SCOTT-MONCRIEFF
EDINBURGH AND GLASGOW

Motherwell College

External Audit Annual Report to the Board of Management and the Auditor General for Scotland 2006/07

6 December 2007

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1 Summary

Finance

- Our audit opinion on the truth and fairness of the College's financial statements is unqualified.
- Our regularity opinion is also unqualified.
- The accounts comply with the Accounts Direction issued by the Scottish Funding Council (SFC) and the Statement of Recommended Practice on Accounting for Further and Higher Education. The deadline for submitting final accounts to SFC will be achieved.
- The College reported a surplus of £2,090,000 to 31 July 2007 (2005/06 - £1,093,000). The historical cost surplus was £2,310,000 after releasing £220,000 from the revaluation reserve in respect of depreciation on re-valued assets.

Governance

- We identified no significant errors or weaknesses during our audit. In general, the College's systems of internal control appear to be adequate, well designed and operating effectively.
- The College has established effective risk management arrangements which are as strong as we have seen in the sector.
- The College's Corporate Governance Statement confirms that the College has been fully compliant with the key principles of the 2003 Combined Code on Corporate Governance during 2006/07.
- A revised Combined Code was issued in 2006 and will be applicable from 2007/08.

Conclusion

This report concludes the 2006/07 audit of Motherwell College. We have performed our audit in accordance with the Code of Audit Practice published by Audit Scotland, International Standards on Auditing and Ethical Standards.

This report has been discussed and agreed with the Director of Finance and Physical Resources and the Financial Controller and has been prepared for the sole use of Motherwell College, the Auditor General for Scotland and Audit Scotland. We would like to thank all members of the College's management and staff who have been involved in our work for their co-operation and assistance during our audit.

Scott-Moncrieff

6 December 2007

2 Introduction

2.1 Auditor General and Audit Scotland

The Auditor General for Scotland is responsible for reporting to the Scottish Parliament on how public bodies spend public money, manage their finances and achieve value for money in the use of public funds. In discharging this responsibility the Auditor General appoints FE College auditors and sets the terms of their appointment.

Audit Scotland is an independent statutory body that provides the Auditor General with the services required to carry out his statutory functions, including preparing a Code of Audit Practice setting out the role and responsibilities of the external auditor.

2.2 Audit appointments

The Auditor General for Scotland has appointed Scott-Moncrieff as external auditor of Motherwell College for the five year period 2006/07 to 2010/11.

This annual report summarises our 2006/07 audit of Motherwell College and highlights the key issues arising from our work.

2.3 Independence and ethical standards

Ethical Standard 1 – *Integrity, objectivity and independence*, issued by the Auditing Practices Board (APB), requires that external auditors ensure that the Audit Committee is appropriately informed on a timely basis of all significant facts and matters that bear upon the auditors' objectivity and independence.

We can confirm that we have complied with the APB Ethical Standards throughout the audit and that, in our professional judgement, we have remained independent and our objectivity has not been compromised in any way.

2.4 Key risks

Our audits are risk based. This means that we focus our resources in the areas of highest priority or risk to the Board. The key audit issues identified for the 2006/07 audit were summarised in our external audit plan presented to the Audit Committee on 25 September 2007. These audit issues were:

- Disposal of the current College site,
- Acquisition of new site and commencement of the College's New Build Programme,
- Combined Code of Corporate Governance,
- Financial Reporting Standard 17 – Retirement Benefits (FRS 17).

This report includes our findings in relation to these key risk areas.

2.5 Scope of the audit

Our audit work can be classified under the following two headings: governance and finance. The main audit objective for each of these areas is summarised below.

2.5.1 Audit areas and audit objectives

Audit area	Audit objective
Governance	To review the College's governance arrangements in relation to: • systems of internal control and risk management, • the prevention and detection of fraud and irregularity, • standards of conduct and prevention and detection of corruption.
Finance	To provide an opinion on the truth and fairness of the College's financial statements and on the regularity of transactions. To review the College's financial standing, and financial management arrangements.

The remainder of this report sets out the results of our work in 2006/07 under the headings of Governance and Finance. The action plan in section 5 details the recommendations we have made during the year.

