Moray College

Report to Members on the 2005/06 Audit

30 November 2006

AUDIT SCOTLAND

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- providing independent reports to public sector bodies on their finances, their corporate governance and how they manage their performance and secure value for money

- providing an independent opinion on whether the annual financial statements of public sector bodies have been prepared in accordance with statutory requirements

Contents

Executive summary

1. This report summarises the main issues arising from the 2005/06 audit. Key aspects of the College's performance are highlighted in the table below, based on the audit work undertaken.

Financial statements
• The financial statements present a true and fair view of the College's financial position. • The Corporate Governance Statement complies with accounting requirements and is not inconsistent with audit findings. • Final accounts preparation procedures and working papers were very good, with only minor changes made as a result of the audit. • The financial statements include full provision for the value of unfunded pension liabilities. • Moray College has treated the Local Government Pension Scheme as a defined contribution scheme for the purposes of disclosure made in the accounts.
Financial position
• The College's surplus for the year was £0.336 million, in line with forecasts reported to the Board of Management throughout 2005/2006. • The Financial Forecast Return (FFR), submitted to the Scottish Funding Council in June 2006, categorises the financial health of the college as "secure" for the current and next three financial periods. The College's improving financial "health" is borne out by improvements in the ratios derived from the financial statements of the College.
Corporate governance
• Most aspects of a sound corporate governance framework are in place. • The College has developed its Risk Management Strategy. • An Audit Committee meets regularly to review issues of governance. • An anti-fraud & corruption policy is in place, supported by a whistleblowing policy. • The reports of the Internal Auditor do not identify any significant system weaknesses or material errors.

2. Key issues for the attention of members are outlined in the Action Plan included in this report.

Introduction

3. The Board of Management is responsible for the administration and management of the College's affairs, including ensuring an effective system of internal control, and is required to present audited financial statements for each financial year. 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 the authority's assets and interests;
- the College has adequate corporate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability; and
- the systems of internal control provide an appropriate means of preventing or detecting material mis-statement, error, fraud or corruption.

4. This report summarises the most significant issues arising from our work during 2005/06.

Financial statements

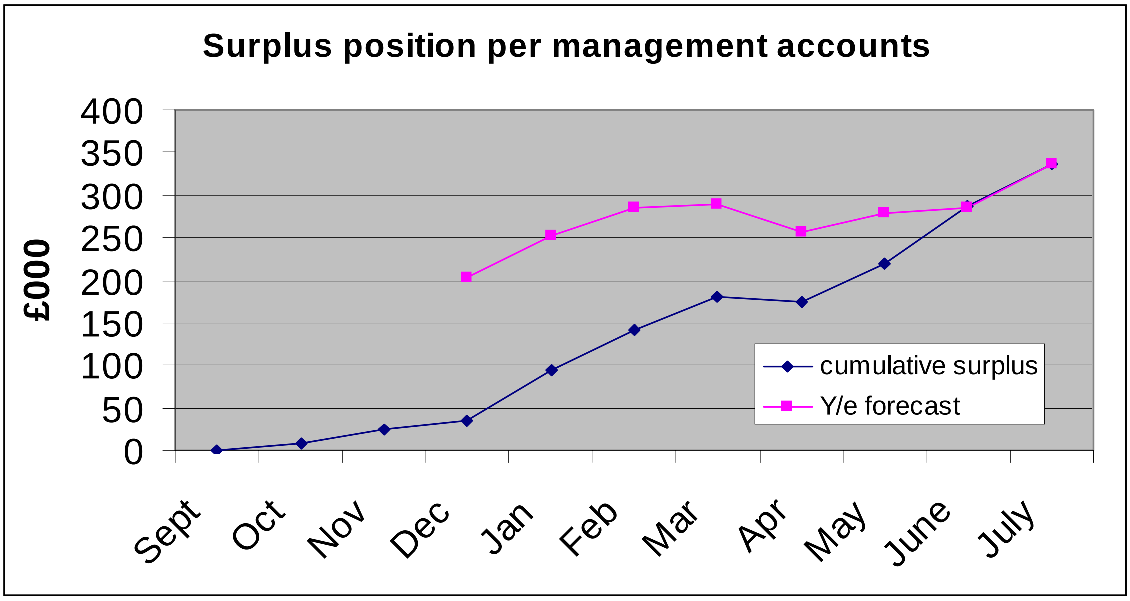
Auditor's report

5. The financial statements give a true and fair view of the College's financial position at 31 July 2006 and income and expenditure during the year.

