James Watt College

Annual Audit Report to the Board of Management and Auditor General for Scotland

Audit for the year ended 31 July 2011

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The contacts at BDO in connection with this report are:

Robert Ralston	**Gordon Kerr**
Partner	Senior Manager
Tel: 0141 249 5214	Tel: 0141 249 8453
Fax: 0141 248 1653	Fax: 0141 248 1653
robert.ralston@bdo.co.uk	gordon.kerr@bdo.co.uk

EXECUTIVE SUMMARY

James Watt College

Financial Highlights

The College achieved a deficit of £977k (2010 deficit of £426k) on its income and expenditure account for the year prior to FRS17 adjustments for the Strathclyde Pension Scheme (SPF). After a credit of £458k to income and expenditure account for FRS17 adjustments (2010 credit of £976k) the overall deficit for the year was £519k (2010 surplus of £550k).

The financial statements disclose retained general reserves of £12.65m (2010 £10.79m). The 2011/12 financial forecast return anticipates a surplus of £179k, excluding adjustments in relation to FRS 17.

Corporate Governance

From our review of Corporate Governance arrangements within the College, we believe the Corporate Governance statement to be neither misleading nor inconsistent with other information made available to us during the course of the audit process. The Corporate Governance statement does not disclose any significant weaknesses in the systems of internal control.

Internal auditors Henderson Loggie concluded that the College operates adequate and effective internal control systems as defined in the audit needs assessment.

The Operating and Financial Review provides a comprehensive account of the College's activities and meets the requirements of the Statement of Recommended Practice Accounting for Further and Higher Education 2007 ("SORP 2007").

Financial Statement Audit

We have completed our audit work in respect of the financial statements of the College and are satisfied that they present a true and fair view of its financial position for the year ended 31 July 2011. Following approval of the financial statements by the Board of Management on 15 December 2011 our audit report will express unqualified opinions on (i) the financial statements of the College for the year ended 31 July 2011 and (ii) regularity.

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

Management provided draft financial statements and supporting working papers in line with the agreed timetable. The draft financial statements and supporting documentation were complete and of a good standard.

The 2010/11 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.

OVERVIEW, SCOPE AND INDEPENDENCE

James Watt College

Overview

• The purpose of this report is to highlight and explain key issues arising from our audit of the financial statements of James Watt College ('the College') for the year ended 31st July 2011.

•This report covers those matters we believe to be material in the context of our work. It was prepared from general information obtained during the audit process, including management accounting information and discussion with management and staff of the College. It has been prepared solely for the use of the College and the Auditor General for Scotland and should not be shown to any other person without our express permission in writing. We do not accept responsibility for this report to any other person and we hereby disclaim any and all such liability. We do not, in preparing this report, accept or assume responsibility for any other purpose or to any other person to whom it is shown or into whose hands it may come save as expressly agreed by our prior written consent. If others choose to rely on the contents of this report, they do so at entirely their own risk.

• 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 2011. 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.

Significant Accounting and Audit Issues

Detailed below are the key accounting and audit issues identified during our work:

- Additional fee waiver
- Impairment of the halls of residence
- Severance
- FRS 17 – retirement benefits
- Strategic restructuring grant
- Local authority project grants
- Estates strategy
- SUM's Achievement
- Future grant funding
- Revaluation of land and buildings

Unadjusted Audit Differences

We are required by International Standard on Auditing (UK & Ireland) 260 to bring to your attention audit adjustments that we have identified but we are not proposing to adjust and which the Board of Management is required to consider. A schedule of such adjustments is included in Appendix 1. We have not included items under £3,860 which we consider to be clearly trivial. Total unadjusted audit differences identified by our audit work would reduce the deficit for the year by £8k and would require reallocations within the Income & Expenditure Account and Balance Sheet respectively. The Board will need to consider the materiality of these identified misstatements in the context of the financial statements taken as a whole.

