

Central College of Commerce Report to the Board and the Auditor General for Scotland

Year ended 31 July 2007



BDO Stoy Hayward

Contents

Contents	1
1 Executive Summary	2
Introduction.....	2
Scope of Work.....	2
Corporate Governance Arrangements	2
Compliance with Scottish Funding Council ('SFC') Accounts Direction	3
Conclusion.....	3
Acknowledgement	3
Financial performance	3
2 Introduction	4
Purpose of Report	4
Audit Bodies	4
College Responsibilities.....	4
Auditors' Responsibilities and Approach	5
3 Scope of Work	6
Financial Memorandum	6
Accounts Direction.....	6
Guidance on Audit	6
Statement of Recommended Practice (SORP)	6

4 Audit Findings	8
Preparation of Financial Statements	8
Audit Opinion.....	8
Financial Performance.....	8
Performance Indicators.....	8
Grant in Aid Funding	9
Corporate Governance Framework and Statement	9
System of Internal Control	9
Prevention and detection of Fraud and Corruption.....	10
Review of Internal Audit	10
Misstatements	10
Accounting and Internal Control System Weaknesses.....	10
Qualitative Aspect of the College's Accounting Practice and Financial Reporting.....	10
FRS 17 – Retirement Benefits	10
Early retirement provision	11
Review of Severance arrangements of former Principal	11
Glasgow City Centre Colleges Project.....	11
Further Education Childcare Funds	11
5 Internal control systems weakness	12
Findings from 2007 audit process.....	12
Recommendations made during 2006 audit.....	12
6 Other Matters.....	13

1 Executive Summary

Introduction

- The purpose of this report is to highlight and explain key issues arising from our audit of the financial statements of Central College of Commerce ('the College') for the year ended 31st July 2007.
- The matters raised in this report, are only those which have come to our attention arising from or relevant to our work that we believe need to be brought to your attention. Our audit work is designed to enable us to form an audit opinion on the financial statements of the College and it should not be relied upon to disclose all irregularities that may exist nor to disclose errors that are not material in relation to the financial statements.
- This report has been prepared solely for the use by the Board of Management of Central College of Commerce and the Auditor General for Scotland.
- We have completed our audit work in respect of the financial statements for the year ended 31 July 2007 and will be issuing an unqualified audit opinion for the year.

Scope of Work

- The accounting rules and regulations applied to Further Education Colleges are specifically laid out in various documents as discussed in section 3 of this report. We can confirm that the College is in compliance with the regulations and disclosures required to be made in the financial statements in respect of these documents.

Corporate Governance Arrangements

- The corporate governance statement within the College's financial statements states that the College has been fully compliant with guidance on corporate governance for the year ended 31 July 2007. We identified no issues of concern in relation to fraud and irregularity nor did we identify any major errors or weaknesses during our audit. In general the College's systems of internal control appear to be adequate.

Compliance with Scottish Funding Council ('SFC') Accounts Direction

- We can confirm in preparing the financial statements the College has complied with the Accounts Direction for Scotland's colleges and universities issued under circular SFC/30/2007.

Conclusion

- The audit of Central College of Commerce was performed in accordance with relevant legal and regulatory requirements and with International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland. This report has been issued to College management and will be considered by the Audit Committee.

Acknowledgement

- The 2006/2007 audit process brought us into contact with a number of staff within the College. We wish to place on record our appreciation of the co-operation extended to us by those personnel.

Financial performance

Profitability	The college made a surplus of £75,000 and a historical cost surplus of £165,000 for the year
Cashflow	There was a net cash inflow of £906,000 during the year.
Balance Sheet	The financial statements show net assets of £9,783,000. The balance on the revaluation reserve carried forward is a surplus of £5,392,000.
Forecasts	The Board of Management are forecasting an operating surplus of £74,000 in the forthcoming year.