3 Governance

3.1 Introduction

The audited body has a responsibility to:

- Develop and implement systems of internal control and at least annually to conduct a review of the effectiveness of the internal control systems.
- Establish arrangements to prevent and detect fraud and irregularity.
- Ensure its affairs are managed in accordance with proper standards of conduct.
- Conduct its affairs and to put in place proper arrangements to ensure that its financial position is soundly based.

It is our responsibility to review and report on the College's governance arrangements.

It is also our responsibility to review the College's governance arrangements in relation to its financial position. This is reported in section 4 – Finance.

3.2 Corporate Governance framework

The Board of Management has formally established the following sub-committees, which contribute to the culture of risk management and internal control at the College: Finance Committee, Audit Committee, Human Resources Committee, Relocation Committee and Remuneration Committee.

3.3 Corporate Governance statement

3.3.1 Requirement for a corporate governance statement

Colleges are required to include a statement on their corporate governance arrangements within their annual accounts. The statement describes the ways in which the College has complied with good practice in corporate governance, including the arrangements for risk management.

3.3.2 The College's corporate governance statement for 2006/07 – fully compliant statement

The College's corporate governance statement for 2006/07 illustrates that the College was fully compliant with the 2003 Code throughout the period.

Principle A6 in the 2003 Combined Code states that "The Board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors." The Board of Management is currently going through a process of self evaluation. To further strengthen the self evaluation process, we recommend that the Board of Management complete a formal, annual evaluation exercise. This process should be formally documented. *See action plan point 5.2.1.*

3.3.3 Combined Code 2006

A revised Combined Code on Corporate Governance was issued in June 2006, which supersedes the Code issued in 2003.

Following consultation with Further Education and Higher Education sector groups, Colleges and Universities, it was agreed that the 2006 Combined Code will be effective for the 2007/08 financial statements. We have recommended in our action plan that the College takes steps in 2007/08 to ensure that it is compliant with the updated Code. *See action plan point 5.2.2.*

3.3.4 Unqualified audit opinion

We have reviewed the Corporate Governance Statement included within the annual accounts. Our audit opinion on this statement is covered by our auditors' report and is unqualified in this respect.

3.4 Statement on Systems of Internal Control

The framework of internal controls operating at Motherwell College is described within the Statement on Systems of Internal Control (SSIC) included within the Corporate Governance Statement in the annual accounts. The College has not identified any significant areas which require to be disclosed in the SSIC.

We are satisfied that the contents of the SSIC are not inconsistent with information gathered during the course of our normal audit work.

3.5 Risk management

The College's process for risk management is a crucial element of the system of internal control. As part of our audit, we have reviewed the College's risk management arrangements.

Motherwell College has an approved Risk Management Policy in place. The College has a risk register for both the general operation of the College and for the Ravenscraig relocation project. The Senior Management Team discuss all risks on a monthly basis. The Audit Committee will discuss all risks quarterly and the Board of Management will consider high risk items quarterly. This discussion of high level risks now appears as a standard agenda item.

The current general operational risk register contains those risks which could potentially result in the College failing to meet its objectives as outlined in the College's strategic plan.

The relocation risk register focuses specifically on the risks that the College faces in its future plans to move to a new purpose build campus at Ravenscraig.

We have concluded that the College has effective risk management systems in place which are clearly embedded in the College's management and governance framework. As such, Motherwell College's risk management arrangements are as strong as we have seen in the sector.

3.6 Internal audit

Internal audit is a key component of the College's corporate governance arrangements. The College's internal audit service is provided by Deloitte & Touche LLP.

As required by the Code of Audit Practice, we undertook a review of the College's arrangements to ensure that the work of Internal Audit is sufficient in quality and volume and performed in accordance with the Code of Audit Practice. The review concluded that the Internal Audit service provided to the College was in compliance with the Code of Audit Practice.

3.6.1 Reliance on Internal Audit

To avoid duplication of effort and ensure an efficient audit process, we planned our audit work to place reliance wherever possible on the work of Internal Audit. We can confirm that the internal audit service has completed their work plan for the year.

During 2006/07 we have reviewed the following Internal Audit reports:

- Capital asset management
- Governance
- Payroll
- Procurement
- Treasury Management

We considered the results from these reports on our own risk assessments. We are grateful to Deloitte & Touche LLP for their assistance during the course of our audit work.