BDO

OVERVIEW, SCOPE AND INDEPENDENCE
Continued…

Key areas	Summary
Scope	The accounting rules and regulations applied to Further Education Colleges are specifically laid out in various documents as discussed on page 8 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. We can confirm that 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. The audit of James Watt 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.
Independence	Under Auditing and Ethical Standards, we are required as auditors to confirm our independence to "those charged with governance". This term refers to the Board of Management in our view and we confirmed our independence to them in a letter on 6 May 2011. Our internal procedures are designed to ensure that all partners and professional staff are aware of relationships that may be considered to bear on our objectivity and independence as auditors. The principal statements of policies are set out in our Conduct of Professional Services Manual. In addition, we have issued supplementary written guidance and embedded the requirements of the Standards in our internal training programmes. The procedures require that audit engagement partners are made aware of any matters which may reasonably be thought to bear on the firm's independence and the objectivity of the audit engagement partner and the audit staff. We confirm that the firm complies with the APB Ethical Standards and, in our professional judgment, is independent and objective within the meaning of those Standards. In our professional judgement the policies and safeguards in place ensure that we are independent within the meaning of all regulatory and professional requirements and that the objectivity of the audit engagement partner and audit staff is not impaired. Should you have any comments or queries regarding this confirmation we would welcome their discussion in more detail.

AUDIT FRAMEWORK

Audit Framework

Audit Framework

BDO LLP was appointed by Audit Scotland as external auditor to James Watt College for 5 years covering the financial years 2006/07 to 2010/11. This year was the final year of the five-year appointment by the Auditor General for Scotland as external auditors of James Watt College ("the College"). This report to the College Board of Management and Auditor General for Scotland provides our opinion and highlights issues arising from our work in relation to our audit work for 2010/11 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 LLP .

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.

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.

AUDIT FRAMEWORK
Continued…

Auditor's Responsibilities and Approach

Audit Framework

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.

AUDIT FRAMEWORK
Continued…

College Guidance

Audit Framework

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. Our audit procedures identified no factors that would lead us to believe that the college does not comply with the terms and conditions of the financial 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

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)

We can confirm that the financial statements of the College are in general in compliance with the requirements of the 2007 SORP.

FINANCIAL HIGHLIGHTS

James Watt College

Key areas	Summary
Financial Highlights	• **Income and Expenditure Account:** The College achieved a deficit of £977k (2010 deficit of £426k) on its income and expenditure account for the year prior to FRS17 adjustments for the Strathclyde Pension Scheme (SPF). After a credit of £458k to income and expenditure account for FRS17 adjustments (2010 credit of £976k) the overall deficit for the year was £519k (2010 surplus of £550k). The forecast surplus for the year was £46k (2010 £45k). •Excluding the FRS 17 adjustments, income rose by £476k compared with the previous year with increased SFC funding partially compensated for by falls in other types of income. Expenditure increased by £1.027m, including additional exceptional restructuring costs of £3.3m partially compensated for by reductions in other staff costs of £1.4m, an impairment charge of £384k and a reduction in other operating expenses of £1.4m. •**Balance Sheet:** The financial statements report net assets at 31 July 2011 of £17.583m. The £1.88m increase on 2009/10 is mainly attributable to an upward revaluation of fixed assets of £2.1m offset by impairment of the halls of residence of £529k. In addition, there was an actuarial gain in the pension scheme of £843k and the deficit on income and expenditure account for the year of £519k.
Cash Flow	During 2010/11, the College experienced a net outflow of cash of £132k (2009/10: inflow of £1.499m).
Financial Forecast	The initial 2010/11 financial plan forecasted a surplus of £46k. The main differences between that which was forecast and achieved are shown on page 13 of this report. The forecast of income and expenditure for the College for 2011/12 shows that income is expected to fall significantly on the current year to £34.4m mainly due to a fall in SFC grant funding.

