INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

Glasgow Metropolitan College

Annual audit report to the Board of Management and Auditor General for Scotland
Year ended 31 July 2009

22 December 2009

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

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About this report
This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the *Code*").

This report is for the benefit of only Glasgow Metropolitan College and is made available to Audit Scotland (together "the beneficiaries"), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scope and objectives section of this report.

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Executive summary

Financial commentary

The College achieved a surplus of £828,000 compared to a forecast surplus of £77,000 and a £1,201,000 surplus in the year ended 31 July 2008. Reasons for the significant increase in outturn compared to the original budget were reported to the finance and estates committee during the year. The financial statements report retained general reserves of £28.3 million.

The 2009-10 financial plan forecasts a surplus of £231,000, however, this is supported by expected investment income returns of £300,000.

Governance and risk management

The corporate governance statement does not disclose any significant weaknesses in the systems of internal control. The content of the statement is consistent with our understanding.

Internal audit concluded that the College "*has a framework of control which provides assurance regarding the effective and efficient achievement of the College's objectives.*"

There is a formal process to record, distribute and monitor action in response to key guidance and circulars.

The operating and financial review provides a comprehensive account of the College's activities and meets the requirements of Statement of Recommended Practice for further and higher education institutions 2007 ("SORP 2007").

The Board of Management has recently highlighted a number of concerns over aspects of the governance arrangements and related processes of the ongoing merger with two other Glasgow colleges. Following a Board of Management letter outlining these concerns to its merger partners and the Shadow Board of the new college, action to address these concerns has recently been initiated.

Financial statements audit

We issued an audit report expressing an unqualified opinion on the financial statements of the College for the year ended 31 July 2009.

Management did not provide draft financial statements and supporting working papers in line with the agreed timetable. The draft financial statements were, however, complete and of good standard and the standard of supporting analysis was good with evidence of accountability and ownership of working papers across the finance department.

The College has accounted for, and disclosed its interest, in New Campus Glasgow Limited as an associate company.

Introduction

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice*. This, and supplementary planning guidance issued by Audit Scotland, specifies a number of objectives for our audit.

Audit framework

This was the third of our five-year appointment by the Auditor General for Scotland as external auditors of Glasgow Metropolitan College. This report to the College's Board of Management and the Auditor General provides our opinion and conclusions and highlights significant issues arising from our work.

We outlined the framework under which we operate, under appointment from Audit Scotland, in the audit plan overview discussed with the Board of Management's audit committee on 21 May 2009.

In accordance with Audit Scotland's Code, the scope of our work for 2008-09 was to:

- provide an opinion on the College's financial statements and, as required by the relevant authorities, the regularity of transactions;
- review and report on (as required by relevant legislation, *the Code* and any guidance issued by Audit Scotland):
  - corporate governance arrangements as they relate to: its review of systems of internal control; the prevention and detection of fraud and irregularity; standards of conduct, and prevention and detection of corruption; its financial position
  - aspects of the College's arrangements to manage its performance, as they relate to economy, efficiency and effectiveness in the use of resources.

Responsibilities of the Board and auditors

External auditors do not act as a substitute for the Board of Management's own responsibilities for putting in place proper arrangements to account for the stewardship of resources made available to its and its financial performance in the use of those resources, to ensure the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the effectiveness of those arrangements and, through the College principal, to make arrangements to secure Best Value.

Acknowledgement

Our audit work has again brought us into contact with a range of College staff. We wish to place on record our appreciation of the cooperation and assistance extended to us by staff during the discharge of our responsibilities.

Service overview; overall position for year; income

- The College achieved a surplus of £828,000 compared to a forecast surplus of £77,000 and a £1,201,000 surplus in the year ended 31 July 2008. Reasons for the significantly increase in outturn compared to the original budget were reported to the finance and estates committee during the year.
- The financial statements report retained general reserves of £28.3 million.
- The 2009-10 financial plan forecasts a surplus of £231,000, however, this is supported by expected investment income returns of £300,000.

Service overview

The College continues to position itself as a specialist vocational training provider, covering key industry sectors such as construction, creative industries, and the food and hospitality sector. The College Principal retired during the year, but returned in a part-time role to continue to support the College – at a strategic level – through the proposed merger. The new Principal will be a joint appointment on behalf of the College, Central College Glasgow and Glasgow College of Nautical Studies, in anticipation of the merger of these three colleges by 1 August 2010. The merger is aimed at assisting with the progress of the New Campus Glasgow project, the aim of which is development and creation of a major new estate for the co-location of the three city centre colleges.