2 Introduction

Purpose of Report

- This report has been prepared in connection with our audit of the financial statements of the College for the year ended 31 July 2007. This report summarises the principal matters that have come to our attention during the course of the audit.
- The contents of the report should not be taken as reflecting the view of BDO Stoy Hayward LLP except where explicitly stated as being so. To a certain extent, the content of this report comprises general information which has been provided by, or is based on discussions with, the management of the College. Except to the extent necessary for the purposes of the audit, this information has not been independently verified.
- One of the purposes of this report is to record features of the year's activities, the way they are treated in the financial statements and the comments thereon provided to audit staff by the College's staff.

Audit Bodies

- The Auditor General, a royal appointment on the nomination of the Scottish Parliament, plays a key role in holding the Scottish public spending bodies to account for the proper, efficient and effective use of public money.
- Audit Scotland is an independent statutory body which was set up in April 2000 to provide assistance and support to the Accounts Commission and to the Auditor General for Scotland in the exercise of their respective functions. The Auditor General is responsible for securing the audit of the Scottish Executive, Further Education Colleges and other public bodies.

- BDO Stoy Hayward LLP was appointed by Audit Scotland as external auditor to Central College of Commerce for 5 years covering the financial years 2006/07 to 2010/11. This report summarises our audit work for 2006/07 and details how the requirements of the Statement of Responsibilities and the Code of Audit Practice have been met by the College and by BDO Stoy Hayward LLP

College Responsibilities

- The College is publicly accountable for the conduct of business and the stewardship of funds under its control. The College's Board of Management is therefore responsible for:
 - establishing adequate corporate governance procedures;
 - ensuring funds from the SFC are used only for the purposes for which they have been given and in accordance with the Financial Memorandum with the SFC and any other conditions which the SFC may from time to time prescribe;
 - ensuring that there are appropriate financial and management controls in place to safeguard public funds and funds from other sources;
 - safeguarding the assets of the College and taking reasonable steps to prevent and detect fraud and other irregularities;
 - securing the economical, efficient and effective management of the College's resources and expenditure;
 - maintaining proper accounting records and preparing financial statements which give a true and fair view of the financial position of the College at the year-end and its income and expenditure for the year.

Auditors' Responsibilities and Approach

- We are required to report to the Board of Management of the College and to the Auditor General for Scotland on the financial statements of the College. Our responsibilities are to:
 - provide an opinion, to the extent required by the relevant authorities, on the financial statements of the College and the regularity of transactions in accordance with standards and guidance issued by the Auditing Practices Board.
 - review and report on the requirements of Audit Scotland's Code of Audit Practice (March 2007), regarding the College's corporate governance arrangements relating to:
 - the College's review of its systems of internal control
 - the prevention and detection of fraud and irregularity
 - standards of conduct, and prevention and detection of corruption
 - its financial position.
 - obtain an understanding of the accounting and internal control systems in place in the College sufficient to allow the audit to be planned and an effective audit approach developed.
- Our audit work is designed to enable us to form an audit opinion on the financial statements of the College and it should not be relied upon to disclose all irregularities that may exist nor to disclose errors that are not material in relation to the financial statements.

3 Scope of Work

- We took reasonable steps to plan and carry out the audit to ensure that the above responsibilities were met and that we complied with the requirements of Audit Scotland's Code of Audit Practice.
- In essence the scope of our work is similar to that applied to a limited company audit, however, the accounting rules and regulations applying to Further Education Colleges are specifically laid down in various documents as detailed below.

Financial Memorandum

- This memorandum sets out the terms and conditions under which the Scottish Funding Council will make payments to the Board of Management of Colleges of Further Education out of funds made available by the First Minister of Scotland. We can confirm the College fully complies with the terms and conditions of the memorandum.

Accounts Direction

- In preparing its annual accounts the College is required to comply with the directions of the Scottish Funding Council (SFC). The Accounts Direction is designed to ensure that disclosures in the financial statements of all colleges follow best practice. We can confirm the College's financial statements comply with the Accounts Direction.

Guidance on Audit

- Audit Scotland's Code of Audit Practice (March 2007) sets down Audit Scotland's requirements for both internal and external audits. In carrying out our audit work we are also required to comply with International Standards on Auditing (UK and Ireland) and to take cognisance of any relevant Practice Notes and other guidance and advice issued by the Auditing Practices Board. We also comply with

relevant ethical standards and guidance issued or adopted by the relevant professional accountancy bodies and any supplementary guidance issued by Audit Scotland.