FINANCIAL HIGHLIGHTS
Income and Expenditure Account

Income

- The table below summarises the main sources of income for 2010/11and 2009/10.
- The College's WSUMs target for 2010/11 was 154,194 (including 3,394 for economic downturn). As the College delivered 158,687 WSUMs, the College will not be liable to repay any recurrent grant to SFC in 2011/12.
- A significant proportion of income (87%), is received from the Scottish Funding Council and there has been a substantial increase in this source of income on the prior year (£1,195k), which is mainly due to the main Grant-In-Aid allocation increasing substantially.
- A decrease in tuition fees and education contracts of £543k. This is mainly as a result of the ending of the MCMC programme at the start of the year (no income was recognised for this at all in the year).
- A decrease in other income and investment income of £228k. This has arisen due to a substantial fall in catering and residency income due to the halls of residence being shut for most of the year.

Income and Expenditure Account	31 July 2011 £'000	31 July 2010 £'000	Variance £'000
Scottish Funding Council Grants	33,705	32,510	1,195
Tuition Fees and Education Contracts	3,163	3,706	(543)
Other Income	1,602	1,830	(228)
Investment Income	130	67	63
Total Income	**38,600**	**38,113**	**487**
Expenditure (see analysis on next page)	**39,119**	**37,563**	**1,556**
(Deficit)/Surplus	**(519)**	**550**	**(1,069)**

FINANCIAL HIGHLIGHTS
Income and Expenditure Account continued…

Expenditure

Total expenditure increased by £1.556m (4.1%), in comparison to 2009/10, to £39.1m. The increase in expenditure is, in the main, due to an increase in staff costs (the restructuring costs portion of this) with the most significant movements detailed as follows. The table below summarises the main categories of expenditure for 2010/11 and 2009/10:

- an increase in staff costs of £2.841m mainly due to exceptional restructuring costs of £4,133k (compared to £824k in the prior year), partly offset by a reduction in other staff costs due to lower staff numbers; and
- a decrease in other operating expenses of £924k which is primarily due to the College's method of accounting for additional fee waiver grant. In 2010, £528k was debited to bad debts as the recoverability of the debtor was uncertain. The additional fee waiver was received in 2011 and the amount received was credited to bad debts.
- a minimal increase of £20k in the depreciation charge.
- a decrease in interest payable of £381k due to there being a current year net credit for interest (of £11k) compared to a prior year net debit for pensions interest (of £362k) as a result of the FRS 17 adjustment.

Expenditure Analysis	31 July 2011 £'000	31 July 2010 £'000	Variance £'000
Staff Costs	23,157	23,625	(468)
Restructuring costs	4,133	824	3,309
Other Operating Expenditure	10,221	11,145	(924)
Depreciation	1,455	1,435	20
Interest Payable	153	534	(381)
Total Expenditure	**39,119**	**37,563**	**1,556**

FINANCIAL HIGHLIGHTS
Balance Sheet

The balance sheet shows an increase of £1,884k in net assets as at 31 July 2011 compared to the previous year end. Significant movements include:

- An increase in tangible fixed assets of £463k. This is a result of the deprecation charge for the year of £1.455m, along with the halls of residence impairment (reduction in NBV of £913k), an upward revaluation of the other land and buildings of £2.062m together with capital expenditure in the year of £769k mainly being the upgrading to the Finnart Street Campus.
- A reduction in debtors of £433k mainly as a result of a reduction in the bursary funds debtor of £406k. This debtor was unusually high in 2010 due to bursary payments being made from the College bank account.
- A decrease in cash of £132k. This is primarily a result of the receipt of £1.725m of capital grants added to a net cash inflow from operating activities of £677k less capital expenditure of £769k and loan repayments of £1.729m.
- A decrease in creditors falling due within one year of £192k including the repayment of an SFC loan of £1.25m and an increase in capital grant deferred income of £957k.
- A decrease in creditors falling due after one year of £496k. This is substantially due to bank loan repayments made in the year.
- A decrease in the pension liability of £1.301m including an actuarial gain of £843k.