Financial position and monitoring

6. The College achieved an in-year surplus of £336,000 (£515,000 historic cost surplus). During the year, the finance department led an initiative to tighten budgets to avoid an adverse out-turn against a projected surplus of £333,000 identified in the Financial Forecast Return (FFR). Budget holders played a key part in delivering year-end savings estimated at £100,000.

7. Forecast out-turns were reported to the Board of Management throughout 2005/2006. The monthly management accounts demonstrate the accumulation of the out-turn position. Shallow growth, through favourable variances against budget in the first five months, was boosted by a release of unused sub-contractor budget from January onwards. The revised growth in the surplus was sustained to the year end, with the exception of shortfalls in education contracts and job centre referrals in April.



8. In terms of the ongoing financial position of the College the FFR, submitted to the Scottish Funding Council in June 2006, categorises the financial health of the college as "secure" for the current and next three financial periods. Improvements in financial "health" are also borne out by improvements in the ratios derived from the financial statements of the College:

- current assets exceed current liabilities and the position has improved (from 1.06 to 1.28);
- cash flows from operating activities are positive and represent 15% of total liabilities (compared to 6% last year);
- the debt ratio (total creditors vs total assets) is consistently about 23%; and
- the interest cover is over 3 times the interest payments made.

9. At 31 July 2006 the College had reduced its accumulated general reserve deficit to £1.3 million (from £1.8 million in at 31 July 2005).

Issues arising

10. The College's audited financial statements and my final report are to be submitted to the Auditor General by 31 December. I am pleased to record that, following approval of the financial statements by the Board of Management on 19 December the audited financial statements will be submitted within this timetable.

11. In accordance with the agreed close-down timetable the unaudited financial statements were received on 26 September and our audit fieldwork commenced on 2 October 2006.

12. Some minor adjustments were made to the amounts and disclosures included in the unaudited accounts. In particular:

- the transfer between the revaluation reserve and general reserve, representing in-year depreciation on the revalued element of assets, was increased by £14,000;
- disclosures relating to financial commitments under operating leases were revised; and
- expenditure and balances on the bursary and other student support funds have changed slightly.

13. Matters arising from the audit of the financial statements are summarised below.

Unfunded pension liabilities

14. The valuation of the unfunded pension liability has been reviewed and discounted at 2.2% (previously this was 3%) in accordance with 2005/2006 SFC guidance. The valuation relates to individuals where ongoing enhancements are paid directly by the College and by Aberdeen City Council Pension Fund, which are reimbursed by the College. The total value of unfunded liabilities at 31 July 2006 is £2.7 million.

Pension disclosures

15. Moray College is a member of the "Local Government Pension Scheme (LGPS) – Aberdeen City Council Pension Fund" and makes contributions to the Scottish Teachers Superannuation Scheme (STSS). From 2005/2006, the College has fully implemented Financial Reporting Standard (FRS) 17. FRS17 sets out the accounting treatment for pension and other retirement benefits. The FRS recognises that in some cases a defined benefit scheme will require to be accounted for as if it were a defined contribution scheme. This situation applies to Moray College, as the College is unable to identify its share of the underlying assets and liabilities in both schemes on a consistent and reasonable basis.

Revaluation Reserve

16. Each year, in the financial statements, the College makes a transfer from the revaluation reserve to the statement of historical cost surpluses and deficits. This transfer reflects the difference between depreciation based on historical cost and depreciation based on current replacement cost (after incorporating revaluation). The College has undertaken individual calculations for each asset and is now able to establish the amount of revaluation reserve attributable to each asset. This will ensure the accuracy of future transfers and to ensure any future individual asset disposals or revaluations can be correctly reflected in revaluation reserve movements.

Legality

17. In reporting my opinion on the College's financial statements I am required to report "as to whether, in all material respects, funds from whatever source administered by the College for specific purposes have been properly applied for the intended purposes". The College is in receipt of a number of specific grants and appropriate records are maintained within its accounting systems to match income and expenditure and I have not identified any material mis-application of funds.