3.7 Prevention and detection of fraud and irregularity

We are required to consider the arrangements made by management for the prevention and detection of fraud and irregularity. Fraud is defined as deception made for personal gain and irregularity is defined as transactions which do not comply with Scottish Ministers guidance. We consider the arrangements made by management in the following ways:

- We examine the financial instructions issued by the College to ensure that they deal adequately with fraud and irregularities and provide a framework for exercising strong internal control,
- Our systems based audit is planned so as to provide a reasonable expectation of detecting misstatements in the annual accounts resulting from fraud or irregularity,
- We focus on specific areas of high risk for potential fraud and irregularity and review the arrangements in place in these areas,
- We review the Technical Bulletins produced by Audit Scotland with regard to fraud reports and ensure that the College has arrangements in place to prevent similar frauds occurring,
- We review the extent and adequacy of the Internal Audit function within the College.

We are pleased to report that we identified no issues of concern in relation to the arrangements for the prevention and detection of fraud or with regard to the legality of transactions.

3.8 Standards of conduct, integrity and openness

We are required to consider the arrangements made by management in relation to standards of conduct and prevention and detection of corruption.

Propriety requires that public business is conducted with fairness and integrity. This includes avoiding personal gain from public business, being even-handed in the appointment of staff, letting contracts based on open competition and avoiding waste and extravagance. Guidance on standards of conduct, accountability and openness has been issued by the Scottish Government (formerly Scottish Executive).

Our work in this area included a review of the arrangements for adopting and reviewing standing orders, financial instructions, registers' of interest and schemes of delegation and complying with national and local Codes of Conduct. We also considered controls over ordering and procurement and disposal of assets.

We are pleased to report that our audit identified no issues of concern in relation to standards of conduct, integrity and openness.

4 Finance

4.1 Introduction

We are required to audit the financial statements in accordance with International Standards on Auditing and to 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;
- whether they have been prepared in accordance with relevant legislation and applicable accounting standards;
- the regularity of the expenditure and receipts.

We are also required to review Motherwell College's financial management arrangements.

4.2 Accounts Direction

The College was required, in preparing its annual accounts, to comply with directions given by the Scottish Funding Council (SFC). We are pleased to confirm that the College's annual accounts for 2006/07 comply fully with the Accounts Direction issued by SFC.

4.3 Statement of Recommended Practice (SORP)

The purpose of the SORP on Accounting for Further and Higher Education is to ensure that the financial statements of institutions are prepared on a comparable and consistent basis.

The SORP takes account of best accounting practice, the requirements of the Funding Councils, the accounting provisions of the Companies Act and other relevant legislation.

We are pleased to report that the 2006/07 annual accounts of the College comply with the SORP in all material respects.

4.4 Annual accounts and audit timetable

The deadline for the submission to SFC of FE College audited annual accounts is 31 December. The accounts will be approved by the Board of Management on 6 December 2007 and will be submitted to SFC and the Auditor General prior to the 31 December deadline.

We received draft accounts and supporting papers on 17 September 2007 as agreed. Generally, the audit process ran smoothly, although a short delay was experienced in relation to the audit of accruals and deferred income due to presentational issues with regards to the back-up documentation required to satisfy our audit purposes.

We are grateful to the Director of Finance and Physical Resources, the Financial Controller and Finance staff for their assistance and support during the course of the audit.

4.5 Auditors' report – unqualified opinion

We are required to give an opinion as to whether the accounts present a true and fair view of the financial position of the College at 31 July 2007 and of its income and expenditure for the financial year.

We are also required to include a regularity assertion in our audit report stating that, in all material respects, expenditure and income were incurred or applied for their intended purposes and in accordance with guidance issued by the Scottish Ministers and the financial memorandum with SFC.

We have issued an unqualified audit opinion on the truth and fairness of the accounts and on the regularity of transactions.

4.6 Review of Accounting Systems

One of the objectives of our audit was to review the accounting systems and internal controls operating at the College to ensure they formed an adequate basis for the preparation of the financial statements.

We identified no control weaknesses during our audit of the accounting systems. In general, the College's systems of internal control appear to be adequate, well designed and operating effectively.

4.7 Financial Standing

Motherwell College has a responsibility to conduct its financial affairs in a proper manner. As part of our audit, we are required to consider the College's financial standing, including the arrangements in place for financial planning, budgetary control and financial reporting.

