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Members of the Board of Management
Glasgow College of Nautical Studies
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7 December 2006

Auditor General
Audit Scotland
110 George Street
EDINBURGH

Dear Board/Auditor General

REPORT ON THE AUDIT FOR THE YEAR ENDED 31 JULY 2006

I have now completed my audit of the college's accounts for the year ended 31 July 2006.

As part of my responsibilities as external auditor to the college I am required to submit, at the conclusion of each year's audit, a final report addressed both to the members of the Board of Management and to the Auditor General.

This report aims to summarise all significant matters which have arisen during the course of the audit and which I feel are worthy of members' attention.

I have pleasure in attaching my final report on the college's audit for the year to 31 July 2006, which will be submitted to the Board of Management.

I should like to take this opportunity to thank the Principal and her staff for their assistance during the course of the audit.

Yours faithfully

Fiona Mitchell-Knight
Senior Audit Manager

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Glasgow College of Nautical Studies

Report on the 2005/06 Audit

Contents

Key Messages

Introduction

In 2005/06 we audited the financial statements and looked at aspects of performance and governance. This report sets out our key findings, summarising key outcomes in 2005/06 and the outlook for the period ahead.

Key outcomes from 2005/06 audit

We have given an **unqualified** opinion on the financial statements of Glasgow College of Nautical Studies for 2005/06.

The income and expenditure account shows a surplus for the year of £704,000 on the year's operations. The balance on the general reserve has increased from £2,751,000 at 31 July 2005 to £3,695,000 at 31 July 2006. The college's plans for the general reserve are dependent on the outcome of the ongoing review of the Glasgow city centre colleges' estates.

The corporate governance statement complies with accounting requirements and is not inconsistent with audit findings. The statement reflects the fact that adequate assurance can be placed on the college's corporate governance arrangements and internal control systems.

The college was subject to an HMIe inspection from March 2006 to May 2006 and was awarded 2 'Good' and 5 'Very Good' ratings. The overall conclusion was that the college has in place effective learning and teaching processes.

Outlook for future audits

The 2006/07 to 2008/09 college strategy was approved by the Board of Management in June 2006. Progress against the targets set in this strategy will be monitored by the board.

The Glasgow city centre colleges' estates review is ongoing. The outcome of this review is fundamental to how the college will operate in the coming years.

On the basis that the college is unable to identify its share of the underlying assets and liabilities of Strathclyde Pension Fund (SPF), the college's accounts reflect reduced pension disclosure requirements in accordance with accounting guidance. The reduced disclosure requirements do not require the inclusion in the accounts of the full cost of benefit entitlements earned by employees or the asset/liability attributable to the college. Therefore in 2005/06 the requirement to account for pension costs in line with FRS 17 has had no impact on the college's surplus. However, it is envisaged that some of this information may be available for SPF with effect from April 2006. This would require the scheme to be accounted for as defined benefit, and is likely to have a significant impact on the college's financial statements.

This is the final year of our appointment to the audit of Glasgow College of Nautical Studies. From 2006/07 the college's auditors will be BDO Stoy Hayward.

Audit Scotland
November 2006

Introduction

1. This report summarises the findings from our 2005/06 audit of Glasgow College of Nautical Studies. The scope of the audit was set out in our 2005/06 audit planning memorandum, which was submitted to the audit committee on 21st March 2006. This described the audit work we planned to carry out in the year.

2. The financial statements of the college are the means by which it accounts for its stewardship of the resources made available to the college and its financial performance in the use of these resources. In accordance with the Further and Higher Education (Scotland) Act 1992 and the accounts direction issued by the Scottish Funding Council, it is the responsibility of the college to prepare financial statements which give a true and fair view of the college's financial position and the income and expenditure for the year.

3. The Board of Management are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:

   - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed;
   - the college's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests;
   - the college has adequate corporate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability;
   - the systems of internal control provide an appropriate means of preventing or detecting material mis-statement, error, fraud or corruption; and
   - the college has proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

4. This is the final year of a five year audit appointment. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by the Board of Management, the Principal, the Director of Finance and their staff during the course of our audit work.