The financial statements report a surplus for the year of £828,000, a decrease of 31% compared to 2007-08. At 31 July 2009 there were retained general reserves of £28.3 million. Management report that £546,000 of the surplus comes from investment income rather than operational activities.

Income

Income for the year has risen by £1.6 million compared to 2007-08, an increase of 6%. As the undernoted table demonstrates, most of the increase has arisen from increases in Scottish Funding Council grants. The principal movements are attributed to:

- a £1,062,000 increase in recurrent grant from the Scottish Funding Council (including fee waiver) as a consequence of higher levels of funding per student than in previous years;
- a £370,000 increase in tuition fee income as a consequence of higher student numbers; and
- a £223,000 decrease in investment income due to reductions in market rates of return on investments as a result of the current economic climate.

	2008-09 £'000	2007-08 £'000	Movement £'000	Movement %
Scottish Funding Council grants	19,809	18,497	1,312	7
Tuition fees and education contracts	4,510	4,087	423	10
Other operating income	2,588	2,514	74	3
Investment income	573	796	(223)	-28
Total	**27,480**	**25,894**	**1,586**	**6**

Expenditure

Expenditure

In line with the increase in income, expenditure has also risen from £24.7 million in 2007-08 to £26.7 million. Individually significant movements included:

- a £965,000 increase in expenditure on wages and salaries primarily as a result of a 3.5% pay increase to staff during the year, plus incremental progression, as well as the slight increase in total staff numbers;
- a £442,000 increase in other operating expenses due to a £298,000 increase in premises costs such as utilities, plus a £140,000 increase in consultants' costs primarily related to the learn, direct and build project; and
- a £331,000 increase in the depreciation charge due to the revised building valuation as at 31 July 2008, and equipment additions during the year.

	2008-09 £'000	2007-08 £'000	Movement £'000	Movement %
Staff costs	18,209	17,023	1,186	7
Other operating expenses	6,151	5,709	442	8
Depreciation	2,292	1,961	331	17
Total	**26,652**	**24,693**	**1,959**	**8**

Balance sheet

The balance sheet shows a decrease of £1.2 million in net assets as at 31 July 2009 compared to the previous year end. Significant movements include:

- an increase in tangible fixed assets of £403,000. This is a result of additions in relation to the College's share of expenditure to date on the New Campus Glasgow project of £1,158,000, in respect of land and buildings under construction. These additions have been offset by the increase in depreciation charge in the year;
- a £318,000 increase in accrued income in respect of European Social Fund projects where the College has yet to receive the outstanding income owed;
- a £638,000 reduction in deferred income as a result of management utilising existing grants brought forward from previous financial years in 2008-09 to fund ongoing various capital and revenue projects;
- a £407,000 reduction in trade creditors due to the College undertaking less capital works during the months prior to the year-end which would, historically, have led to higher creditors at the year-end; and
- a £3,026,000 million increase in the College's pension liability as at 31 July 2009, as a result of the worsening economic climate during the year impacting on asset values.

	2009 £'000	2008 £'000	Movement £'000	Movement %
Fixed assets	30,855	30,452	403	1
Stock	18	12	6	50
Debtors	1,392	1,121	271	24
Cash and short-term investments	10,391	10,372	19	0
Creditors: amounts falling due within one year	(2,856)	(4,097)	1,241	(30)
Provisions for liabilities and charges	(1,296)	(1,180)	(116)	10
Pension liability	(3,586)	(560)	(3,026)	540
Net assets	**34,918**	**36,120**	**(1,202)**	**(3)**

Financial forecasts

Financial forecasting

The probable outturn reported to the finance and estates committee in June 2009 was £288,000 against the budget for the year of £77,000. Management prepared a detailed reconciliation for the meeting outlining the changes from the budget position. An updated report to the finance and estates committee in September 2009 revised the probable outturn to £749,000, against an actual outturn of £828,000. The main reasons for the movement from the June 2009 figures to the actual outturn were as follows:

- recognition of £327,000 of European Social Fund income which management had not included previously until formal approval for the grant funding for the 2009 programme had been received;
- a further increase of £200,000 in tuition fees for the year over that anticipated in June;
- additional other operating income of £192,000 over a number of budget lines;

These increase in the outturn were offset by an increase in the early retirement provision of £190,000 following the Scottish Funding Council's guidance in respect of revised actuarial factor tables to be used when calculating the provision required.