Balance Sheet Category	31 July 2011 £'000	31 July 2010 £'000	Variance £'000
Fixed Assets	25,071	24,608	463
Stock/Debtors	1,749	2,185	(436)
Cash	8,319	8,451	(132)
Creditors: Amounts falling due within 1 year	(11,255)	(11,447)	192
Creditors: Amounts falling due after 1 year	(3,394)	(3,890)	496
Pension Liability	(2,907)	(4,208)	1,301
Net Assets	**17,583**	**15,699**	**1,884**

FINANCIAL HIGHLIGHTS
Financial Forecasts

Financial Forecasting

- The initial 2010/11 financial plan forecasted a surplus of £46k. The table below (bottom left) shows the reconciliation between the forecast outturn and the actual amount generated during the course of the year. The main reasons for the movement from the forecast to the actual outturn were as follows:
  - Increase in SFC grant income of £93k. There was also an increase in other sources of income including £130k worth of European income being released from a claw back provision and higher than budgeted tuition fees.
  - An increase in payroll costs re higher than budgeted voluntary severance costs of £3,883k. Other salary costs are down by £1,064k due to there being fewer staff members employed after the restructuring programme.
  - The forecast depreciation charge was £607k higher than the actual charge.
  - Other operating expenses were £518k lower than forecast with the largest saving being in administration costs.

- The table below (bottom right) summarises the forecast income, expenditure and cash balances for the College for 2011/12.
- Income is expected to fall in 2011/12(by £4.2m) with a corresponding decrease in expenditure (excluding any FRS 17 adjustments). This should result in a modest surplus of £179k, excluding FRS 17 adjustments. College expenditure will have to be monitored closely, in particular staff costs which represent 61% of forecasted College expenditure, in order to achieve the forecasted surplus.

Forecast vs. Actual	31 July 2011 £'000	31 July 2010 £'000
Forecast outturn per budget	**46**	**45**
Increase/ (Decrease) in SFC grant income	93	(272)
Increase in other income	414	743
(Increase) in exceptional restructuring costs	(3,883)	(700)
(Increase)/decrease in payroll and other operating expenditure	2,353	(242)
FRS 17 adjustments	458	976
Actual outturn at year end	**(519)**	**550**

Forecast Income, Expenditure and Cash Balances for 2011/12	£'000
Income	34,439
Expenditure	(34,260)
Forecast surplus for the year ending 31 July 2012	**179**
Cash balance at 31 July 2011	8,319
Forecast movement in cash during 2011/12	(4,137)
Resulting cash balance at 31 July 2012	**4,182**

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters

James Watt College

Additional Fee Waiver - Recognition of Income

- With respect to fee waiver, the college is not in a clawback position for 2010/11 and due to the high level of demand amongst students the College is in a position to receive an additional fee waiver grant. Calculations were agreed showing that the College may receive an additional fee waiver grant of £229k. However, due to the economic downturn and the resultant increase in the number of students with fee waiver needs across the college sector, SFC may not be able to meet the demand from all colleges for additional fee waiver grant due to funding constraints.

BDO Conclusion

Management have recognised the fee waiver income of £229k within income in the financial statements and have made full provision against non recovery of the amount by debiting bad debts with the same amount. Whilst our preferred presentation would have been to exclude the £229k from both income and expenditure (income should not be reflected in the financial statements unless it is more likely than not to be received), we are satisfied that the net result is unaffected.

Estates Strategy

- An “Estates Strategy” paper was put to the Board of Management in April 2008. Decisions taken on the future use of the College’s estates could indicate the need for impairment in the current carrying values of the College’s land and buildings in 2009/10. The estates strategy is updated on a yearly basis and fully refreshed every five years; the most up to date strategy – from November 2009 – was obtained. This noted the progress on the targets set in the original estates strategy. An estates strategy update paper was presented to the Board in September 2011.

BDO Conclusion

Having reviewed the latest estates strategy document and discussed it with management, there is no indication that any of the properties at each campus require to be impaired at the year-end, other than the Halls of Residence (see page 15).

