk.</p> <p>The Partnership receives significant income in the form of requisitions from the constituent local authorities, Scottish Government grants and operating income associated with the subway and bus stations. As grants and requisitions are agreed in advance of the year, with adjustments requiring formal approval, we do not regard the risk of fraud from this revenue recognition as significant.</p> <p>Other sources of income are from subway, bus stations and rental income. These revenues are prescribed by specific regulations or are recognised on a cash basis without credit terms (i.e. subway revenue). This minimises the level of judgement required in revenue recognition by management and we do not regard the risk of fraud from this revenue recognition as significant.</p> <p>There is a risk that expenditure is not recognised appropriately, in the correct period, or in line with the Code. This includes expenditure in the following areas:</p> <ul style="list-style-type: none"> ■ third party payments to bus operators; ■ employee costs; and ■ depreciation and impairments. | <ul style="list-style-type: none"> ■ We will review the treatment of significant elements of income. This will include building an expectation of subway income taking into account patronage numbers and fare changes occurring in the year. ■ We will review actual income and expenditure against budgeted amounts and obtain explanations and evidence for significant variances. We will select samples of expenditure and agree to source documentation and obtain explanations for expenditure that has not been recognised in line with the Code. ■ We will agree grant income to supporting documentation including grant offer letters. ■ We will perform year-end testing over bus operator payments by selecting a sample and agreeing to contracts or variations. ■ We will perform testing over controls relating to employee costs and at the year-end build an expectation of employee costs, taking into account employee numbers and any pay rises occurring in the year. We will also use data analytics to identify unusual activity in relation to employee costs. ■ We will develop an expectation of depreciation taking into account additions, disposals and revaluations or impairments in the year. We will also review the accounting entries relating to these impairments and valuations to ensure that they are Code compliant. |

| FOCUS AREA | WHY | AUDIT APPROACH |
|---|---|---|
| <p>Property, plant and equipment</p> | <p>There are a number of capital projects ongoing, the most significant being the subway modernisation programme.</p> <p>There is a delivery risk associated with this project which would inhibit the realisation of the Partnership's strategy. There is also a risk to the financial statements relating to the recognition of expenditure and the valuation of the assets that have been subsequently recognised.</p> | <ul style="list-style-type: none"> ■ We will hold discussions with staff responsible for overseeing the subway modernisation programme and other capital projects and for recording the related accounting entries. ■ We will audit the valuations of completed subway stations, integrating a KPMG valuation specialist to challenge the valuation assumptions. ■ We will review the accounting treatment of the valuations to verify appropriate recognition and disclosure in the financial statements. ■ We will obtain supporting documentation for significant additions and disposals. |
| <p>Transport infrastructure assets</p> | <p>The 2016-17 Code will adopt requirements of the Code on transport infrastructure assets ("the transport code"), which requires measurement of these assets on a depreciated replacement cost basis.</p> <p>This will represent a change in accounting policy from 1 April 2016 and require retrospective restatement. Local authorities are advised to have implemented a robust project plan through 2015-16 to ensure preparedness for the requirements of the 2016-17 Code.</p> | <p>We will consider SPT's plan to meet the requirements of the transport code, including assessing the completeness of information for an opening balance sheet. We will evaluate the extent to which management is prepared for the change in accounting policy.</p> |

| FOCUS AREA | WHY | AUDIT APPROACH |
|-----------------------------------|--|---|
| <p>Retirement benefits</p> | <p>SPT accounts for its participation in the Local Government Pension Scheme in accordance with IAS 19 Retirement benefits, using a valuation report prepared by actuarial consultants.</p> <p>SPT's actuaries use membership data and a number of assumptions in their calculations based on market conditions at the year end, including a discount rate to derive the anticipated future liabilities back to the year end date and assumptions on future salary increases.</p> <p>IAS 19 requires the discount rate to be set by reference to yields on high quality (i.e. AA) corporate bonds of equivalent term to the liabilities. The calculation of the pension liability is inherently judgemental.</p> | <p>Our audit approach to IAS19 includes:</p> <ul style="list-style-type: none"> ■ review by KPMG specialists of the financial assumptions underlying actuarial calculations and comparison to our central benchmarks; ■ testing of scheme assets and rolled-forward liabilities; ■ testing of the level of contributions used by the actuary to those actually paid during the year; ■ testing of membership data used by the actuary to data from SPT; and ■ agreeing actuarial reports to financial statement disclosures. |