Performance

Introduction

5. In this section we summarise key aspects of the college's performance and provide an outlook on future performance.

6. It is the responsibility of the Board of Management to ensure that proper arrangements are in place to secure the economy, efficiency and effectiveness in the use of its resources. As part of the auditor's statutory responsibilities we are required to consider whether the college has made appropriate arrangements to fulfil its duty in this regard.

Overview of performance in 2005/06

7. The college has in place a strategy document setting out the college's strategic aims and key targets for the period. The college strategy is reviewed and updated on an annual basis by the Board of Management. Progress against the targets set in the 2005/06 to 2007/08 strategy was reported to the Board of Management in June 2006, and incorporated into the 2006/07 to 2008/09 college strategy. The college strategy is discussed further at paragraph 11.

8. Over recent years the college has attracted increasing student numbers. The college's contract with the Scottish Funding Council is 38,008 weighted SUMS. In 2005/06, this contracted amount was exceeded by 6,757 (8,461 in 2004/05), due to increased demand for training for seafaring personnel and bespoke community programmes and following a policy of non-displacement of other college curricula.

9. HMIe published a report on Glasgow College of Nautical Studies in September 2006 relating to the outcome of a review carried out from March to May 2006. The college was awarded 2 'Good' and 5 'Very Good' ratings and the overall conclusion was that the college has in place effective learning and teaching processes.

10. During the year reports have been published describing the issues which have led to the poor financial health of Inverness College. Senior staff in Glasgow College of Nautical Studies have considered the findings in these reports and they are of the view that the weaknesses in corporate governance arrangements identified in the Inverness College are not replicated in Glasgow College of Nautical Studies. These findings are now to be considered by the Audit Committee and the Board of Management.

Performance outlook

11. In June 2006, the Board of Management approved the college strategy 2006/07 to 2008/09. This identifies the college's purpose as being *"to provide a relevant, responsive, excellent, innovative and inclusive education and training service to its identified market, to ensure full participation in the pivotal role played by colleges in delivering the learning society".* Key targets are set to support the achievement of the five strategic aims:

    - Relevant - the college will develop and promote its course portfolio and education and training service through identifying and responding to customer needs, by liaising with its customer base and in partnership with its stakeholders. This will be facilitated through analysis and evaluation of market information, self evaluation and college performance indicators;
    - Responsive – in accordance with its mission statement, the college will continue to address the differentiated needs and expectations of its diverse customer base in order to raise the quality of life and economic opportunities for all on a socially and environmentally sustainable basis;
    - Excellent – through placing the learner at the centre of college systems we will facilitate support and guide learners, evaluate and assess their achievements effectively and embed a quality culture across all areas of college activities;
    - Innovative – college provision will proactively respond to informed and accurate perceptions of customer needs and demands together with future opportunities, expectations and government directives. Investment will be made in staff employment and development, in the college estate, equipment and ICT as appropriate; and
    - Inclusive – in working towards wider access to further and higher education and creating an inclusive society where everyone can contribute, the college will, through recognition of the particular needs of its local population, continue to provide appropriate supported learning choices and ensure equal opportunities for all.

12. The college strategy includes clear links to other strategy documents which have been approved by the Board of Management, and demonstrates how these support each strategic aim.

13. The college strategy states that it is essential that the college develops a course of action which enables the current education and training service to be properly and sufficiently resourced to provide an appropriate response to the markets in the future. The strategy reflects the Glasgow city centre colleges' estates review which is ongoing. The outcome of this review is fundamental to how the college will operate in the coming years.

Financial position

Introduction

14. In this section we summarise key aspects of the college's reported financial position and performance to 31 July 2006 and provide an outlook on potential future financial risks.

Revenue Account

Revenue performance 2005/06

15. The college's income and expenditure account shows a surplus for the year of £704,000 on the year's operations compared to an expected surplus of £875,000 as per the 2005 financial forecast return (FFR). This overspend was primarily due to a higher than anticipated staff pay award (4% compared to 3% included in budget). The college's surplus in 2004/05 was £737,000 and £274,000 in 2003/04. The college's 2006 FFR records an anticipated surplus of £636,000 for 2006/07.

16. After adjusting for the difference between the actual depreciation charge for the year and depreciation based on historical cost, a historical cost surplus of £948,000 is shown (£981,000 in 2004/05).

