

Highlands and Islands Transport Partnership (HITRANS)

External Audit Annual Report to the Board and the Controller of Audit for the financial year ended 31 March 2018

September 2018

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Our audit at a glance



We have fulfilled our responsibilities per International Standards on Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice throughout our work and this final report to the Board and the Controller of Audit concludes our work.



Materiality was set at 2% of gross expenditure within our plan, and was updated to reflect the draft financial statements at £29,000. We identified one adjustment to the draft financial statements in relation to defined benefit pension scheme assets and we are satisfied these have been corrected in the financial statements (appendix 2).



Significant audit risks were: management override of controls; the risk of fraud in revenue and expenditure recognition as set out in International Auditing Standards (ISAs UK) practice note 10; and the recognition of defined benefit pension scheme transactions. Our risk assessment remained unchanged and we did not identify any adjustments in these areas in our work.

An audit underpinned by quality



We have built on our understanding and relationship with the Highlands and Islands Transport Partnership (the HITRANS) during the year supporting our audit process.



Our work was undertaken in accordance with our agreed timetable. The draft financial statements produced by officers were of a good standard with complete information and good supporting working papers. We thank officers for their support and assistance during our work.



A wider scope audit for the HITRANS as set out in our plan, was considered not appropriate. However we have considered your financial planning and governance arrangements as part of our audit. We have raised one recommendation, following up on a prior year observation, around the need to develop medium term financial plans.

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Adding value through our external audit work

First and foremost our objective is to ensure we deliver a quality external audit which fully complies with International Standards on Auditing (ISAs) UK and the Audit Scotland Code of Practice (2016). By ensuring our audit is efficient and effective, gives you assurance over our opinion.

Through this Annual Report we seek to provide insight and commentary over certain aspects of the HITRANS's arrangements, sharing relevant practices with the Board and Officers.

We have continued to build on our working relationship with management and our understanding of as an organisation. During the year we have worked with officers to develop our audit approach through greater understanding of your financial transactions.

Introduction

This report is a summary of our findings from our external audit work for the financial year ended 31 March 2018.

Our work has been undertaken in accordance with International Standards of Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice 2016.

In accordance with our reporting responsibilities the report is jointly addressed to the Controller of Audit and HITRANS.

Once finalised this report will be made publically available on the Audit Scotland website (www.audit-scotland.gov.uk)

We would like to thank the HITRANS' officers and the finance team for an effective year-end audit process and all their support and assistance in the audit process.

Structure of this report

As set out in our Audit Plan (February 2018) we consider in accordance with the Audit Scotland Code of Practice that HITRANS is a smaller body. Therefore full wider scope is not appropriate. Our report concludes on our financial statements audit and certain aspects of the HITRANS' arrangements as follows:

Financial statements – Section 2 and Appendix 1

Financial and governance arrangements – Section 2

Our Opinion

For the financial year ended 31 March 2018 we have issued an **unmodified audit opinion**

- True and fair view of the financial statements
- Other information in the annual report
- Other prescribed matters (which include the audited information in the remuneration report)

Basis of preparation

HITRANS' financial statements are prepared in accordance with the 2017/18 CIPFA Code of Practice on Local Authority Accounting ('the 2017/18 Code'). There were no significant changes within the 2017/18 Code that impact on the HITRANS' financial statements.

The audit process

A complete set of financial statements were made available to the public on 28 June 2018, meeting the statutory deadline of the end of June.

The draft financial statements were supported by good working papers and the audit was efficient.

We identified one change to the financial statements and have no unadjusted differences to report. We identified minor disclosure enhancements and these have been reflected in the financial statements (see Appendix 2).

The financial statements audit



Our audit work was completed in accordance with International Standards on Auditing (UK) (ISAs) and the Audit Scotland Code of Audit Practice (May 2016). Based on our audit procedures performed we have issued an unqualified audit opinion on the financial statements including:

- give a true and fair view in accordance with applicable law and the 2017/18 CIPFA Code of Practice on Local Authority Accounting ('the 2017/18 Code');
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code, and with the requirements of applicable law;
- the information given in the Management Commentary is consistent with the financial statements and that report has been prepared in accordance with statutory guidance;
- the information given in the Annual Governance Statement is consistent with the financial statements and that report has been prepared in accordance with applicable guidance; and
- audited parts of the remuneration report have been prepared in accordance with the guidance.