| What we do | Accounts/transactions suited to this testing | KPMG's approach to: |
|---|---|---|
|  <p>Extensive controls testing</p> <p>Reduced substantive testing</p> | <ul style="list-style-type: none"> ■ Low value transactions ■ High volume ■ Homogenous transactions ■ Little judgement | <ul style="list-style-type: none"> ■ Payroll expenditure ■ Net expenditure of continuing operations ■ Bus operator payments |
|  <p>Moderate controls testing</p> <p>Moderate substantive testing</p> | <ul style="list-style-type: none"> ■ Low/medium value ■ High/medium volume ■ Some areas requiring judgement | <ul style="list-style-type: none"> ■ Subway income ■ Debtors, creditors and accruals ■ Cash |
|  <p>Limited controls testing</p> <p>Extensive substantive testing</p> | <ul style="list-style-type: none"> ■ High value ■ Low volume <p>or</p> <ul style="list-style-type: none"> ■ Unusual non-recurring ■ Accounting estimates ■ Significant judgments | <ul style="list-style-type: none"> ■ Property, plant and equipment ■ Pension scheme liability ■ Journals ■ Taxation and non-specific grant income ■ Borrowings |

Financial position

In February 2015 the committee approved a revenue budget of £4.48 million for 2015-16, funded by £4.26 million of local authority requisitions and £0.22 million draw on reserves. As at 10 October 2015 projected outturn expenditure is expected to be £393,000 under budget.

Significant risks and audit focus areas

International Standard on Auditing (UK and Ireland) 315: *Identifying and assessing risks of material misstatement through understanding the entity and its environment* requires the auditor to determine whether any of the risks identified as part of risk assessment are significant risks and therefore requiring specific audit consideration. We have set out our assessment of significant risks, along with other audit focus areas, below.

| RISK | WHY | AUDIT APPROACH |
|--|--|--|
| Fraud risk from management override of controls | Professional standards require us to communicate the fraud risk from management override of controls as a significant risk; as management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. | <ul style="list-style-type: none"> Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to the audit of SCTSJC. In line with our methodology, we will carry out appropriate controls testing and substantive procedures, including over journal entries, and significant transactions that are outside the organisation's normal course of business, or are otherwise unusual. |
| FOCUS AREA | WHY | AUDIT APPROACH |
| Fraud risk from revenue recognition | <p>Professional standards require us to make a rebuttable presumption that the fraud risk from income recognition is a significant risk.</p> <p>SCTSJC receives income in the form of requisitions from the constituent local authorities. As this income is agreed in advance of the year, with adjustments requiring formal approval, we do not regard the risk of fraud from this revenue recognition as significant.</p> | <ul style="list-style-type: none"> We will consider significant elements of income and agree the funding received to Council requisitions and bank statements. We will perform testing of controls over journal entries and substantively test journal entries related to income. |

Code of practice on Local Authority Accounting in the United Kingdom 2015-16 (“the Code”)

The 2015-16 financial statements will be prepared in accordance with the *Code of practice on local authority accounting in the United Kingdom 2015-16* which is based on International Financial Reporting Standards (“IFRS”).

The 2015-16 Code has a number of amendments from the 2014-15 Code and management should consider if these changes will impact the financial statements. The amendments include:

- adoption of IFRS 13 *Fair Value Measurement*, including consequential amendments as a result of adopting this standard;
- amendments to underline the importance of the consideration of materiality when preparing disclosures;
- amendments made as a result of the Local Authority Accounts (Scotland) Regulations 2014; and
- some changes to section 4.10 on heritage assets to reflect that FRS 30 has been replaced by FRS 102.

We consider that the adoption of IFRS 13 may have an impact on the Partnership’s financial statements as there are assets held at fair value.