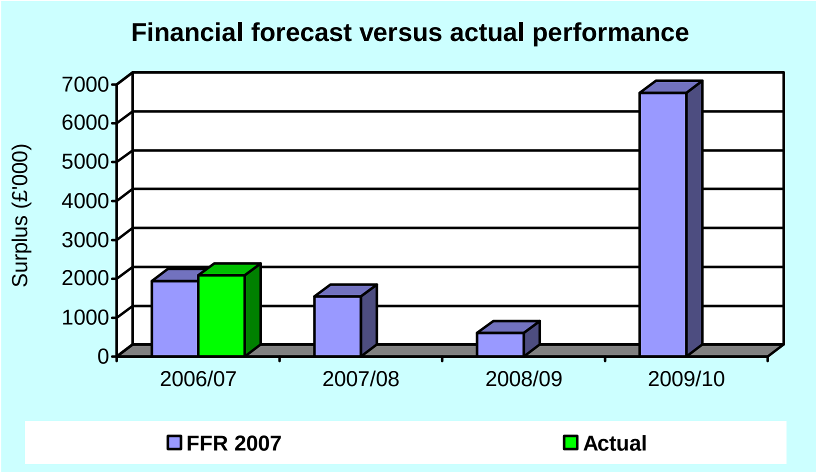
It is important that such arrangements are adequate in order to properly control the College's operations and use of resources.

4.7.1 Financial Management

Budgets are devised at the start of the year, approved by the College and updated during the year to take account of new information. Management accounts are distributed monthly to the members of the Finance Committee for review.

The College submits annual financial forecast returns (FFRs) to SFC detailing the expected results for the current year and the next three years. SFC uses the FFRs to assess the financial performance of individual Colleges and the sector as a whole.

The graph below compares the actual results from continuing operations prior to the release of the revaluation reserve for 2006/07 with the FFR forecasts and shows the latest projections contained within the 2007 FFR.



As shown above, the College is expecting to achieve surpluses over the next three years. The surplus in 2009/10 is unusually high, due to the predicted gain on sale of £6,252,000 which will arise following the disposal of the current College site. Subsequent to the preparation of the FFR, the accounting treatment for the disposal was agreed with Scott-Moncrieff which will result in this gain on sale being brought forward and reported within the 2008/09 financial statements.

4.7.2 Financial position

The College reported a surplus of £2,090,000 to 31 July 2007 (2005/06 - £1,093,000). The historical cost surplus was £2,310,000 after releasing £220,000 from the revaluation reserve in respect of depreciation on re-valued assets.

In total, the College has reserves and deferred capital grants of £23.003m. Of this, £6.080m is held within the revaluation reserve.

The Income and Expenditure account reserve as at 31 July 2007 totals £6,516,000, a strong position for the College as the new build programme commences.

As at 31 July 2007 the College had incurred £8,402,000 of capital expenditure in relation to the Ravenscraig project, which has been disclosed in the financial statements as "Assets in the course of construction". The College has deferred the capital grants received from the Scottish Funding Council in respect of this expenditure.

4.7.3 Conclusion

Based on the work we have carried out, Motherwell College appears to have effective financial management arrangements in place.

4.8 New Build Programme

The construction of the new College is only part of a larger development plan to regenerate a site in excess of 100 acres. In relation to Motherwell College, this project has a budgeted cost of £69.8 million. The financing for the project is closely monitored, and will be financed as follows:-

Scottish Funding Council	£42.4M
Land receipts	£12.8m
College resources	£14.6M
Total	**£69.8M**

Land and buildings in respect of the current College site have been sold to a housing developer. The missives were signed in November 2006 but, in accordance with the legal documentation, title for the existing land and buildings will not pass until October 2008.

Due to the size and length of this project, the issues of disposal of the existing site, the acquisition and construction of the new site and the application of the Lennartz principles to the VAT incurred will remain key audit risks in respect of the audit of the 2007/08 financial statements.

4.9 FRS 17 – Retirement Benefits

The College has previously accounted for the Strathclyde Pension Fund (a defined benefit pension scheme) as if it were a defined contribution pension scheme. This treatment is permitted by Financial Reporting Standard 17 – Retirement Benefits (FRS 17) under certain circumstances. As part of our audit, we considered whether the continued accounting for the scheme in this manner is appropriate and consistent with guidance issued for the College sector and with the practice adopted by other Colleges within the Strathclyde area.