Audit approach and materiality

Our audit approach was set out in our annual audit plan presented to the Board in February 2018. As set out in our plan, our materiality calculations were based on the audited 2016/17 financial statements. We subsequently updated our materiality calculation to be based on the draft 2017/18 financial statements. Overall materiality has been set at £29,000 (2% of gross expenditure) and performance materiality is set at £22,000. (75% of materiality). We report to management any audit difference identified over £2,000 (trivial as 5% of materiality).

We did not identify any additional significant audit risks from those identified in our audit plan.

Internal control environment

During the year we sought to understand the HITRANS's overall control environment (design) as related to the financial statements. Our understanding has built on our understanding of key financial controls processes in place at the Highland Council. In particular we have:

- Considered procedures and controls around related parties, journal entries and other key entity level controls.
- Performed walkthrough procedures on key financial controls in particular journals, ledger controls, income and expenditure transactions.

Our work over controls is limited to our ISA requirements in understanding an entities control environment. Our audit is not controls based and we do not seek reliance over controls. Our audit is fully substantive based in nature.

We identified no material weaknesses or areas of concern from this work which would have caused us to alter the planned approach, set out in our plan.

Internal Audit

As set out in our external audit plan we have not placed formal reliance on the work of internal audit. We reviewed the internal audit plan and individual reports issued to date, to consider if any impact on our audit approach, with none being noted.

The findings of internal audit do not disagree with our knowledge and understanding of the HITRANS as an organisation.

Identified audit risks and our conclusions

	Identified audit risk at planning	Work completed	Our conclusion
Risk of fraud in revenue	<p>As set out in ISA 240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. The majority of HITRANS's income is from government grants. The nature of this income is well forecast and agreed to confirmation letters therefore we rebut the presumed risk around this revenue stream. We therefore focus our risk on other income. The risk is prevalent primarily on transactions around the year end where there is a inherently higher risk of misstatement.</p>	<ul style="list-style-type: none"> Developed our understanding of the HITRANS's material revenue streams including walkthrough of key transactions. Performed targeted review and testing of key revenue streams during the year Performing revenue cut off procedures and substantive testing over pre and post year end balances Testing the existence and recoverability of balances at the year end 	<p>From our audit procedures performed we are satisfied that revenue is free from material misstatement.</p> <p>We are satisfied that transactions have been recognised in the appropriate financial year.</p>
Risk of fraud in expenditure	<p>Operating expenditure is understated or not treated in the correct period (risk of fraud in expenditure). As set out in Practice note 10 (revised) which applies to public sector entities, we recognise that there is a risk that expenditure could be materially misstated. The risk is prevalent primarily on transactions around the year end where there is a inherently higher risk of misstatement.</p>	<ul style="list-style-type: none"> Developed our understanding of the HITRANS's material expenditure streams including walkthrough of key transactions. Perform cut-off at year end on post year end transactions and performed procedures to ensure expenditure allocated in appropriate financial year Confirmed the completeness of creditors balances through testing for unrecorded liabilities 	<p>From our audit procedures performed we are satisfied that expenditure is free from material misstatement.</p> <p>We are satisfied that transactions have been recognised in the appropriate financial year.</p>
Management override of controls	<p>As set out in ISA 240 there is a presumed risk that management override of controls is present in all entities</p>	<ul style="list-style-type: none"> Developed our understanding of the entity level controls in place at the HITRANS that reduce the risk of management override Performed review of journal transactions for unusual transactions or balances. Evaluated key areas of judgement within the financial statements and the basis for these judgements / application of accounting policies Reviewed unusual and/or significant transactions 	<p>We did not identify any significant areas of bias in key judgements by management.</p> <p>We have not identified any unusual or significant transactions during the course of the year that would indicate management manipulation.</p>