In accordance with International Standards on Auditing (UK and Ireland) ISA 240 “The Auditor’s responsibility to consider fraud in an Audit of a Financial Report”, we will undertake specific procedures and report findings to management and the Audit and Standards Committee in respect of financial reporting fraud. The following diagram highlights the phases of our work on fraud.

| Discuss fraud | Assess fraud risk | Tailor audit response |
|---|---|---|
| <ul style="list-style-type: none"> ■ Discussions with: <ul style="list-style-type: none"> – Audit and Standards Committee; – Chief Executive; – Director of Finance and HR; and – Finance team members. | <ul style="list-style-type: none"> ■ Preliminary fraud risk assessment: <ul style="list-style-type: none"> – Management oversight; – Internal control framework; – Nature of operations. | <ul style="list-style-type: none"> ■ Our audit procedures are designed to have a reasonable chance of detecting misstatements as a result of fraud or error <ul style="list-style-type: none"> – Review and test the fraud risk assessment process, systems and controls to prevent, deter and detect fraudulent activity. – Evaluate the design of financial reporting controls during process testing to assess their effectiveness in detecting fraud. – Identify and select specific journal entries for detailed substantiation and consolidation journals for appropriate evidence and basis. – Review significant accounting estimates for management bias. ■ The audit team will review and discuss fraud related risks and controls with the Assistant Chief Executive (Business Support), the audit and assurance team and other members of senior management. ■ We will incorporate an element of unpredictability into our testing, as individuals within SPT who are familiar with our audit procedures may be able to use that knowledge to conceal fraudulent financial reporting. |

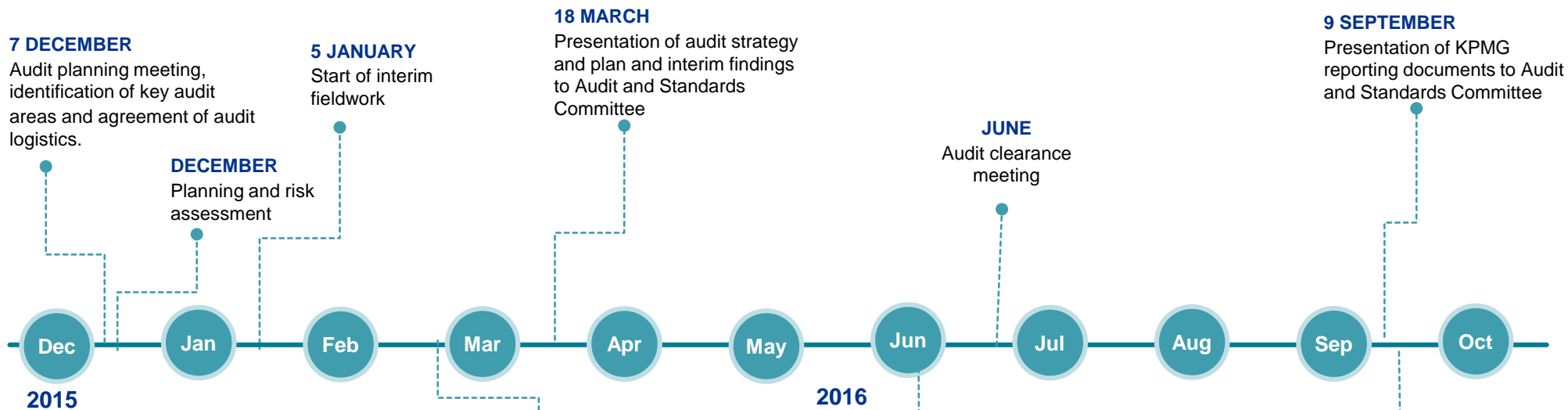


The National Fraud Initiative (“NFI”) is a data matching exercise which compares electronic data within and between participating bodies in Scotland to prevent and detect fraud. We prepared a short return to Audit Scotland on the Partnership’s progress and engagement with the NFI process in February 2016.

The Accounts Commission has developed a new approach to Best Value in 2015-16, with emphasis on driving continuous improvement. This will develop joint responsibility between Audit Scotland’s performance audit and best value group and local auditors. We will continue to work with the performance audit and best value group to consider the approach to best value during this audit, and report our findings in the annual audit report.

In November 2013 the Accounts Commission and Auditor General for Scotland published a report on Scotland’s public sector workforce. It is our responsibility to establish the extent that the Partnership has implemented the recommendations to help identify any common and emerging issues across the public sector. We will perform targeted follow up work, submit a short questionnaire to Audit Scotland and report our findings in our annual audit report.