Statement of Recommended Practice (SORP)

- The HE/FE SORP board issued the revised SORP effective from 1 August 2003. The SORP combines the requirements of institutions of Further and Higher Education to ensure financial statements are prepared on a consistent basis. We can confirm that the financial statements of the College comply with the SORP.
- A revised SORP: Accounting for Further and Higher Education was published in July 2007 which will be effective for 2007/08. This reflects changes in accounting standards and in best accounting practice since the 2003 SORP was published. The key changes in the SORP are as follows:
 - The disclosure requirements of *FRS 25 Financial Instruments: disclosure and presentation* & *FRS 29 Financial Instruments : disclosures* apply on adoption of *FRS 26 Financial Instruments : measurement*.
 - *FRS 26 Financial Instruments : measurement* will apply to colleges qualifying as listed entities (including those with listed debt in issue) or those institutions adopting fair value accounting.
 - For colleges which do not have listed debt and are not applying fair value accounting in accordance with the Companies Act or *FRS 26*, the relevant parts of *FRS 4: Capital Instruments* remain applicable.
 - The disclosure requirements in respect of *FRS 17 Retirement benefits* has been amended. It now states that the Local Government Pension Scheme (LGPS) is a multi employer scheme where it is normally possible for

individual employers as admitted bodies to identify their share of assets and liabilities. The SORP therefore considers these schemes should be accounted for as defined benefit schemes (provided that the assets and liabilities relating to colleges can be measured on a reliable and consistent basis) and that the exemption which allows accounting on a defined contribution basis is unlikely to apply. However, in the unlikely case that the exemption does apply, the SORP requires that, in addition to the defined contribution disclosures required by FRS 17, colleges should disclose:

- the reason why sufficient information is not available to account for the scheme as a defined benefit scheme;
- the fact that the scheme is a defined benefit scheme but the college is unable to identify its share of the underlying assets and liabilities;
- any available information about the existence of the surplus or deficit in the scheme and the implications of that surplus or deficit for the college.

This may apply to the SPF scheme in 2007/08.

4 Audit Findings

Preparation of Financial Statements

- The financial statements and the required working papers were ready for audit on 3 September 2007, in line with the agreed timetable.

Audit Opinion

- We are satisfied that the financial statements of the College present a true and fair view of its financial position as at 31 July 2007. Following approval of the financial statements by the Board of Management on 12 December 2007, our audit report expresses unqualified opinions on (i) the financial statements of the College for the year ended 31 July 2007 and (ii) regularity.

Financial Performance

Surplus for Period

- The College made an historic cost surplus of £165,000 in respect of the year ended 31 July 2007 compared to a surplus of £146,000 for the year ended 31 July 2006.
- Net assets at 31 July 2007 are £9,783,000 (31 July 2006: £8,824,000)
- The balance on the income and expenditure account carried forward as at 31 July 2007 is a surplus of £1,063,000 (31 July 2006: £898,000).
- The balance on revaluation reserve carried forward as at 31 July 2007 is a surplus of £5,392,000 (31 July 2006: surplus £5,482,000).

Cash Flow

- During 2006/2007 the College experienced a net inflow of cash of £906,000 (2005/06: outflow of £695,000).

Going Concern Basis

- In preparing the accounts on a going concern basis the Board of Management is satisfied that SFC will provide sufficient funding to enable the College to operate for at least twelve months from 12 December 2007.

Performance Indicators

- The Scottish Further Education Funding Council's ('SFEFC') financial security campaign was announced in December 2002, its principal objective being that all colleges would report underlying operating surpluses by the end of 2005-06. Financial security is defined as the ability, on a continuing basis, 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.
- Under the terms of the financial memorandum between SFC and the College, it is the responsibility of the governing body "to ensure that the institution strives to achieve best value from its use of public funds from all sources". It is intended that the financial performance indicators used by the Funding Council, when set alongside other performance data, will support the college in seeking best value.
- The table below has been produced from the data published by the Funding Council through circular SFC/33/2007 in respect of the Financial Statements as at 31 July 2006. The formulae have then been applied to the 2006/07 Financial Statements.