17. The balance brought forward on the general reserve at 1 August 2005 was £2,751,000. An amount of £244,000 was transferred from the revaluation reserve to the general reserve in respect of the depreciation charge for the year and £4,000 was transferred from the general reserve to restricted reserves. The balance on the general reserve at 31 July 2006 is £3,695,000. The college's plans for these funds are dependent on the outcome of the ongoing review of the Glasgow city centre colleges estates.

Pension Disclosures

18. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions including projecting increased life expectancy. *Financial Reporting Standard 17 (Retirement Benefits)* is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. 2005/06 is the first year of full FRS 17 disclosure requirement for further education colleges. This means that for defined benefit schemes, the pension asset or liability attributable to the college has to be recognised in the balance sheet and the full costs of benefit entitlements earned by employees, and not simply the cost of employer contributions to the fund, are to be reflected in the income and expenditure account.

19. Retirement benefits to employees of the college are provided by the Scottish Teachers' Superannuation Scheme (STSS) and the Strathclyde Pension Fund (SPF). These are both defined benefit multi-employer schemes. On the basis that the college is unable to identify its share of the underlying assets and liabilities of both schemes, the college has used reduced disclosure requirements available for defined benefit schemes in accordance with FRS 17. The reduced disclosure requirements are the same as for a defined contribution scheme, and do not require the inclusion in the accounts of the full cost of benefit entitlements earned by employees or the asset/liability attributable to the college. Therefore in 2005/06 the requirement to account for pension costs in line with FRS 17 has had no impact on the college's surplus.

20. In recent years, there has been an ongoing national debate as to whether local government pension schemes, of which SPF is one, should be accounted for as defined benefit or defined contribution schemes. Scottish Funding Council guidance for 2005/06 says that the characteristics of the SPF scheme enable colleges to consider using the reduced disclosure requirements. In common with other colleges, the treatment adopted by the college is in line with this guidance. However, this represents a change in accounting policy from previous years, and this has been reflected in the statement of accounting policies included within the financial statements.

Financial position outlook

21. Strathclyde Pension Fund (SPF) has issued a funding strategy statement for consultation. It is envisaged that separate employer rates will be introduced by 2008 at the earliest though a small number of separate rates may be introduced with effect from April 2006. Assets are currently apportioned based on the liability profile though employer assets have been tracked for each employer since 2002. Indications are, therefore, that in future years the college will have the information required to enable it to account for the SPF as a defined benefit scheme, and reflect the full costs of benefit entitlement, and any asset or liability in the scheme in the financial statements. This is likely to have a significant impact on the college's financial statements in future years.

Governance

Introduction

22. In this section we comment on key aspects of the college's governance arrangements during 2005/06.

Overview of arrangements in 2005/06

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

24. The corporate governance statement included within the financial statements reflects the Board of Management's view that adequate assurance can be placed upon the adequacy and effectiveness of the college's corporate governance arrangements and internal financial control system.

25. In our opinion, the corporate governance statement included within the financial statements complies with the requirements of the accounts direction and is not inconsistent with the findings of our audit.

Systems of internal control

26. It is the responsibility of the college's management to maintain adequate financial systems and associated internal controls. The auditor evaluates these systems of internal control, both for the purpose of giving an opinion on the statement of accounts, and in order to report to the college on the adequacy of such systems and controls.

27. A review and assessment of the college's corporate governance arrangements was carried out. This assessment included a review of the college's committee minutes and completion of a number of standard Audit Scotland checklists. This work confirmed that overall the college's corporate governance arrangements appear to be well developed and operating effectively.

28. Audit's conclusions are that overall the college's financial systems are adequate for the purpose of producing the financial statements.

Review of internal audit

29. Internal audit plays a key role in the college's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. To maximise the reliance that can be placed on internal audit and to avoid duplication of effort, the adequacy of internal audit is assessed each year.

30. Internal audit services are provided by Deloittes. An assessment was made of the adequacy of the internal audit input and it was concluded that external audit can place formal reliance on their work.

31. Overall, satisfactory progress has been made in implementing internal audit recommendations and progress towards any remaining actions will continue to be monitored by the Audit Committee.

32. Internal audit's annual report to the Board of Management for 2005/06 says that, based on the work done, they have found that the college has an adequate framework of controls over the systems examined.