In accordance with International Standard on Auditing (UK and Ireland) 610: *Considering the work of internal audit*, we will continue liaison with internal audit and evaluate internal audit processes against Public Sector Internal Audit Standards. The general programme of work will be reviewed for significant issues to support our general work in assessing SPT’s annual governance statement. Specific internal audit reviews which will be considered include treasury management and IT controls.



| Audit Scotland reporting deadlines | |
|--|-------------------|
| ■ Audit strategy | 31 March 2016 |
| ■ NFI Report | 29 February 2016 |
| ■ Annual audit report | 30 September 2016 |
| ■ Whole government accounts submission | 30 September 2016 |

| Output | Description | Report date |
|---|--|--|
| NFI report | <ul style="list-style-type: none"> ■ We report on the SPT's actions to investigate and follow-up NFI matches. | <ul style="list-style-type: none"> ■ By 29 February 2016 |
| Audit strategy | <ul style="list-style-type: none"> ■ Our strategy for the external audit of SPT and SCTSJC, including significant risk and audit focus areas. | <ul style="list-style-type: none"> ■ By 31 March 2016 |
| Interim management report | <ul style="list-style-type: none"> ■ We report our findings from our interim audit visit where we will update our planning for the year end and perform controls testing. | <ul style="list-style-type: none"> ■ By 31 March 2016 |
| Submit fraud returns | <ul style="list-style-type: none"> ■ We report on any frauds over £5,000. | <ul style="list-style-type: none"> ■ By 27 May 2016 |
| Independent auditor's report | <ul style="list-style-type: none"> ■ Our opinion on SPT's and SCTSJC's financial statements. | <ul style="list-style-type: none"> ■ By 30 September 2016 |
| Annual audit report to the Partnership and the Controller of Audit | <ul style="list-style-type: none"> ■ We summarise our findings from our work during the year. | <ul style="list-style-type: none"> ■ By 30 September 2016 |
| Submit WGA assurance statement | <ul style="list-style-type: none"> ■ We complete the assurance statement for the preparation of Whole of Government Accounts and submit to the National Audit Office. | <ul style="list-style-type: none"> ■ By 30 September 2016 |

Our interim audit fieldwork was based on updating our understanding of the strategic and operating culture and framework in which services are delivered. Audit procedures performed include inquiring of senior personnel, observing the application of specific controls and inspecting documents and reports.

| Audit area | Key areas considered | Findings |
|------------------------------|---|--|
| Entity level controls | <ul style="list-style-type: none"> ■ Organisation wide policies ■ Audit and standards committee, partnership, strategy and programmes committee, and other committee meetings ■ Risk register ■ Audit and assurance | <ul style="list-style-type: none"> ■ No deficiencies in the entity level controls environment were identified. ■ The entity has a process to identify and address business risks. ■ The major activities that the entity uses to monitor internal control over financial reporting are appropriate. ■ The audit and assurance program is progressing well and no significant findings have been noted. |
| General IT controls | <ul style="list-style-type: none"> ■ User access ■ Super users ■ Passwords ■ Program changes | <ul style="list-style-type: none"> ■ We have considered general IT controls as part of our audit procedures. Our review of controls has focused on access controls. Our testing of IT controls is ongoing and we are hoping to complete this prior to starting our year end audit. |
| Budget monitoring | <ul style="list-style-type: none"> ■ Budget setting ■ Budget monitoring | <ul style="list-style-type: none"> ■ Controls tested over budget setting and monitoring are designed appropriately, implemented and are operating effectively. |

Interim audit Control framework (continued)

Based on our understanding of key audit risk areas we have identified the classes of transactions, disclosure and account balances that are key to the financial statements. Where the audit objective has a controls approach, we have updated our understanding of accounting and reporting activities over each area and identified and tested key financial controls. We have evaluated the design and implementation of these controls and, where appropriate, tested the operating effectiveness.

We are pleased to report that prior year control recommendations have been implemented by management during the period, as noted in the relevant sections below.

| Audit area | Key areas considered | Findings |
|--|---|--|
| Capital and revenue expenditure | <ul style="list-style-type: none"> ■ Payment run processing and approval ■ Tendering process ■ Accounts payable to general ledger reconciliation ■ Third party payments – bus operators | <ul style="list-style-type: none"> ■ Testing adjustments made by the bus operations team to payments made to bus operators found the control to be operating effectively. Following a prior year recommendation, a higher level review of bus operator adjustments has been implemented on a four weekly basis. A summary sheet is prepared, however our testing identified that this had been signed as prepared once it had been returned from review. We recommended that the summary sheet signed as prepared on the date it is prepared and this was implemented immediately. ■ The remainder of the controls tested were found to have been designed appropriately, implemented and operating effectively. |
| Cash | <ul style="list-style-type: none"> ■ Bank reconciliations | <ul style="list-style-type: none"> ■ Our testing identified that bank reconciliations are prepared and reviewed ensuring appropriate segregation of duties. Following a recommendation from our 2014-15 interim report, reconciliations are now dated by the reviewer. Bank reconciliations tested were prepared and reviewed in a timely manner. |
| Payroll costs | <ul style="list-style-type: none"> ■ Payroll exception reporting. | <ul style="list-style-type: none"> ■ Controls tested have been designed appropriately, implemented and are operating effectively. |

