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

Year ended 31 July 2008

BDO Stoy Hayward

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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 ('the College') for the year ended 31st July 2008.
- 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 and the Auditor General for Scotland.
- We have completed our audit work in respect of the financial statements for the year ended 31 July 2008 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 2008. 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/35/2008.

Conclusion

- The audit of Central College 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 2007/08 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.

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 2008. 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 for 5 years covering the financial years 2006/07 to 2010/11. This report summarises our audit work for 2007/08 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)

- A revised SORP: Accounting for Further and Higher Education was published in July 2007 which was effective for all colleges in 2007/08. The key change in the SORP which is relevant to the college is as follows:

  - The requirement for an operating and financial review which encompasses an overview of the college's finances and operations and takes account of good practice.

- We can confirm that the financial statements of the College, and in particular the operating and financial review, are in general in compliance with the requirements of the 2007 SORP. The following areas, as laid out in the model financial statements, could be further enhanced, in terms of the level of content, by the College during 2008/09:

  - Performance indicators;

  - Principal risks and uncertainties

- In addition to the key change affecting the college the following areas are subject to new emphasis within the revised SORP which affect the college:

  - Component accounting. This is an area which should be borne in mind by college management in the future in light of the refectory and foyer redevelopment. College management should ensure future projects are split into component parts based on useful economic life and depreciated accordingly.

- 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.

The above applies to the SPF scheme in 2007/08.

The college considers that it is unable to identify its own share of the underlying assets and liabilities within the SPF scheme on a reasonable and consistent basis. No definitive guidance has been issued by the SFC and therefore the College continues to account for contributions to this scheme as if it is a defined contribution scheme.

4 Audit Findings

Preparation of Financial Statements

- The financial statements and the required working papers were ready for audit on 18 September 2008, 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 2008. Following approval of the financial statements by the Board of Management on 10 December 2008 our audit report expresses unqualified opinions on (i) the financial statements of the College for the year ended 31 July 2008 and (ii) regularity.

Financial Commentary

- This section summaries the main financial features and key movements from the prior year.

Income and expenditure account

- The College made a surplus of £79,000, 0.6% of total income (2006/07: £75,000 and 0.6%) in respect of the year ended 31 July 2008. The sector average for 2006/07 was 1.6%.

Income

- Total income increased by £261,000 (2.2%). The increase is primarily due to an increase £463,000 in Scottish Funding Council Grants, offset by a reduction in Tuition Fees and Education Contracts of £37,000 and Other Income of £195,000.

- The table below summarises the main sources of income for 2007/08 and 2006/07.

	2007/08	**2006/07**	**2007/08**	**2006/07**
	£'000	**£'000**	**%**	**%**
Scottish Funding Council Grants	8,740	8,277	71%	69%
Tuition Fees and Education Contracts	2,699	2,736	22%	23%
Other Income	706	901	6%	7%
Investment Income	199	169	1%	1%
Total Income	**12,344**	**12,083**	**100%**	**100%**

- A significant proportion of income is received from the Scottish Funding Council and the various sources of income remain relatively consistent with 2006/07. The college is not as dependant on SFC Grants as other College's delivering over 45,000 WSUMs from review of the 2006/07 Scottish Funding Council performance indicators. Total Funding Council Grant income is normally in the region of 75%, based on the 2006/07 statistics for colleges in this category.

Expenditure

- Total expenditure increased by £257,000 (2.1%) in comparison to 2006/07. This is consistent with the increase in income and therefore the reported surplus. The increase in costs is, in the main, due to an increase in staff costs with the most significant movements detailed below:
  - An increase in staff costs of £369,000 due to salary increases; and
  - A decrease in other operating expenses of £124,000 as a result of estates expenditure being deferred to 2008/09 once the income is received.
- The table below summarises the main sources of expenditure for 2007/08 and 2006/07.

	2007/08	**2006/07**	**2007/08**	**2006/07**
	£'000	**£'000**	**%**	**%**
Staff costs	9,033	8,664	74%	72%
Other Operating Expenditure	2,682	2,806	22%	23%
Depreciation	469	464	4%	4%
Interest payable	81	74	<1%	1%
Total Expenditure	**12,265**	**12,008**	**100%**	**100%**

- Proportionately expenditure remains consistent with 2006/07.

Balance sheet

- Net assets at 31 July 2008 are £9,632,000 (31 July 2007: £9,783,000)
- The balance on the income and expenditure account carried forward as at 31 July 2008 is a surplus of £1,232,000 (31 July 2007: £1,063,000).
- The balance on revaluation reserve carried forward as at 31 July 2008 is a surplus of £5,302,000 (31 July 2007: surplus £5,392,000).