Narrative elements of your annual accounts

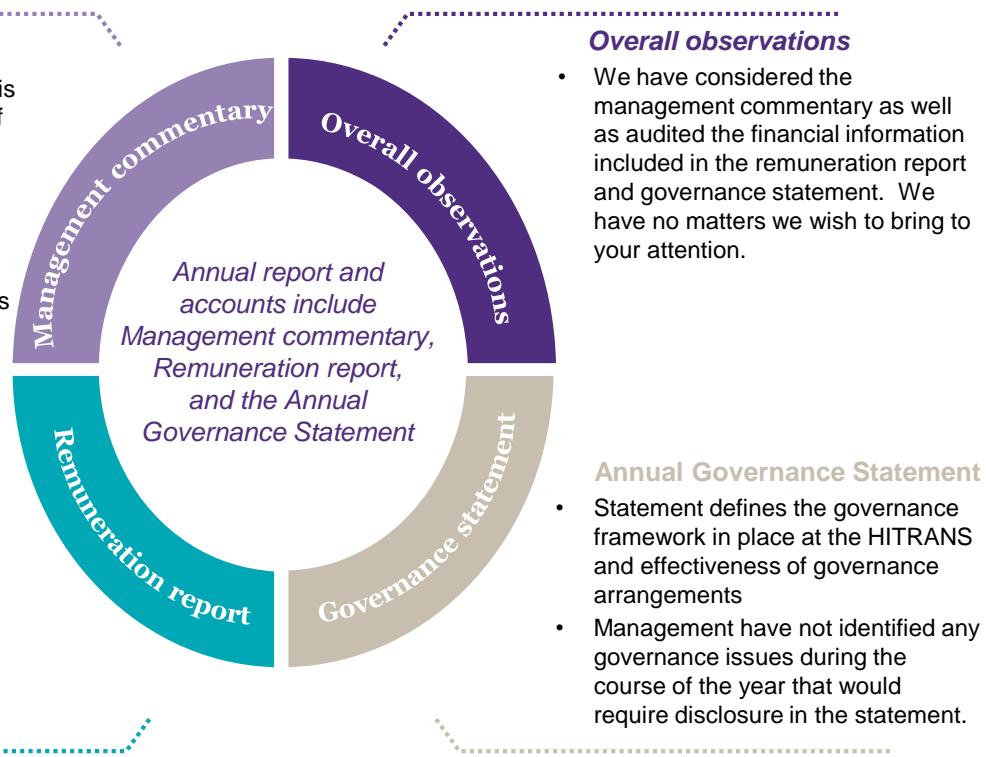
In accordance with our responsibilities we have reviewed your narrative aspects of the Annual Report and Accounts. We have considered the consistency of this narrative with our understanding and the financial statements and have set out our observations below. We have also audited the required information in the remuneration report (marked audited) and have no matters we wish to bring to your attention.

Management commentary

- The Management commentary is in line with our understanding of HITRANS and in particular the vision and strategic priorities of HITRANS
- The Management commentary statement is clear and concise
- Financial Outlook and Key Risks are well articulated and there is discussions around service changes and future developments

Remuneration Report

- The remuneration report has been prepared in accordance with Local Authority Accounts (Scotland) Regulations 2014.
- The Senior Post Holders and Senior Councillors note to the accounts in line with requirements.



Going concern

HITRANS is funded through requisitions from constituent authorities to meet annual operating costs. The HITRANS's share of defined benefit pension scheme liabilities of £0.726 million and holiday pay accruals of £6,000 exceed assets held. Consequently, HITRANS has net liabilities of £0.732 million as at 31 March 2018.

Management are satisfied that the HITRANS will continue to receive funding from constitution authorities to meet annual operating obligations, including pension charges, in delivering statutory services. As a result they are satisfied that the entity continues to represent a going concern. We have obtained confirmation of HITRANS funding for 2018/19 and concur with Officer's going concern assessment.

Fraud and irregularity

In relation to the audit risk of fraud in respect of expenditure we tested the HITRANS' cut off arrangements in particular (timing) and identified no issues in accruals or prepayments which would indicate potential fraud. There are no post balance sheet events or legal uncertainties at year-end. There were no frauds identified by management during the year and no indication of fraud through our audit work.

Key aspects of your financial statements

As set out in our audit plan we consider particular aspects of your financial statements in relation to management judgements including estimates and where management may have particular options or choices in what accounting standards or disclosure requirements to apply. We have summarised where these apply, and our conclusions below.

HITRANS' accounting policies are in accordance with the CIPFA Code of Practice on Local Authority Accounting and we consider these to be appropriate to the organisation and consistent with those adopted in prior years.