Interim audit Control framework (continued)

| Audit area | Key areas considered | Findings |
|-----------------|---|---|
| Journals | <ul style="list-style-type: none"> ■ Automated journal controls ■ Review of journals posted | <ul style="list-style-type: none"> ■ Controls tested over journals are designed appropriately, implemented and are operating effectively. Following previous recommendations, an automated control has been put in place for journals that are prepared by junior members of the finance department to be sent automatically for authorisation by senior accountants. We found this control to be operating effectively. ■ We noted the posting system in place does not allow for out of balance journals to be posted and that access controls for posting journals were operating effectively. |

Appendices

Mandated communications with the Audit and Standards Committee

| Matters to be communicated | Link to Audit Committee papers |
|---|--|
| Independence and our quality procedures ISA 260 (UK and Ireland). | <ul style="list-style-type: none"> ■ See next page |
| The general approach and overall scope of the audit, including levels of materiality, fraud and engagement letter (ISA 260 (UK and Ireland)). | <ul style="list-style-type: none"> ■ Main body of this paper |
| <ul style="list-style-type: none"> ■ Disagreement with management about matters that, individually or in aggregate, could be significant to the entity's financial statements or the auditor's report, and their resolution (AU 380). | <ul style="list-style-type: none"> ■ In the event of such matters of significance we would expect to communicate with the Audit and Standards throughout the year. ■ Formal reporting will be included in our audit highlights memorandum for the September 2016 Audit and Standards Committee meeting, which focuses on the financial statements. |
| <ul style="list-style-type: none"> ■ Significant difficulties we encountered during the audit. ■ Significant matters discussed, or subject to correspondence, with management (ISA 260). | |
| <ul style="list-style-type: none"> ■ Our views about the qualitative aspects of the entity's accounting and financial reporting. ■ The potential effect on the financial statements of any material risks and exposures, such as pending litigation, that are required to be disclosed in the financial statements (ISA 260 and ISA 540). | |
| <ul style="list-style-type: none"> ■ Audit adjustments, whether or not recorded by the entity, that have, or could have, a material effect on its financial statements. We will request you to correct material uncorrected misstatements (including disclosure misstatements) (ISA 450). | |
| <ul style="list-style-type: none"> ■ The selection of, or changes in, significant accounting policies and practices that have, or could have, a material effect on the entity's financial statements (ISA 570). | |
| <ul style="list-style-type: none"> ■ Material uncertainties related to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern (ISA 570). | |
| <ul style="list-style-type: none"> ■ Expected modifications to the auditor's report (ISA 705). | |
| <ul style="list-style-type: none"> ■ Related party transactions that are not appropriately disclosed (ISA 550) | |

Professional ethical standards require us to communicate to you as part of planning all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of Andy Shaw and the audit team. This letter is intended to comply with this requirement although we will communicate any significant judgements made about threats to objectivity and independence and the appropriateness of safeguards put in place.

We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the APB Ethical Standards. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values;
- Communications;
- Internal accountability;
- Risk management; and
- Independent reviews.

Please inform me if you would like to discuss any of these aspects of our procedures in more detail.

There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed to the Finance, Risk and Audit Committee.

Confirmation of our audit independence

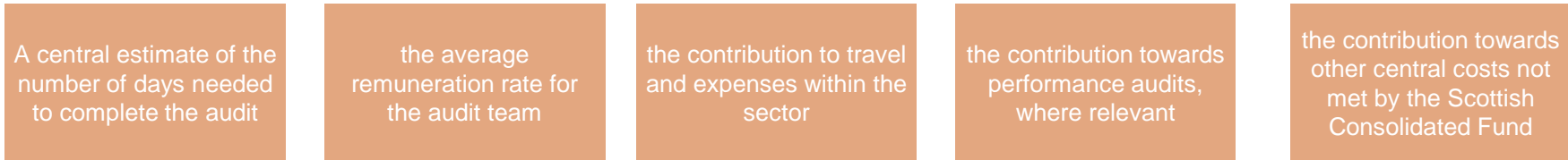
We confirm that as at 26 February 2016, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of Andy Shaw and the audit team is not impaired.