2009-10 financial forecast

The following table summarises the 2009-10 financial forecast.

	£'000
Income	27,062
Expenditure	26,831
Forecast surplus for the year ending 31 July 2010	**231**
Cash and short term investments balance at 31 July 2009	10,391
Forecast cash and short term investments balance at 31 July 2010	10,722
Forecast movements in cash and short term investments during 2009-10	**331**

The surplus forecast for 2009-10 represents a significant reduction on the actual 2008-09 outturn. Income is expected to fall by £418,000, of which £631,000 represents an increase in funding from the Scottish Funding Council, no major change in tuition fee income, but a decrease of £801,000 in respect of other income and £273,000 less investment income.

Expenditure is forecast to increase by £179,000. This includes a £267,000 increase in staff costs, £188,000 decrease in other operating expenses and a £100,000 increase in depreciation.

Governance and risk management

- The corporate governance statement does not disclose any significant weaknesses in the systems of internal control. The content of the statement is consistent with our understanding.
- Internal audit concluded that the College "*has a framework of control which provides assurance regarding the effective and efficient achievement of the College's objectives.*"
- The College has in place a formal process to record, distribute and monitor action in response to key guidance and circulars.
- The operating and financial review provides a comprehensive account of the College's activities in line with the requirements of the SORP 2007.
- The Board of Management has recently highlighted a number of concerns over the ongoing merger with two other Glasgow colleges. Following a Board statement outlining these concerns to its merger partners and the Shadow Board of the new college, action to address these concerns has recently been initiated.

Introduction

Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all publicly-funded bodies.

Through the College principal, the Board of Management is responsible for establishing arrangements for ensuring the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the adequacy of these arrangements. The *Code* requires auditors to review and report on the College's corporate governance arrangements as they relate to:

- the College's reviews of its systems of internal control, including reporting arrangements;
- the prevention and detection of fraud and irregularity;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- its financial position.

Governance arrangements

The Board of Management comprised 12 members as at 31 July 2009, with a further appointment made in August 2009. In addition, the College has co-opted one member to the finance and estates committee. The skills of the members of the Board of Management including those with relevant skills and expertise in finance, accountancy, marketing and management consultancy. Management are aware of the importance of ensuring that the new Board members have a timely induction and are appropriately trained to ensure that there roles are fully understood. The College has seven standing committees, including the finance and estates committee and the audit comittee, all of which report into the Board of Management. Each committee has its own terms of reference and is formally constituted. The committees comprise representation from staff, students and non-executive members. This structure demonstrates best practice and provides the Board of Management with appropriate oversight and monitoring of financial and academic activities.

The College secretary and clerk to the Board of Management role is performed by the head of planning. It is considered best practice that this role is held by an individual who is independent of College management.

Recommendation one

Governance and risk management (continued)

Risk management

The Board of Management takes responsibility for overseeing risk management within the College, with the principal and senior management team acting as policy advisors. As part of the risk management process, the senior management team regularly considers risk and a risk assessment matrix is compiled and submitted to the audit committee. The risk assessment matrix identifies, prioritises and assesses risks to the College according to the likelihood and the impact of each risk. The audit committee meet regularly during the year to review the College's response to identified risks.

The College's approach to risk management is based on guidance produced by the Chartered Institute of Public Finance and Accountancy ("CIPFA") for the further and higher education sectors in Scotland. The most recent assessment matrix did not include any assessment in relation to the impact of possible public expenditure restraints, albeit that management was intending that this should be fully discussed with the Board of Management in due course.

Corporate governance statement

The corporate governance statement for 2008-09 provides details on how the Board of Management have established processes and controls in order to comply with the combined code on corporate governance, issued in 2003. The statement highlights that the College is committed to exhibiting best practice in all aspects of corporate governance. The corporate governance statement is informed by the results of internal consideration of the arrangements that have been put in place by the Board of Management.