Our conclusion is that it is reasonable for the College to account for the Strathclyde Pension Fund, as presently constituted, as a defined contribution scheme in 2006/07. However this position will require to be reviewed on an annual basis to take account of changes to the scheme, particularly the introduction of separate employer contribution rates planned for 2008. Therefore this will again be an issue which will require to be monitored and considered in respect of the 2007/08 financial statements.

4.10 International Financial Reporting Standards (IFRS)

The Chancellor announced in his 2007 budget speech the decision to adopt IFRS for public sector accounting by 2008/09. Whilst this does not have an immediate impact on the Motherwell College accounts, the College should be aware of this issue as it could have significant implications in the future.

4.11 FE/FE SORP 2007

The HE/FE SORP Board issued a draft revised SORP for comment in January 2007 (the "2007 SORP"), on which the consultation period concluded on the 13th April 2007. The 2007 SORP does not contain any significant changes, but does include enhanced guidance and explanations on the application of UK GAAP to educational institutions' financial statements. The 2007 SORP will be mandatory for the 2007/08 reporting year.

5 Action Plan

Our annual report action plan details the control weaknesses and opportunities for improvement that we have identified during 2006/07.

We have made no priority one recommendations in 2006/07.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist.

5.1 Priority rating

To assist the College in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated. The rating structure is summarised as follows:

Priority 1	High risk, material observations requiring immediate action.
Priority 2	Medium risk, significant observations requiring reasonably urgent action.
Priority 3	Low risk, minor observations which require action to improve the efficiency, effectiveness on economy of operations or which otherwise require to be brought to the attention of senior management.

5.2 Issues from our 2006/07 Audit

Title	Issue Identified	Risk and Recommendation	Management Comments
5.2.1 Board of management evaluation *Report ref 3.3*	The Board of Management does not perform an annual self evaluation exercise.	To further strengthen the self evaluation process, we recommend that the Board of Management complete a formal, annual evaluation exercise. This process should be formally documented. **Priority 3**	The process of Board of Management evaluation has already commenced ***Responsible Individual:*** Secretary to the Board ***Implementation Date:*** December 2007
5.2.2 Combined Code 2006 *Report ref 3.3*	A revised Combined Code on Corporate Governance was issued in June 2006, which supersedes the Code issued in 2003.	The College should review its current corporate governance arrangements against the requirements of the 2006 Combined Code. The College should take action to address any areas of non-compliance to ensure that it is compliant for its 2007/08 financial statements. **Priority 2**	Agreed ***Responsible Officer:*** Director of Finance and Physical Resources ***Implementation Date:*** December 2007

Title	Issue Identified	Risk and Recommendation	Management Comments
5.2.3 Ravenscraig Project Cut Off *Report ref 4.8*	An issue was noted in relation to the cut off of expenditure and the accrual of capital grant for this project. The capital grant claim is completed for expenditure incurred up to the 25th of each month. Therefore there was a period between the 25th and 31st July where expenditure had been incurred, but no accrual had been recorded within the financial statements. Similarly, the corresponding capital grant due in respect of this outlay had not been accrued within the financial statements. Post year-end, the project manager now prepares a valuation of the work performed on the Ravenscraig site to the 19th of each month.	As the construction on the Ravenscraig site progresses, there is a risk that the expenditure incurred in the period between performance of the valuation and the year-end may be in the region of £2m. We would recommend that procedures are introduced to ensure that this cut off issue is addressed in advance of the 31 July 2008 year-end. Consideration will also have to be given to the level of capital funding which may require to be accrued in respect of this expenditure. **Priority 3**	Agreed that a process will be introduced to address this issue as part of the year-end procedures. ***Responsible Individual:*** Financial Controller ***Implementation Date:*** July 2008
5.2.4 Employee Numbers *Report ref - N/A*	It was noted during audit fieldwork that the number of employees per the payroll summaries did not agree to the numbers per the staffing lists, which are in turn used to prepare the employee numbers disclosure contained within the financial statements.	There is a risk that the disclosure in the financial statements or within other regulatory submissions may be incorrect. Employee numbers per the payroll summaries should be reconciled to the staffing lists prior to calculation of the full time equivalent figures. Following identification of this issue, it was addressed immediately and the disclosure contained within the financial statements is now accurate. **Priority 3**	The Financial Controller will liaise with the Human Resources Manager to ensure agreed reconciliations take place ***Responsible Individual:*** Financial Controller ***Implementation Date:*** July 2008

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