This report is intended solely for the information of the Audit and Standards Committee and should not be used for any other purposes.

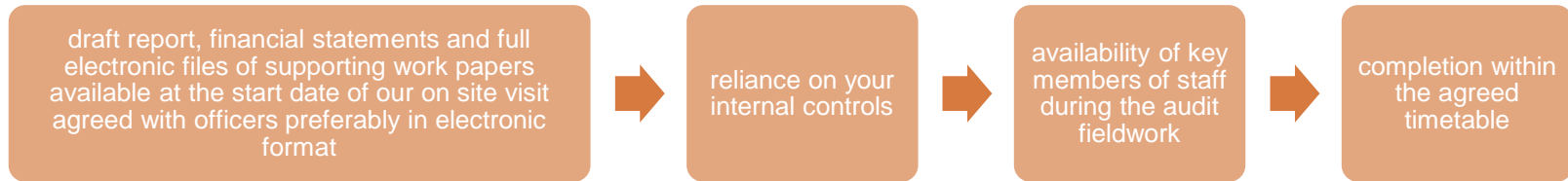
Yours faithfully

KPMG LLP

Audit Scotland requires that the fee for our work is set within an indicative range, depending on the assessment of risk and other factors facing SPT. The indicative fee range is calculated using a number of inputs:



The indicative fee ranges are based on the following assumptions to ensure an efficient audit process:



Audit Scotland has notified us that the fee range for 2015-16 is £58,300 to £71,260 in line with the 2014-15 fee. We have proposed a fee of £64,780, which represents the mid-point. Should we be required to undertake significant additional audit work in respect of any of the areas of audit focus or other matters arise, we will discuss with management the impact of this on our proposed fee.

Strathclyde Concessionary Travel Scheme Joint Committee

For SCTSJC, the applicable fee range is £4,000 to £6,000, with a mid-point of £5,000. We proposed a fee at the mid-point.

Audit Scotland code of audit practice – responsibilities of auditors and management

Responsibilities of auditors

Responsibilities of management

Financial statements

Auditors are required to audit financial statements in accordance with the timescales set by Audit Scotland, which may be shorter than statutory requirements, and give an opinion on:

- whether they give a true and fair view of the financial position of audited bodies and their expenditure and income; and
- whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements.

Auditors should review and report on, as appropriate, other information published with the financial statements, including the directors' report, annual governance statement, statement on internal control or statement on internal financial control and the remuneration report.

Where required, auditors should also review and report on the Whole of Government Accounts return.

Audited bodies' financial statements are an essential part of accounting for their stewardship of the resources made available to them and their performance in the use of those resources. Audited bodies are responsible for:

- ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority;
- maintaining proper accounting records;
- preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the relevant financial reporting framework (e.g. the Financial Reporting Manual or an Accounting Code of Practice);
- preparing and publishing with their financial statements an annual governance statement, statement on internal control or statement on internal financial control and a remuneration report; and
- preparing consolidation packs and, in larger bodies, preparing a Whole of Government Accounts return.

Corporate governance arrangements

Consistent with the wider scope of public audit, the Code gives auditors a responsibility to review and report on audited bodies' corporate governance arrangements as they relate to:

- bodies' reviews of corporate governance and systems of internal control, including their reporting arrangements;
- the prevention and detection of fraud and irregularity;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- the financial position of audited bodies.

Through its chief executive or accountable officer, each body is responsible for establishing arrangements for ensuring the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies usually involve those charged with governance (including audit committees or similar groups) in monitoring these arrangements.