Regularity

The Board of Management considers all incoming correspondence relevant to its strategic management role from the Scottish Funding Council and other regulatory or advisory bodies, such as Audit Scotland. The audit committee also considers any applicable correspondence. The College therefore considers all incoming guidance received from these bodies, and can demonstrate that they take appropriate action when required. While there is procedures for monitoring all guidance issued, management should consider implementing a formal record of actions taken for each circular received to its existing log of circulars and guidance.

Internal audit

The approved internal audit programme for 2008-09 has been completed and the internal auditors have concluded that the College "*has a framework of control which provides assurance regarding the effective and efficient achievement of the College's objectives*". Internal audit also concluded that "*the College has, based on the areas examined in 2008-09, proper arrangements to promote and secure value for money.*"

Internal controls

In accordance with our audit plan, we undertook detailed testing in relation to both entity level and key financial controls. We relied on the work carried out on internal audit around tuition fees and debtors and student records. Testing of the design and operation of controls over significant risk points in terms of major financial systems confirms that controls are designed appropriately and operating effectively.

Prevention and detection of fraud and irregularity

The College has in place an over-arching fraud prevention policy, in addition to a whistle-blowing policy. Both policies are readily available to staff on the College's intranet and are also published on the College's website. The fraud prevention also includes a plan on the response to any frauds identified. Management has not reported any frauds, material or otherwise, during 2008-09. In addition to these policies, the College has implemented procurement and tendering procedures to ensure that the risk of financial irregularity is mitigated.

Governance and risk management (continued)

College mergers

At the beginning of the year, merger discussions between the College and Stow College were abandoned. A subsequent proposed merger of the College with two other Glasgow city centre colleges is reported as one of the principal risks facing the College. In respect of the merger, which is due to take place on 1 August 2010, this is progressing on a `host model' basis where the College will be the host college. A Shadow Board has been formed. Despite variations in the comparative sizes of each partner, this comprises an equal representation from all three colleges, with an additional co-opted member for their skills and experience.

On 14 October 2009, the Board of Management held a special meeting to discuss a number of governance issues regarding the merger process which had arisen from senior management and Board member concerns. These included the consideration of the need for independent members of the Shadow Board, recruitment procedures over the principal of the merged college, the appointment of a merger co-ordinator; and the balance, co-option and voting rights on the Shadow Board. At the end of this meeting, the Board of Management agreed a statement outlining their concerns, which included the resolve to consider withdrawal from the merger process unless their concerns were addressed.

A further special meeting was held on 2 November 2009 to discuss the impact of the Board's statement. It was noted that action had been taken in respect of all concerns. The Board of Management will, however, continue to give detailed consideration to the merger process and progress. The Scottish Funding Council continues to monitor the progress of the discussions.

Standards of conduct

There are comprehensive human resources policies and procedures in place at the College. All policies are readily accessible to staff via the intranet and are published on the internet pages of the college. There are codes of conduct in place for general staff, senior management and members of the Board of Management. There is a formal register of interests for recording members of the Board of Management and senior managers' interests. This is considered to be best practice and assists in demonstrating consideration of independence in decision-making and the awarding of contracts.

Best Value / value for money

The 2008-09 planning guidance for further education colleges issued by Audit Scotland indicated that there was no requirement for auditors to undertake performance audit or other Best Value studies during the year.

Scottish Funding Council enquiry

On 9 June 2009 the Scottish Funding Council issued an enquiry letter to all further education colleges in Scotland as a result of findings by the Scottish Funding Council's internal auditors. These asked colleges to ensure that:

- all non-trivial contracts entered into by institutions are committed to writing;
- statutory child protection requirements in relation to Enhanced Disclosure checks are adhered to;
- Boards of Management avoids the prospect of any actual perceived conflicts of interest for board members at all times; and
- colleges are aware of and adhere to guidance issued in relation to provision provided in collaboration with other organisations.

The College has replied to this enquiry with positive affirmations that it already complies with best practice in each of these areas.

Key findings

- We issued an audit report expressing a unqualified opinion on the financial statements of the College for 2008-09.
- Management did not provide draft financial statements and supporting working papers in line with the agreed timetable. The draft financial statements were, however, complete and of good standard and the standard of supporting analysis was good with evidence of accountability and ownership of working papers across the finance department.
- The College has accounted for, and disclosed its interest, in New Campus Glasgow Limited as an associate company.