BDO

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

Impairment of the Halls of Residence

- During the year the College marketed its Halls of Residence and revalued them at 31 July 2011 to the anticipated recoverable amount. An impairment provision of £913k was reflected through the financial statements with £529k debited to the revaluation reserve and £384k debited to the income and expenditure account. The College disposed of the Halls of Residence in the post year end period.

BDO Conclusion

The College's has correctly accounted for the impairment of the Halls of Residence in accordance with FRS11 – Impairment of Fixed Assets.

SUMs Achievement

- SFC require the College to achieve total WSUMs within 2% of its target for the year to avoid being in a clawback position.

BDO Conclusion

The College certificate to SFC shows a WSUMs total for the year to 31 July 2011 of £158,687. This figure is in excess of its target for the year of 154,194 and accordingly there should be no clawback of SFC grant for non achievement of WSUMs target.

KEY ACCOUNTING AND AUDIT MATTERS

From the Audit Planning Memo & Other Matters Continued…

Severance scheme
The College has implemented a severance scheme to encourage voluntary redundancy and reduce payroll costs. The College should ensure that the accounting treatment of the severance scheme is correct and that the College severance policy and procedures are appropriate, legal and have been applied consistently.
BDO Conclusion
Severance payments made during 2010/11 were found to comply with the College severance policy and have been correctly accounted for and disclosed in the financial statements.

Future grant funding
The College, in line with the wider public sector, is facing significant uncertainty over future funding levels and the impact and scope of public sector funding cuts.
BDO Conclusion
Despite the fact that funding cuts are likely to affect the College in the upcoming financial year and beyond, the College is in a strong cash position with £8.3m in the bank at 31 July 2011 (albeit there is also a bank loan creditor of £3,890k at the year end) and is forecasting an income and expenditure account surplus for the year ending 31 July 2012 of £179k and a bank balance of £4.2m. Cash and bank is forecast to be £4.1m lower than at 31 July 2011 mainly due to capital expenditure. Management have concluded that the college has adequate cash resources for at least twelve months from the date of approval of the financial statements and we consider management's use of the going concern assumption to be appropriate in the circumstances.

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

Strategic Restructuring Grant
Included within accruals and deferred income is a balance of restructuring grant of £215k which has been brought forward from year ended 31 July 2009 with no release in either 2010 or 2011. Last year management explained that the restructuring grant of £215k had not been required in 2010 as the college had made its own savings in the year and had used the savings to fund the restructuring. Last year we were advised that the £215k grant would be released to income and expenditure account in 2010/11. The grant was not released to income and expenditure account in 2010/11 and once again we were given the explanation that this was because other savings had been found.
BDO Conclusion
We are not able to determine if the accounting treatment of this grant is correct.

Local authority project grants
Also included within accruals and deferred income is a balance carried forward of £466k in respect of support fund grant monies disbursed by local authorities acting as agents. The creditor reduced from £596k at 31 July 2010 as management took the view that the College has fulfilled its obligations in relation to a particular contract and there was no risk of clawback. The grant terms refer to project outcomes and also levels of expenditure to be incurred by the College. As things stand, any costs incurred by the College on the projects have been covered by the income release. Management have concerns that the College costs are not as high as those detailed in the original offers and it is uncertain if the funders will wish the difference to be repaid. The projects have had no formal sign off and there has been no communication from the funders indicating any dissatisfaction. Quarterly returns have been submitted as required. The funders, we understand, can go back seven years and audit the grants.
BDO Conclusion
The College has taken a prudent view with regards to the residual balances on the contracts. The College should continue to monitor the projects and either release the relevant balance to income and expenditure account when obligations have been fulfilled or repay the relevant balance to the funders if required.

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

Revaluation of Land and Buildings

On the 31 July 2011 a revaluation of college land and buildings was performed by James Barr & Co, a firm of Chartered Surveyors. The valuation on a depreciated replacement cost basis has been incorporated into the financial statements giving rise to an increase of £2.062m in the revaluation reserve.

