INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

Banff and Buchan College

Annual audit report for 2005-06 to the Board of Management and the Auditor General for Scotland

18 December 2006

AUDIT

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Notice: About this report

This report has been prepared in accordance with the responsibilities set out within Audit Scotland's *Code of Audit Practice* ('the Code') and *Statement of Responsibilities of Auditors and Audited Bodies*.

This report is for the benefit of only Banff and Buchan College and is made available to Audit Scotland (together the beneficiaries), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes but that we have not taken account of the requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes 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 scope and objectives section of this report.

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Executive summary

Financial position

The financial statements reflect a surplus for the year of £2,000 and an income and expenditure account balance of £433,000 at 31 July 2006 after a transfer to designated reserves.

The College fully implemented FRS 17 for the first time during 2005-06. In line with the transitional disclosures in prior years, the College has continued to account for their pension costs on a defined contribution basis as the College is unable to identify its share of the underlying assets and liabilities in the Aberdeen City Council Pension Fund on a consistent and reliable basis.

Corporate governance

During the 2005-06 financial statements audit our work has identified no significant weaknesses in the operation of financial controls and procedures.

During the year the College's internal auditor produced audit reports on purchasing / procurement, risk management / business continuity, client services, commercial issues and has conducted a follow up review of the recommendations made in 2004-5 by the College's previous internal auditors. For the areas reviewed, it was reported that 'internal controls do take account of good practice'. In some areas a number of recommendations have been made to 'further improve processes.'

The 2005-06 corporate governance statement on the systems of internal control prepared by the College does not disclose any major weaknesses.

We have not identified any significant control weaknesses in relation to fraud and irregularity, standards of conduct or prevention of corruption.

Financial statements

On 14 December 2006 we issued an audit report expressing an unqualified opinion on the financial statements of the College for the year ended 31 July 2006 and on the regularity of the financial transactions reflected in those financial statements.

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Introduction

Audit framework

2005-06 was the final year of our five-year appointment as external auditors of Banff and Buchan College ("the College"). This report summarises our opinion and conclusions and highlights significant issues arising from our work. While a requirement of Audit Scotland's *Code of Audit Practice*, this report, having been discussed in draft with the audit committee, also discharges our obligations under International Auditing Standard 260: *Communication of audit matters to those charged with governance*.

The framework under which we operate under appointment by Audit Scotland was outlined in the audit plan for the year discussed with the College's audit committee on 8 March 2006.

The scope of the audit was to:

- provide an opinion on, to the extent required by the relevant authorities, the College's financial statements and the regularity of transactions in accordance with the standards and guidance issued by the Auditing Practices Board;
- review and report on, to the extent required by relevant legislation and the requirements of the Code, the College's corporate governance arrangements in relation to systems of internal control, the prevention and detection of fraud and irregularity, standards of conduct, and prevention and detection of corruption; and the College's financial position; and
- review and report on, to the extent required by relevant legislation and requirement of the Code, aspects of the College's arrangements to manage its performance, as they relate to the economy, efficiency and effectiveness in the use of resources.

Our audit planning process identified a number of other areas for specific attention:

- compliance with legislation and financial regulations;
- financial security;
- recognition of funding provided for specific purposes and the regularity of corresponding expenditure.

Basis of information

External auditors do not act as a substitute for the College's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

To a certain extent the content of this report comprises general information that has been provided by, or is based on discussions with, management and staff of the College. Except to the extent necessary for the purposes of the audit, this information has not been independently verified. The contents of this report should not be taken as reflecting the views of KPMG LLP except where explicitly stated as being so.

Acknowledgement

Our audit has continued to bring us into contact with a range of College staff. We wish to place on record our appreciation of the continued co-operation and assistance extended to us by staff in the discharge of our responsibilities. Since this is the final year of our audit appointment it is our intention to minimise the disruption to the College from a change in auditor through briefing and liaison on unresolved issues with the incoming auditor's staff.

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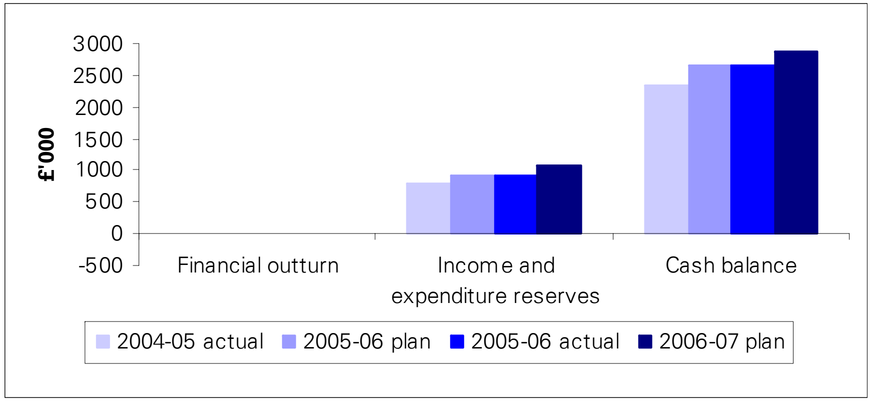
Financial position