Cash Flow

- During 2007/2008 the College experienced a net inflow of cash of £273,000 (2006/07: inflow of £906,000).

Financial Forecasting

- The 2007-08 financial plan forecast a surplus of £82k. The timing of receipts in relation to SFC grant income resulted in monies being received later than originally budgeted. The effect being expenditure relating to this income was delayed until the money was received in 2008/09.

Financial Forecasting

	2007/08
	£'000
2007-08 forecast outturn per budget	82
Reduction in SFC grant income	-325
Increase in other income	39
Reduction in exceptional restructuring costs	80
Reduction in other operating expenditure	203
2007/08 actual outturn at 31 July 2008	**79**

- The reduction in SFC income is not controllable by the College and accordingly the College has deferred expenditure associated with these costs in relation to restructuring and other operating expenses until the income is available.
- The following table summarises the forecast income, expenditure and cash balances for the College for 2008/09.

	£'000
Income	12,237
Expenditure	12,213
Forecast surplus for the year ending 31 July 2009	24
Cash balance at 31 July 2008	2,858
Forecast movement in cash during 2008/09	-763
Resulting cash balance at 31 July 2009	**2,095**

- Both College income and expenditure are expected to decrease in 2008/09. The reduction in income will be due to the sector wide cut in ESF funding slightly offset by an increase in grant-in-aid. College expenditure will have to be monitored accordingly, in particular staff costs, in order to remain in surplus.
- The reduction in cash forecast for 2008/09 arises as a result of a deferral of capital grants received in 2007/08 which will be spent in 2008/09.

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 10 December 2008.

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/44/2008 in respect of the Financial Statements as at 31 July 2007. The formulae have then been applied to the 2007/08 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.

	Central College Factor 2007-08	**Central College Factor 2006-07**	**Group Average Factor 2006-07**	**Sector Average Factor 2006-07**
Underlying operating surplus/ (deficit) % of total income	0.6%	0.6%	2.6%	3.3%
Operating surplus/ (deficit) % of total income	0.6%	0.6%	2.0%	1.6%
Designated plus I&E reserves % of total income	12.2%	11.1%	6.1%	17.0%
Historical cost surplus/ (deficit) % of total income	1.4%	1.4%	3.5%	4.0%
Current assets: Current liabilities	1.7	2.0	1.7	1.4
Interest Cover	N/A	N/A	6.5	5.0

Grant in Aid Funding

- The College's WSUMS target for 2007/08 was 48,185 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 2008/09.

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 2007/08.

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 2007/2008.

    - Payroll and Human Resources
    - Procurement
    - Estates Management

In November 2008, Deloitte issued the internal audit report for the year ended 31 July 2008. 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

- No internal control weaknesses were identified during the course of our audit. In the prior year one internal control weakness was identified and implementation of this has now taken place. This is discussed in section 5.

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 from 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 debate regarding the appropriate accounting treatment of the Strathclyde Pension Fund has not been resolved to a definitive position. Following a further review the Scottish Funding Council ('SFC') issued its findings and conclusions in a letter dated 17 October 2008. The SFC states that "whilst the arguments are finely balanced regarding the accounting treatment, the direction of travel does appear to be towards accounting for the SPF as a defined benefit scheme". Although the SFC is minded to advise colleges in the SPF to consider the possibility of accounting for the scheme as defined benefit, no directive to this effect is given, and it is acknowledged that there is scope within FRS17, as currently worded, to account for the scheme as defined contribution.

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.

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 due to be finalised by December 2008, 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. However as the project is still subject to approval no impairment provision is required in the year to 31 July 2008.

Further Education Childcare Funds

- The College has treated FE Childcare funds in accordance with paragraph 55 of the SORP which states that 'Where an institution disburses funds it has received as paying agent on behalf of a Funding body or other body, and has no beneficial interest or risks related to the receipt and subsequent disbursement of the funds they should be excluded from the income and expenditure of the institution.' 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 2007-08 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 College has not included FE Childcare Funds in the income and expenditure within the financial statements. We reported on this in our report to the Board of Management in 2006/07. The College received and disbursed approximately £70,000 in relation to FE Childcare funds. This 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 2008 audit

- No recommendations have been made in 2008.

Recommendations made during 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 at 31 July 2007

- 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

Management Response at 31 July 2008

- The detailed risk review was delayed until October 2008. A risk management workshop took place in mid October where full consideration of all risks was undertaken and the recommendation was implemented.
- From this the three year internal audit plan was established to focus on the risk areas. This was approved by the audit committee in November 2008.

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 the 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. A statutory instrument was laid in parliament in June 2008 which came into force on 27th June 2008. This disapplies the section in the Act in relation to controlling activities, consequently charitable status is maintained.

BDO Stoy Hayward LLP

10 December 2008