BDO Conclusion

We are satisfied that the revaluation has been performed by an appropriately qualified person and that the accounting for the revaluation has been correctly reflected in the financial statements in accordance with FRS 15 – Tangible Fixed Assets.

FRS 17 – Retirement Benefits

The College participates in The Strathclyde Pension Fund which is a pension providing benefits based on final pensionable pay. The College will quantify its share of the assets and liabilities of the scheme by instructing Hymans Robertson LLP to prepare an FRS 17 report for accounts purposes as at 31 July 2011. The impact on the College's balance sheet of a change in one of the many variables involved in the actuarial valuation can be substantial and the College needs to be satisfied that the assumptions used in the actuarial valuation are correct for the College.

BDO Conclusion

The actuarial assumptions used in the valuation report have been deemed to be reasonable and the College has correctly incorporated the figures in the report into their financial statements.

CORPORATE GOVERNANCE

Corporate Governance
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. The corporate governance arrangements of an organisation are the means by which strategy is set and monitored, managers are held to account, risks are managed, stewardship responsibilities are discharged and institutional sustainability is ensured. The Code of Audit Practice requires that auditors 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.
The Board of Management is required to report on its compliance with the *“UK Corporate Governance Code 2010”*.
Board of Management: has six formally constituted committees which have specific terms of reference and act with delegated authority from the Board (being the Audit Committee, Finance & Resources Committee, HR Development Committee, Learning & Teaching Committee, Remuneration Committee, and Nominations Committee). • ***Composition:*** the Board is comprised of 16 members as at 31 July 2011; hence, the Board has no more than the recommended maximum of 16 members. The skills of the members of the Board included those with relevant skills and expertise in finance, marketing, logistics, human resources and management consultancy. The College representatives include the Principal, a member of the teaching staff, a member of the support staff and the Student President. The College follows the principle that the Board has a majority of members who are external and independent (i.e. neither staff nor student of the College). The College clerk to the Board of Management is performed by Sandy Adamson, thereby meeting the best practice that the role is held by an individual who is independent of College management. The recommended maximum period of office for board members of 12 years has been adhered to. • ***Timing:*** The Board exceeded the recommendation for meeting not less than 4 times during the year, with 5 meetings in 2010/11. Therefore, the Board met at sufficiently regular intervals during the course of the year in order to discharge its duties effectively.

CORPORATE GOVERNANCE Continued…

Corporate Governance continued…

Board of Management continued…

- ***Responsibilities:*** It was noted that no one individual has unfettered powers of decision-making. Arrangements are in place to enable the chairman to hold meetings with the other non-executive governing body members without executives present when deemed appropriate.
- ***Development and Evaluation:*** Management are aware of the importance of ensuring that the new Board members have a timely induction and appropriate development programme. In their Corporate Governance report of November 2011, Henderson Loggie, the College internal auditors recommend that;
  - On an annual basis Board members development needs should be reviewed and followed up with an agreed training plan; and
  - Self evaluation questionnaires were last completed by Board of Management members during 2009. The Board recognises that a self evaluation process is required and is investigating the most appropriate method of doing this.

Audit Committee: is comprised of 5 members as at 31 July 2011. The committee, with 4 non-executives, meets the recommendation that there be at least 2 independent non-executive members. With no qualified accountants, the Audit Committee does not meet the recommendation that at least one member of the committee has recent and relevant financial expertise. It was noted that the Chair of the Board of Management was not also a member of the Audit Committee and that no member of the Audit Committee was also a member of the Finance Committee.

Remuneration Committee: is comprised of 5 members as at 31 July 2011. It is recommended that if the Chair of the Board of Management is a member of the Remuneration Committee they should not chair the committee. The College does not follow this recommendation.

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.