- As can be seen Central College of Commerce performs relatively favourably in comparison to other Colleges within their Group (Income base > £10m-£15m) and the Sector.

	<u>Central College Factor 2006-07</u>	<u>Central College Factor 2005- 06</u>	<u>Group Average Factor 2005-06</u>	<u>Sector Average Factor 2005-06</u>
Underlying operating surplus/ (deficit) % of total income	0.6%	0.4%	1.6%	2.2%
Operating surplus/ (deficit) % of total income	0.6%	0.4%	1.2%	0.8%
Designated plus I&E reserves % of total income	11.1%	9.2%	4.0%	10.5%
Historical cost surplus/ (deficit) % of total income	1.4%	1.1%	2.5%	1.9%
Current assets: Current liabilities	2.0	2.0	1.3	1.3
Interest Cover	N/A	N/A	4.5	3.0

Grant in Aid Funding

- The College's WSUMS target for 2006/07 was 47,614 and the College has over delivered in relation to the year. As a result the College will not be liable to refund any amounts received in 2007/08.

Corporate Governance Framework and Statement

- The Board of Management has five formally constituted committees which have specific terms of reference and act with delegated authority from the Board.
- We reviewed the College's corporate governance arrangements. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of the organisation. The college has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.
- From our review of Corporate Governance arrangements within the College we do not believe the Corporate Governance statement to be misleading or inconsistent with other information made available to us during the audit process.

System of Internal Control

- 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 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.
- 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.

- Our review of the statement concluded that it complies with guidance and is not inconsistent with other information we are aware of from our audit.

Prevention and detection of Fraud and Corruption

- The College's arrangements for preventing and detecting fraud and corruption were assessed during the audit. This assessment showed the arrangements to be operating satisfactorily. No frauds were identified by the College in 2006/07.

Review of Internal Audit

- Internal audit is a key element of the internal control system set up by management. A strong internal audit function is necessary to ensure the continuing effectiveness of the internal control systems established. The College therefore, needs to have in place a properly resourced internal audit service of good quality.
- Internal audit services are provided by Deloitte. An assessment was made of the adequacy of the internal audit input and it was concluded that we as external auditors were able to place reliance on the work of internal audit. Accordingly a certain amount of reliance was placed on the work of internal audit in the following areas during 2006/2007.
 - Governance & risk management arrangements
 - IT Controls
 - Financial Controls

In August 2007, Deloitte issued the internal audit report for the year ended 31 July 2007. This concluded that, the College has an adequate framework of control, based on the systems examined.

Misstatements

- There were no adjusted or unadjusted misstatement of significance uncovered in the course of our audit work.

Accounting and Internal Control System Weaknesses

- One internal control weakness was identified during the course of our audit. This is listed in section 5 along with any weaknesses noted previously by external audit.

Qualitative Aspect of the College's Accounting Practice and Financial Reporting

- Our overall assessment, based on our work undertaken, is that the financial procedures of the College are adequate to enable annual financial statements to be produced in the prescribed form.

FRS 17 – Retirement Benefits

- This standard was published in November 2000 introducing significant changes to the way in which colleges should account for defined benefit pension schemes. Full implementation of FRS17 – 'Retirement Benefits' was mandatory for 2005/06 year ends. The College participates in the Scottish Teachers Superannuation Scheme ('STSS') and the Strathclyde Pension Fund ('SPF') which are defined benefit pension schemes. All colleges treat the STSS scheme as a defined contribution scheme as there is general agreement that they are unable to identify their share of the scheme's assets and liabilities. The SFC's *Detailed notes for guidance on the completion of 2006-07 financial statements* sets out the treatment of the SPF scheme suggesting it should be treated as a defined contribution scheme. This is discussed further in the paragraph below. As auditors we concur with the treatment of the two schemes for the year ended 31 July 2007.
- In relation to the SPF scheme it is envisaged that separate employer rates will be introduced by 2008 at the earliest. Assets are currently

apportioned based on the liability profile though employer assets have been tracked for each employer since 2002. Indications are that the SPF are moving in the same direction as the Lothian Pension Fund and hence towards full defined benefit disclosures. However consensus at a meeting of college representatives, Audit Scotland, SPF Hymans Robertson and the SFC in 2006 was that the characteristics of the scheme, as presently constituted, enable college representatives to consider using the reduced disclosure requirements available for defined benefit schemes, within the criteria of FRS17.