HITRANS' financial statements are not complex with limited areas of judgement or estimation. They provide transparent reporting of income and expenditure throughout the year.

Accounting estimates and judgements

HITRANS' significant accounting estimates and judgement impacting on the annual accounts are the following:

- **Defined benefit pension schemes**—HITRANS participates in the Highland Council Pension Fund. The HITRANS recognises its share of the cost of retirement benefits as well as the entity's share of the scheme assets and liabilities. This is estimated through actuarial valuation. During our audit we identified an adjustment to the value of scheme assets as at 31 March 2018. This was due to the actuarial valuation of scheme assets being based on forecast valuation. Due to asset performance exceeding expectation, the actual value of assets was materially higher than outturn position. Management has obtained a revised actuarial valuation and this has been reflected in the final accounts (appendix 2).



Financial and governance commentary

For smaller bodies we are allowed under the Audit Scotland Code of Practice to not apply the full wider scope audit. In our judgement, taking into account the nature of HITRANS and your income and expenditure streams we feel it is appropriate to treat you as a smaller body under the code. However, we will focus on financial sustainability considering your financial sustainability as well as governance arrangements.

Key observations



Financial position & sustainability

HITRANS reported a breakeven position for the year ended 31 March 2018. Funding from constituent authorities was £25,000 below budget, primarily due to the third party contributions received for research and development activity. HITRANS had net liabilities as at 31 March of £0.732 million (2017 : Liabilities of £1.215 million) primarily due to long term defined benefit pension scheme liabilities.

HITRANS face particular financial challenges in balancing public sector funding constraints alongside increasing pressures on pay and non-pay costs. For 2018/19 the HITRANS' budget has assumed that there will be no increase in constituent council requisitions.

Management recognise the medium term pressures facing the organisation and is working towards identifying further cashable efficiency savings for 2019/20. Currently HITRANS, like other transport authorities, faces challenges in planning strategically as it is limited to annual funding settlements and unable to hold reserves. The draft Transport Bill, currently going through the Scottish Parliament legislative process, may enable partnership authorities to retain reserves. This would allow greater strategic financial planning.

Action plan 1.

Like many public bodies, HITRANS faces financial pressures. The Transport Bill, currently going through legislative process, may allow HITRANS the opportunity to retain reserves, providing scope for more strategic financial planning.



HITRANS Governance

HITRANS has an established governance framework in place consisting of policies, procedures and systems of internal control to support the delivery of partnership outcomes. In addition, the Board receives monitoring reports on the progress of delivering the Regional Transport Strategy enabling oversight of the organisation's performance.

Key strategic risks are reported annually to the Board and internal audit provide assurance around the adequacy and effectiveness of HITRANS internal control framework.

From review of corporate publications, the HITRANS board minutes and papers we have not identified any material concerns around governance arrangements in place.

HITRANS has well established governance framework in place. These facilitate monitoring and oversight of the delivery of the Regional Transport Strategy and strategic risks to the organisation.

Appendices

Action plan and follow up of 2016/17 recommendations

Audit adjustments

Independence, fees and fraud responsibilities

Communication of audit matters with the Board

Action plan

We have set out below, based on our audit work undertaken in 2017/18, those risks and recommendations we consider are of a higher risk to HITRANS that Officers may wish to consider in the future.

Recommendation	Agreed management response
Strategic financial planning	<p>Management response: Officers will continue to engage with Transport Scotland to make the case for longer term budget commitments which might become more practical once Scottish Government move to longer term budgeting. Recent proposals for additional Active Travel funding to the RTP have been made on the basis that these should be provided with a guarantee to the end of the current Scottish Parliament term (to 2021).</p>

Strategic financial planning
Due to annual funding settlement as well as restrictions on the organisation's ability to hold reserves, HITRANS financial plans are primarily based on an annual basis. Given the financial pressures facing the organisation it is important that medium to longer term financial plans are in place to ensure that HITRANS has a sustainable operating model in place to support service delivery.

With the draft Transport Bill, there is potentially opportunity for HITRANS to retain reserves in the future providing an opportunity for more strategic financial planning and investment decisions.,.