Prevention and detection of fraud and irregularities

33. The college has appropriate arrangements in place to prevent and detect fraud. These arrangements include policies on the prevention of fraud and whistle-blowing.

34. The Director of Finance has confirmed that no frauds were identified in 2005/06.

Financial statements

Introduction

35. In this section we summarise key outcomes from our audit of the college's financial statements for 2005/06. We comment on the accounting issues faced and provide an outlook on future financial reporting issues.

36. We audit the financial statements and give an opinion on:

- whether they give a true and fair view of the financial position of the college and its expenditure and income for the period in question; and
- whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.

37. We also review the corporate governance statement by:

- considering whether disclosures in the statement comply with the requirements of the Scottish Funding Council; and
- assessing whether disclosures in the statement are consistent with our knowledge of the college.

Overall conclusion

38. We have given an **unqualified** opinion on the financial statements for 2005/06.

39. The college's unaudited financial statements were submitted for audit on 18 September 2006, in line with the agreed timetable. A file of working papers was provided, and this was of a high standard. Key staff were readily available for consultation throughout the audit process which enabled the audit to progress smoothly.

40. Audit Scotland's work during 2005/06 included the audit of the student support funds. Revisions were made to the bursary fund figures, and a minor procedural recommendation was made to the relevant officers in relation to the HE hardship fund and childcare fund. The student support funds have now been certified.

Accounting practice

41. The college's financial statements comply with the requirements of the statement of recommended practice: accounting for further and higher education (SORP) and the funding council's 2005/06 accounts direction. During the course of the audit a number of issues arose which were resolved in discussion with the Director of Finance. This practice is an established part of the audit process. A number of minor changes have been made to the accounts following completion of the audit.

Intangible assets

42. No intangible assets are disclosed within the college's balance sheet. In 2005/06, the Director of Finance considered whether to capitalise a software licence, however, took the decision that as the college operates a rolling programme for the continual replacement of software, the most appropriate treatment would be to include the purchase of the software licence in the income and expenditure account for the year. Audit is of the opinion that this treatment is reasonable, however, the college should continue to consider the capitalisation of future purchases of software licenses which extend beyond one year and which are above the college's de minimis level of £5,000 for individual items.

Legality

43. Each year we request written confirmation from the Principal that the college's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Principal has confirmed that, to the best of her knowledge and belief and having made appropriate enquiries of the board of management, the financial transactions of the college were in accordance with the relevant legislation and regulations governing its activities.

44. There are no additional legality issues arising from our audit which require to be brought to the board's attention.

Financial reporting outlook

45. Overall the college is well placed to continue to prepare annual financial statements in accordance with accounting and statutory requirements. It has a record of responding positively to audit issues and developing accounting practice.

Change of external auditor

46. Regular rotation of auditors is required by auditing standards and is an important component in guarding against perceived or actual threats to auditors' objectivity and independence. Audit Scotland's policy is to rotate auditors at least once every five years. Where the audit is carried out by Audit Scotland staff rather than a private firm, the engagement lead and other key staff will be rotated.

47. This is the final year of our current appointment to the audit of Glasgow College of Nautical Studies. From 2006/07 BDO Stoy Hayward will become the college's appointed auditor. The change of auditor represents an opportunity to build on existing good practice to continuously improve accounts preparation processes in partnership with the incoming auditor.

Final Remarks

48. The members of the board of management are invited to note this report. We would be pleased to provide any additional information that may be required.

49. The co-operation and assistance given to us by the Principal, the Director of Finance and their staff over the five years of our audit appointment is gratefully acknowledged.

Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Risk Identified	Planned Action	Responsible Officer	Target Date
1	The Glasgow college estates review is not yet complete. The outcome of this review will have a significant impact on the college's activities.	Ongoing review by the Principal and the Board of Management.	Principal Board of Management	Ongoing
2	Separate employer rates may be available for the Strathclyde Pension Fund with effect from April 2006, and this would mean that the pension scheme would be accounted for as a defined benefit scheme, with the full costs of benefit entitlement, and any asset or liability in the scheme included in the financial statements. This is likely to have a significant impact on the college's financial statements in future years.	Continue to monitor developments in this area.	Director of Finance Board of Management	Ongoing