Audit Scotland code of audit practice – responsibilities of auditors and management

| Responsibilities of auditors | Responsibilities of management |
|---|--|
| Systems of internal control | |
| <p>Auditors are required to review and report on the compliance statements given by bodies under the relevant code or framework before their publication. This is discharged by reviewing and, where appropriate, examining evidence relevant to audited bodies' arrangements in accordance with any guidance issued by Audit Scotland. Auditors are not required to consider whether the statements cover all risks and controls, or form an opinion on the effectiveness of procedures, but report where compliance statements are not consistent with their knowledge of the body.</p> | <p>Audited bodies are responsible for developing and implementing systems of internal control, including risk management, financial, operational and compliance controls. They are required to conduct annual reviews of the effectiveness of their governance, systems of internal control, or internal financial control, and report publicly that they have done so. Such reviews should take account of the work of internal audit and be carried out by those charged with governance, usually through bodies' audit committees.</p> |
| Prevention and detection of fraud and irregularities | |
| <p>Auditors should review and report on these arrangements. While auditors do not substitute for audited bodies own responsibilities, and are not responsible for preventing or detecting fraud or irregularity, they should be alert to the potential for breaches of procedures, and of fraud and irregularity. Auditors examine evidence that is relevant to these arrangements, particularly aspects of internal financial control such as segregation of duties, authorisation and approval processes and reconciliation procedures.</p> | <p>Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. This includes:</p> <ul style="list-style-type: none"> ■ developing, promoting and monitoring compliance with standing orders and financial instructions; ■ developing and implementing strategies to prevent and detect fraud and other irregularity; ■ receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity; and ■ participating, when required, in data matching exercises carried out by Audit Scotland. |

Audit Scotland code of audit practice – responsibilities of auditors and management

Responsibilities of auditors

Responsibilities of management

Standards of conduct and arrangements for the prevention and detection of bribery and corruption

Auditors should consider whether bodies have adequate arrangements in place to maintain and promote proper standards of financial conduct and to prevent and detect bribery and corruption. Auditors review and, where appropriate, examine evidence that is relevant to these arrangements and reporting their findings.

While auditors are not responsible for preventing or detecting failure to maintain an appropriate level of integrity and openness, they should be alert to the potential for corruption and breaches of standards of conduct in all aspects of their work. If weaknesses in arrangements are identified or notified, auditors should report them promptly to management or those charged with governance.

Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and should put proper arrangements in place for:

- implementing and monitoring compliance with appropriate guidance on standards of conduct and codes of conduct for members and officers;
- promoting appropriate values and standards; and
- developing, promoting and monitoring compliance with standing orders and financial instructions.

Financial position

Auditors should consider whether audited bodies have established adequate arrangements to ensure that their financial position is soundly based, where appropriate, examining evidence that is relevant to the arrangements.

Auditors should have regard to audited bodies’:

- financial performance in the period under audit;
- compliance with any statutory financial requirements and financial targets;
- ability to meet known or contingent statutory and other financial obligations;
- responses to developments which may have an impact on their financial position; and
- financial plans for future periods.

Audited bodies are responsible for conducting their affairs and for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- such financial monitoring and reporting arrangements as may be specified;
- compliance with any statutory financial requirements and achievement of financial targets;
- balances and reserves, including strategies about levels and future use; and
- the impact of planned future policies and foreseeable developments on their financial position.

Audit Scotland code of audit practice – responsibilities of auditors and management

Responsibilities of auditors

Responsibilities of management

Best Value, use of resources and performance

The Local Government (Scotland) Act 1973 places a duty on the auditors of local government bodies to be satisfied that proper arrangements have been made for securing Best Value and complying with responsibilities relating to community planning.

Auditors of local government bodies also have a responsibility to review and report on the arrangements that specified audited bodies have made to prepare and publish performance information in accordance with directions issued by the Accounts Commission.

Auditors should undertake appropriate work to satisfy themselves that bodies have put in place adequate arrangements for the collection, recording and publication of statutory performance information by reviewing and examining evidence that is relevant to these arrangements in accordance with any guidance issued by Audit Scotland.

Local authorities have a statutory duty to make arrangements to secure Best Value; defined as the continuous improvement in the performance of functions. In securing Best Value, local authorities must maintain a balance of quality and cost considerations and have regard, among other things, to economy, efficiency and effectiveness (or 'value for money') and the need to meet equal opportunity requirements and contribute to the achievement of sustainable development. Local authorities also have a duty for community planning, which is to initiate, maintain and facilitate consultation among and with public bodies, community bodies and others about the provision of services in the area of the local authority and the planning of that provision.

Achievement of Best Value or value for money depends on the existence of sound management arrangements for services, including procedures for planning, appraisal, authorisation and control, accountability and evaluation of the use of resources. Audited bodies are responsible for ensuring that these matters are given due priority and resources, and that proper procedures are established and operate satisfactorily.

The Local Government Act 1992 requires the Accounts Commission to specify information which local authorities must publish about their performance.



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