CORPORATE GOVERNANCE
Continued…

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 Henderson Loggie. An assessment was made of the adequacy of the internal audit output and it was concluded that we as external auditors were able to use the work of internal audit in planning our own procedures. Accordingly cognisance was made of the work of internal audit in the following areas during 2010/11:

- IT Network Arrangements
- Procurement and Creditors Purchasing
- Risk Management and Business Control
- Staff Recruitment and Retention
- Corporate Governance
- EMA, Bursaries and WSUMs

On 25 November 2011, Henderson Loggie issued the internal audit report for the year ended 31 July 2011. This concluded that the College operates adequate and effective internal control systems as defined in the audit needs assessment.

Risk Management

The Board has responsibility for the identification and management of risks facing the College. A risk assessment matrix of the exposure to risk, and the extent to which these risks are controlled, including implementation of actions to mitigate risk, is updated and presented to the Board of Management every quarter to review the College's response to identified risks. This identifies, prioritises and assesses risks to the College according to the likelihood and the impact of each risk.

CORPORATE GOVERNANCE
Continued…

Prevention and Detection of Fraud and Corruption
The College's arrangements for preventing and detecting fraud and corruption were assessed during the audit. It was noted that a fraud was uncovered in the year by the College and was alerted to the fraud response committee, who duly engaged the internal auditors to carry out an investigation into the matter. The College has in place an over-arching fraud prevention policy, in addition to a whistle-blowing policy. Both of the 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. In addition to the aforementioned policies, the College has also implemented tendering and procurement procedures to mitigate the risk of financial irregularity.

Operating and Financial Review (OFR)
The college has utilised the model style of OFR contained in the model financial statements which can be found on the SFC website. The college OFR complies with the additional guidance on the content of the OFR issued by the Scottish Funding Council on 2 October 2009. The information given in the OFR by the college is consistent with the financial statements.

PREPARATION OF THE FINANCIAL STATEMENTS

Preparation of the Financial Statements

Our Audit Planning Memorandum issued to the College in May 2011 outlined the various stages of the audit process. In relation to the key factors of the production of the financial statements, our assessment was as follows:

Completeness of Draft Financial Statements: We received a set of draft financial statements on 3rd October 2011, the first day of audit fieldwork. The draft accounts were of good quality. Most issues were resolved by the end of fieldwork and a revised draft received on 10 November 2011. Any outstanding matters were resolved prior to receipt of the final accounts and audit sign off.

Quality of Supporting Documentation: Prior to the beginning of our audit fieldwork, we issued an "Information to be Prepared by Client" request setting out the required supporting documentation to be in place for the beginning of audit field work. The supporting documentation that was received was of a high standard with few additional schedules required from the Finance staff.

Response to Audit Queries: Management provided high quality and timeous responses to all of the audit queries that were posed to them.

APPENDIX 1
Unadjusted Audit Differences

Unadjusted Audit Differences

We are required by International Standards on Auditing 260 "Communication of matters to those charged with governance" to communicate all uncorrected audit differences, other than those we clearly believe to be trivial.

Total unadjusted audit differences identified by our audit work would only alter the reported deficit by an immaterial amount. The Board of Management will need to consider the materiality of these identified misstatements in the context of the financial statements taken as a whole. These are set in the table below:

		Income & Expenditure Account		Balance Sheet	
Unadjusted Audit Differences	**£'000**	**DR £'000**	**CR £'000**	**DR £'000**	**CR £'000**
Deficit for the Year before Audit Adjustments	(519)	●	●	●	●
Reallocation of the provision for the potential non-recoverability of the fee waiver debtor	-	229	229		
Correction for over accrual of consultants costs	8		8	8	
Total Adjustments	**8**	229	237	8	0
Deficit for the Year after Audit Adjustments	**(511)**				

The matters raised in our report prepared in connection with the audit are those we believe should be brought to your attention. They do not purport to be a complete record of all matters arising. This report is prepared solely for the use of the company and may not be quoted nor copied without our prior written consent. No responsibility to any third party is accepted.

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