Early retirement provision

- Included in the balance sheet is a provision for the cost of providing for enhanced pensions. The College recalculated this early retirement provision using the actuarial tables, guidance issued by SFC and an appropriate interest rate.

Review of Severance arrangements of former Principal

- Deloitte in their capacity as internal auditors undertook a review of the process by which the early retirement and severance package of the, now former, Principal of the College was determined. This review was undertaken to ensure compliance with the requirements of the *Guidance on Severance Arrangements to Senior Staff in Scottish Further Education Colleges* as determined by the SFC, and the College's own internal policy *College Policy statement on Severance Arrangements for Senior Staff*. In order to confirm compliance internal audit reviewed the procedures adopted and relevant supporting documentation for the determination of the package against their understanding of key clauses in the guidance. From their review there was evidence to confirm that the College has complied with the majority of the mandatory and general requirements of the SFC guidance in principle. No matters or recommendations were brought to managements attention.

Glasgow City Centre Colleges Project

- In conjunction with three other colleges in Glasgow the College is currently working on an estates strategy. The business case for this strategy is still in development however any valuations undertaken on the College's estates could indicate the need for impairment in the current carrying values of the College's land and buildings. We discussed this ongoing project with college management and the implication of impairment of the current carrying values having regard to the expected duration of future use. Discussions with regards to this project remain ongoing and there is no indication of impairment at this stage.

Further Education Childcare Funds

- The College has treated FE Childcare funds in accordance with paragraph 67 of the SORP which states that 'Where an institution disburses funds it has received as paying agent on behalf of a Funding Council or other body, and has no beneficial interest in the funds, the receipt and subsequent disbursement of the funds should be excluded from the income and expenditure account of the institution where the institution does not have control over the future economic benefits.' What constitutes an agency arrangement depends on the fund and its characteristics. FE Childcare funds are not deemed to meet the definition of an agency agreement in the SFC's *Detailed notes for guidance on the completion of 2006-07 financial statements* and should therefore be included in the income and expenditure account as colleges have more discretion in the manner in which these funds are disbursed. The sum of money received and disbursed by the College is not material in the context of the income and expenditure figures, or the surplus, reported and we therefore have not recommended any adjustment.

5 Internal control systems weakness

Findings from 2007 audit process

Adequacy of Risk Strategy Document

Findings

- We reviewed the College risk strategy document as part of our audit process to determine if it adequately reflected all potential risks which may effect the College. We felt that while the key potential risks were addressed the register does not adequately detail the causes, consequences and controls the College has in place to mitigate the risks identified.

Recommendation

- We recommend the College review the risk register as it currently stands and give consideration to detailing causes of the risks identified, the consequences if the risk occurred and the controls in place, within the College, to mitigate the risk occurring so that there is a clear detailed strategy in place.

Management Response

- This is a good recommendation and will improve our overall understanding of risks. This recommendation will be implemented during our detailed risk review currently planned for March 2008

Recommendations made during 2006 audit

- No recommendations were made by the external auditors in 2006.

6 Other Matters

- 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”).

All charities, including Scotland's colleges, are required to demonstrate to the Office of the Scottish Charity Regulator (OSCR) that they meet the new charity test, set out in the Act. In a pilot, on John Wheatley College, OSCR ruled that the college did not meet the charity test because its constitution permits Scottish Ministers to direct or otherwise control its activities. This ruling means that at present none of Scotland's colleges would currently pass the charity test. The Scottish Government is reviewing the situation and in a statement issued on 30 October 2007, pledged government support to ensure that colleges retain their charitable status.

BDO Stoy Hayward LLP

19 December 2007