18. With regard to the source and application of Higher Education (HE) funding, relative student activity provides a reasonable guide and basis for the allocation of costs and the activity achieved. Actual activity (811) is reasonably consistent with the funded target (798). I accordingly conclude that, in all material respects, funding for the Further Education and Higher Education streams were applied for their intended purposes.

19. There are no additional legality issues arising from our audit which require to be brought to board members' attention.

Corporate governance statement

20. The College, in accordance with the Accounts Direction, has included in its financial statements a statement covering the responsibilities of the Board of Management in relation to corporate governance. The statement records that the Board complies with all of the provisions of the Combined Code on Corporate Governance 1998 and it has complied throughout the year ended 31 July 2006. Our review of the statement of corporate governance concluded that it complies with guidance and is not inconsistent with other information we are aware of from our audit.

21. The College has not yet adopted the revised corporate governance combined code (2003) and is applying the 1998 Combined Code. Full compliance with the 2003 Code is required from next year (2006/2007) and I recommend that the College obtains and reviews the revised code at an early opportunity.

Bursary and other student support funds

22. Notes to the financial statements, identify a number of funds which are not included in the College's Income & Expenditure Account and which are subject to separate audit certification. The Internal Auditor has confirmed that there are no significant issues arising from their work and consequently I have formed the view that there are no material issues arising from the audit of these funds.

Corporate governance

Overview

23. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. Last year we reported that although the College had most aspects of a sound corporate governance framework in place, further improvement was still required on the identification and evaluation of all significant operational risks to the College.

24. A review and assessment of the College's corporate governance arrangements was carried out during the audit. This assessment included a review of the College's committee minutes and completion of a number of standard Audit Scotland checklists. The checklists cover issues relating to systems of internal control, arrangements for the prevention and detection of fraud and corruption, standards of conduct, issues of legality and the College's financial position.

25. Specific developments are set out in the following paragraphs.

Risk management

26. There has been significant progress in developing/ updating risk management with the College during 2005/2006. Work was undertaken to enhance the Risk Management Policy and the Risk Management Group met on six occasions to review the Risk Register and put in place an action plan to manage the top 25 identified risks. The Director of Finance has conducted a number of risk workshops to increase awareness amongst College staff. As Risk Management processes are further developed in subsequent years, the College should consider demonstrating a link with Strategic Objectives; widening the process of identifying risks; and by embedding risk management as a normal part of general management practice.

Anti-fraud and corruption arrangements

27. The College has appropriate arrangements in place to prevent and detect fraud and corruption. The existing fraud and corruption policy was approved in February 2003 and a "whistleblowing" policy was approved in July 2005.

Systems of internal control

28. The College has an Audit Committee which meets regularly to review reports from the senior management team, internal auditors and Audit Scotland.

29. Reliance was placed on the work of internal audit in 2005/06 to evaluate a number of key systems in place within the College. I have reviewed the reports of the internal auditor and have not identified any significant system weaknesses or material errors from their work.

Previous Years Follow up.

30. Our review confirmed that all 5 of the issues identified in our 2004/05 audit report have been addressed.

Action plan

No.	Issue, risk & recommendation	Responsible officer	Response & agreed action	Action date
1. (para 21)	**Revised Combined Code on Corporate Governance 2003** The College identifies in the financial statements that it has complied with the 1998 Code. Compliance with the Revised Code on Corporate Governance is required with effect from 2006/2007. *Risk: The College may not anticipate, or incorporate, changes in the Code on Corporate Governance.* ***Recommendation:*** The College should review the Combined Code on Corporate Governance 2003 and identify any actions that may be required.	W Duncan	Agreed, the College will review the Combined Code on Corporate Governance 2003.	31 March 2007
2. (para 26)	**Risk Management** There has been significant progress in developing/ updating risk management with the College during 2005/2006, but this could be further developed by demonstrating a link with strategic objectives; widening the process of identifying risks to other staff/management groups; and by embedding risk management as a normal part of general management practice. *Risk: Major risks relating to strategic objectives will not be identified or addressed and actual management practice may not reflect organisational risk management priorities.* ***Recommendation:*** Risk management should demonstrate a link with strategic objectives; include other staff/management groups; and embed risk management as a normal part of general management practice.	F Hutcheon	Agreed, the Risk Management Group will ensure that risk is clearly linked to the strategic objectives.	31 March 2007