Funding Council circular FE/54/02, issued on 20 December 2002, defines a college that is financially secure as one that "*on a continuing basis, is able to generate operating surpluses reliably and as planned, and through that accumulate a reasonable level of financial reserve. The college must also generate sufficient cash to finance its operations and meet its liabilities; regular operating surpluses would ensure this.*"

Figure 1 provides a summary of the College's planned and actual financial results, based on the formal returns submitted by the College to the Funding Council.

Figure 1: comparison of planned and actual results



The financial statements show increases of over 13% in income and expenditure in 2005-06 compared to the previous year reflecting increased Funding Council grants. The surplus for 2005-06 was £2,000 (2004-05: £5,000) after depreciation of fixed assets, in line with break-even budget which was set for the year. On an historical cost basis, the surplus for the year was £123,000 which after a transfer of £483,000 to designated reserves, gives an accumulated income and expenditure balance of £433,000 at 31 July 2006. The College's total cash balances as at 31 July 2006 were £2,652,000 (2005: £2,336,000).

Grant income from the Scottish Funding Council increased by £822,000 due to a 6.8% increase in recurrent funding, plus recognition of additional ring-fenced funding. The College's reliance on its core grant was 76% (2004-05: 77%), but College management are continuing to explore ways to reduce this level of reliance.

The Scottish Funding Council allocated £915,000 of ring fenced funding to the College during 2005-06, primarily for the estates expenditure, financial security, childcare assistance costs and the funding of teachers superannuation. The College's financial monitoring procedures include consideration of the use of this funding to ensure it is used for the purposes identified.

2005-06 SUMS outturn

The College's outturn against its 2004-05 and 2005-06 SUMS targets are shown in Figure 2.

Figure 2: SUMS outturn

	2004-05	2005-06
SUMS target	37,364	**36,667**
SUMS actual	37,945	**37,258**
Impact on recurring grant	£Nil	**£Nil**

Provisions

The College has a pension provision for £321,000 relating to pension costs arising from the early retirements awarded to former employees who are members of the Scottish Teachers' Superannuation Scheme. The provision has been updated to reflect 2005-06 using the assumptions and measurement basis from the prior year.

Capital income and expenditure

The College is not currently undertaking any significant capital programme, with capital expenditure during 2005-06 totalling only £41,000.

Budget

The College's financial forecast return to the Funding Council indicates a break-even position for 2006-07, with a £2,000 surplus for 2007-08. This is in line with the College's traditional tight operating position. The key pressures identified in setting the budget for the year were the then outstanding settlement of the 2006-07 pay award to staff and the known increase to 13.5% in employer contributions to the Scottish Teachers' Superannuation Scheme from April 2007.

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Corporate governance

Introduction

Corporate governance is concerned with structures and processes for decision-making, control and behaviour at the upper levels of the College in accordance with the fundamental principles of openness, integrity and accountability. Management is responsible for establishing arrangements for the conduct of its affairs, including compliance with applicable guidance, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice. The *Code* requires auditors to review aspects of the corporate governance arrangements as they relate to:

- the Board's review of its systems of internal control;
- the prevention and detection of fraud and irregularity; and
- standards of conduct, and the prevention and detection of corruption.

Control environment

The College has in place an appropriate system of high level College-wide financial and corporate governance controls. This includes committee and board structures, a code of conduct per the constitution and articles of governance, a register of board members' interests a scheme of delegation and a risk management strategy which includes an up to date risk register.

During the 2005-06 audit process our work has identified some minor areas for improvement in the operation of financial controls and procedures. Recommendations for formalising the processes around disposal of tangible fixed assets and the monitoring of the deficit position on the College's catering function were discussed with the audit committee on 29 November 2006.

Overall, audit testing of the controls and procedures over teaching income, cash and banking, payroll starters and leavers, and authorisation of payments to suppliers, employees and other creditors revealed no material weaknesses.

Scottish Funding Council Circular FE/35/05 requested that its revised draft financial memorandum should be formally considered by each college's board of management during late 2005 to allow timely and efficient adoption from 1 January 2006 The financial memorandum was agreed by the Board of Management on 14 December 2005.

Oversight of the Council's internal control and reporting arrangements is provided through its audit committee.

Internal audit

During 2005-06, Henderson Loggie were appointed as internal auditors to the College following a tendering exercise. We have reviewed the scope and extent of work performed by internal audit during 2005-06 and considered the impact of their findings and conclusions on our work, where appropriate.