Audit opinion

On 22 December 2009 we issued an audit report expressing an unqualified opinion on the financial statements for the year ended 31 July 2009 and on the regularity of transactions reflected therein.

Financial statements – compilation arrangements

We received a draft set of financial statements, including narrative statements, on 15 October 2009. This was after the start of the audit fieldwork commenced on the previously agreed date of 5 October 2009. The draft financial statements were, however, complete and of a high standard. The draft Board of Management report was received on 20 October 2009. The standard of analysis was good and there was evidence of accountability and ownership of working papers across the finance department. We have made one recommendation to management within our report to those charged with governance to improve the efficiency of the audit process.

Accounting for New Campus Glasgow Limited

The College's associate company, New Campus Glasgow Limited, is responsible for the development of a major new estate for the co-location of three of Glasgow's city centre colleges. Following the withdrawal of Stow College from the project, the College has a one third share in the company and it has accounted for its interest in the result and net assets of the Company. Due to the funding arrangements of the Company, its result for the year and net assets are both £nil.

We discussed with College management in advance of the audit fieldwork that the three colleges having an interest in the project would need to account within fixed assets for their third share of the assets under construction at the year end. This is because New Campus Glasgow is carrying out the construction project on behalf of the colleges. Following receipt of information from the Company, the College has included its share of land purchased by the Company on behalf of the colleges, as well as its share of assets under construction. The fixed asset additions are matched by deferred capital grant funding provided by the Scottish Funding Council for the project.

Corporation tax risk

As part of our audit planning for the College, we performed a high-level review of the various potential corporation tax issues.

There is always a risk when a charity has trading activities that this could expose them to a corporation tax charge from HM Revenue and Customs ("HMRC"). This could arise from generating a profit or a loss on an activity that is considered to be a non-primary purpose (NPP) trading activity. A NPP profit is subject to corporation tax. If a loss arises on NPP trading activities this creates a non-charitable expenditure charge which is equal to the loss. This non-charitable expenditure charge is subject to corporation tax. If the activities that this loss arose from are run on a commercial basis (with a view to making a profit) or the College itself is considered to be commercial (i.e. the College has a surplus in the year and in recent years) then the non-charitable expenditure charge can be sheltered by the corresponding loss thus self cancelling.

If there are NPP trading activities and the total income arising from these is less than £50,000 then normally this is covered by the small trading exemption available to charities.

Closed courses

Closed or restricted courses are deemed to be a non-primary purpose activity. A closed course is broadly one where the attendees are drawn form a narrow range of the public, or the criteria for selection for the course exclude the wider general public, or the benefit is not to a sufficiently wide sector of the public. A typical example would be where a College provides a course or training specifically for a single business. Provided the overall income arising from these activities (when taken together with any other NPP activities) is less that the £50,000 small trading threshold then we believe the tax risk from the offering of these services to be low.

Area for development	Action plan reference
Management should review the various income streams of the College to identify any areas of potential tax risk. If the income arising on these activities exceeds the small trading exemption of £50,000 a corporation tax return and computation should be prepared and submitted to HMRC. If the income falls within the small trading exemption, supporting evidence should be prepared to detail and record management's analysis in case of any future enquiries by HMRC.	Two

Appendix one – action plan

Priority rating for recommendations		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the Board or systems under consideration. The weakness may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the controls to meet their objectives in any significant way. These are less significant observations than grades one and two, but we still consider they merit attention.

No.	Issue and recommendation	Management response	Officer and due date
1	The College secretary and clerk to the Board of management role is performed by the Head of Planning. It is considered best practice that this role is held by an individual who is independent of College management. *(Grade three)*	The College Board are satisfied with the current service provided by the Head of Planning. During future merger discussions the role of the College secretary and clerk to the Board will be reviewed and the best approach agreed.	Principal June 2010
2	During our audit we have identified a number of areas where the College could be open to the risk of tax exposure. We recommend that management analyse the various income sources of the College to identify any areas of tax risk. A record should then be kept of this analysis to aid in any future tax enquiries. *(Grade three)*	The College is aware of recent Corporation Tax issues in higher education institutions. Further analysis and investigation of potential tax exposure will be undertaken.	Vice-Principal (Corporate Services) April 2010