Timescale: Ongoing and will review at end of March 2019

Action Owner: Partnership Director and Treasurer

Audit adjustments

Uncorrected and corrected misstatements

We are pleased to report that there were no uncorrected misstatements to the financial statements arising during our audit.

The following adjustment was identified during the course of the audit and corrected in the financial statements.

Item	Dr (£'000)	(Cr) (£'000)	Description
1	Other operating income (Pension reserve)	(24)	
	Defined benefit pension liability	24	<i>Being adjustment to recognise defined benefit pension scheme net assets.</i>

Disclosure misstatements

In accordance with auditing standards we are required to highlight significant disclosure misstatements to allow the Board to evaluate the impact of these matters on the financial statements. There were no material/significant disclosure misstatements identified we wish to bring to your attention.

Fees, independence, fraud arrangements

External Audit Fee

Service	Fees £
External Auditor Remuneration	8,250
Pooled Costs	730
Contribution to Audit Scotland costs	520
Contribution to Performance Audit and Best Value	0
2017-18 Fee	9,500

The audit fee was calculated in accordance with guidance issued by Audit Scotland and agreed with Management.

The above fee has not changed and our final fee was £9,500.

Fees for other services

Service	Fees £
We can confirm there are no non-audit fees for the 2017/18 financial year	Nil

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention.

We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

We are required by auditing and ethical standards to communicate any relationships that may affect the independence and objectivity of the audit team.

We can confirm no independence concerns have been identified.

Fraud arrangements

In assessing our audit risks, the audit team was alert to the possibility of fraud at HITRANS.

As part of our audit work we are responsible for:

- identifying and assessing the risks of material misstatement of the financial statements due to fraud in particular in relation to management override of controls.
- Leading a discussion with those charged of governance (for HITRANS this is assumed to be the Board) on their view of fraud.
- designing and implementing appropriate audit testing to gain assurance over our assessed risks of fraud
- responding appropriately to any fraud or suspected fraud identified during the audit. – None were identified in-year

As auditors we obtain reasonable but not absolute assurance the financial statements as a whole are free from material misstatement, whether due to fraud or error.

We will obtain annual representation from management regarding managements assessment of fraud risk, including internal controls, and any known or suspected fraud or misstatement.

It is HITRANS's responsibility to establish arrangements to prevent and detect fraud and other irregularity. This includes:

- 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.

Throughout the audit we worked with HITRANS to review specific areas of fraud risk, including the operation of key financial controls.

We also examined certain policies in place, strategies, standing orders and financial instructions, as relevant to the fraud framework, to ensure that they provide a reasonable framework of internal control.

No suspected frauds or irregularities have been identified by Management and reported in-year.

Communication of audit matters with the Accountable Officer

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance who for HITRANS we deem to be the Treasurer	•	
Overview of the planned scope and timing of the audit, including planning assessment of audit risks and wider scope risks	•	
Confirmation of independence and objectivity	•	•
We are independent of the HITRANS and have not identified any conflicts of interest		
A statement that we have complied with relevant ethical requirements regarding independence. Relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence	•	•
We have not incurred any non-audit fees during the year and no threats to independence identified		
Significant matters in relation to going concern	•	•
No significant going concern matters identified		
Views about the qualitative aspects of the HITRANS accounting and financial reporting practices, including accounting policies, accounting estimates and financial statement disclosures	•	
Set out in the Financial statements Section		
Significant findings from the audit	•	
No significant findings from our audit		
Significant matters and issues arising during the audit and written representations that have been sought	•	
Letter of representation was signed by the relevant Officer. This is our standard, unmodified letter of representation.		
Significant difficulties encountered during the audit	•	
No difficulties encountered		
Significant deficiencies in internal control identified during the audit	•	
None identified		
Significant matters arising in connection with related parties	•	
None identified		
Identification or suspicion of fraud involving management and/or which results in material misstatement of the financial statements	•	
None identified. A nil fraud return was submitted to Audit Scotland in April 2018 in accordance with the planning guidance.		
Non-compliance with laws and regulations	•	
None noted		
Unadjusted misstatements and material disclosure omissions	•	
None noted. Minor disclosure amendments only and these were not material in nature		
Expected modifications to the auditor's report, or emphasis of matter	•	
None, an unqualified opinion		

International Standards on Auditing (UK) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table above. We communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to HITRANS' Officers and the Board



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