During the year the College's internal auditor produced audit reports on purchasing / procurement, risk management / business continuity, client services, commercial issues and has conducted a follow up review of the recommendations made in 2004-5 by the College's previous internal auditors. For the areas reviewed, it was reported that 'internal controls do take account of good practice'. In some areas a number of recommendations have been made to 'further improve processes.'

Within the internal audit report, 'follow-up reviews' (May 2006), it was reported that eight out of ten recommendations had been fully implemented, one recommendation had been partially implemented and with little progress having been made on the remaining recommendation. There are, however, no high priority recommendations outstanding.

Corporate governance statement

As part of the development of corporate governance, public sector bodies are required to make a statement of how they have applied the principles of corporate governance. We are required to review this to assess whether the description of the process adopted in reviewing the effectiveness of the system of internal control appropriately reflects the process. We are not required to provide an opinion on the College's systems of internal controls.

The 2005-06 corporate governance statement on the systems of internal control prepared by the College does not disclose any major weaknesses.

Fraud and irregularity, standards of conduct, and the prevention and detection of corruption

Work in these areas has been addressed over the duration of our appointment. In relation to fraud, we have had regard to relevant auditing standards when completing our work.

We also had regard to Statement of Auditing Standards 110: *Fraud and Error* and International Standards on Auditing 240: *The Auditor's Responsibility to Consider Fraud in the Audit of Financial Statements*.

Performance audit

The terms of appointment from Audit Scotland include a requirement for a proportion of our audit time to be spent on performance audit work. Performance audit work covers a variety of areas, both financial and non-financial, including both Audit Scotland centrally directed studies and locally determined studies based on agreement between each organisation and their auditors.

No performance audit studies were identified by Audit Scotland for the College during 2005-06.

Reviews and inspections

The College has not been subject to any external inspections in the year in respect of impacting on the financial or governance arrangements of the College.

The Charities and Trustee Investment (Scotland) Act 2005 ("the Act") came into force in April 2006, introducing new duties and responsibilities for the Office of the Scottish Charity Regulator ("OSCR"). Over time OSCR intends to undertake a rolling review of charities entered in the Scottish charity register to assess whether they meet, and continue to meet, the charity test: purposes will have to be charitable in the context of the charity test set out in Section 7 of the Charities and Trustee Investment (Scotland) Act 2005 and charities will have to show that they provide public benefit. OSCR has recently proposed that the first phase of the rolling review should focus on those charities where uncertainty may exist regarding their ability to meet the new test, for example whether stated purposes are charitable, or where 'unduly restrictive conditions', such as fees, may exist. We understand that OSCR has written to parent organisations and umbrella bodies of such charities to inform them of the proposals and to invite comments.

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Audit opinion

On 14 December 2006 we issued an audit report expressing an unqualified opinion on the financial statements of the College for the year ended 31 July 2006 and on the regularity of the financial transactions reflected in those financial statements.

Audit completion

An important measure of proper financial control and accountability is the timely closure and publication of audited financial statements. Figure 3 summarises the key elements of the audit process with which we require management to engage.

Figure 3: key elements of the audit process

Completeness of draft financial statements
A set of draft financial statements were received at the start of the final audit visit, with only a small number of disclosure sections incomplete and few presentational adjustments were required.
Quality of supporting working papers
Due to the high standard of documentation received in prior years we did not issue a separate prepared by client list, requesting only that the documentation required for our audit of the financial statements be prepared in line with that provided in those years. A comprehensive set of supporting working papers were provided from the outset of the audit and were of a suitably high standard.
Response to audit queries
Our routine audit queries were dealt with in a timely and effective manner.

Financial adjustments and confirmations

No adjustments were required to be made to the financial statements in respect of material misstatements or errors. However, a number of disclosure and clarification adjustments were made to ensure SORP compliance and improve the overall presentation of the financial statements.

Confirmations and representations

We confirm that as of 14 December 2006, in our professional judgement, KPMG LLP was independent within the meaning of regulatory and professional requirements and the objectivity of audit staff is not impaired. This has been confirmed separately in writing to the audit committee.

In accordance with auditing standards, we obtained representations from the Board's directors on material issues prior to signing our opinion. There were no audit differences requiring adjustment.

Significant accounting issues

FRS 17: Retirement benefits

The College fully implemented FRS 17 for the first time during 2005-06. In line with the transitional disclosures in prior years, the College has continued to account for their pension costs on a defined contribution basis as the College is unable to identify its share of the underlying assets and liabilities in the Aberdeen City Council Pension Fund on a consistent and reliable basis.

This is consistent with our understanding of the structure of the College's pension schemes, and in accordance with guidance issued by Audit Scotland.