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Chartered Accountants

Edinburgh's Telford College

Annual Audit report for 2010/11 to the Board of Management and The Auditor General for Scotland

External Audit Report No: 2011/02

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Corporate Governance

- The Group has shown a surplus for the year of £1.185 million (2009/10 - £2.155 million surplus), against an original budgeted surplus of £0.782 million set out in the 2010 Financial Forecast Return (FFR) to the Scottish Funding Council (SFC) in July 2010. The income and expenditure account balance at 31 July 2011 was a surplus of £29.442 million (31/07/10 - £27.267 million).

- The College's internal auditors, in their annual report, concluded that 'In our opinion Edinburgh's Telford College has a framework of controls in place, in the areas which we have reviewed, that provides reasonable assurance regarding the effective and efficient achievement of the College's objectives and the management of key risks, except for the issues identified in our March 2011 report on the residences contract' (which was signed with a third party in December 2009). 'In our opinion, there were fundamental weaknesses with the College's arrangements for planning, implementing, reporting and approving this contract. Since the appointment of the new Principal and Chair of the Board, actions have been taken to address these weaknesses'.

- The College's new governance structure came into force from 1 August 2010 with the number of Board committees decreasing from eight to three, and a Shadow Governance Council was formed. A new College Governance Framework was also approved in June 2011.

- A further internal audit review of corporate governance in August 2011 reported that no major weaknesses in the College's corporate governance arrangements had been identified, that there was a clear commitment by the College to improving and developing robust governance arrangements and that the College had made significant improvements and refinements to previous corporate governance structures within a short period of time.

- The College's Corporate Governance Statement confirms that the College has been fully compliant with the principles of the UK Corporate Governance Code during 2010/11 except in the College's arrangements for planning, implementing, reporting and approving the residences contract.

- We identified no material control weaknesses during our audit. Issues noted in previous years relating to the new student records system have been largely addressed, although there were still some issues noted regarding completion of registers while undertaking the Education Maintenance Allowance (EMA) audit.

- The College has an on-going process for identifying, evaluating and managing its significant risks.

Performance

- The College reviewed its strategy and introduced a new Strategic Plan in 2010/11 based around nine strategic drivers and objectives approved by the Board of Management on 9 November 2010.

- The College reviewed its risk management processes in 2010/11 to ensure that the risk management processes and structure were fit for purpose. As a result the Corporate Risk Register was redrafted and given a new format which categorises risks against either the nine strategic drivers or a set of corporate risks. Under the new structure a Risk Assessment Monitoring Group has been set up to review risks and update the Risk Register before this is reviewed by the Shadow Governance Council and Board.

- Performance reports and information were submitted to the Board and Committees during the year. For the first time a College Self-Assessment Report was produced summarising the College's performance.

- There is an ongoing material risk to the FE sector in relation to how the global economy will perform which could affect the College's commercial and international income. In addition, the UK Border Agency's requirements for international students have been tightened, which will lead to lower international student numbers and income in future.

Financial Statements

- On 13 December 2011 we issued an audit report expressing an unqualified opinion on the financial statements of the College for the year ended 31 July 2011 and on the regularity of the financial transactions reflected in those financial statements. The audit report included an 'emphasis of matter' paragraph noting that the College did not seek the consent of the Scottish Funding Council prior to entering the occupancy guarantee arrangement with a third party, as required by the Financial Memorandum.

- The financial statements of the College comply with the Accounts Direction issued by the SFC and the Statement of Recommended Practice (SORP) on Accounting for Further and Higher Education.

- One audit adjustment was made to the unaudited financial statements which affected only the balance sheet. Further adjustments were made to disclosures in the notes to the financial statements.

- The College exceeded its WSUMs target for 2010/11 by 653 WSUMs (0.5%), (2009/10 – 699 WSUMs excess, 0.6%).

Outlook

- The future for all colleges will include change driven by funding constraints and Scottish Government plans for rationalisation of education provision to over 16s. A number of reviews and consultations are currently underway to inform change, with increased regionalisation a key message from the Scottish Government.

- The College has taken steps to prepare for the changes primarily through creating a new sustainable operating model. A review of curriculum and operations in 2010/11 led to severances and cost reductions to assist the College to remain sustainable in the future.

- The Board of Management, at its meeting on 21 November 2011, decided to enter into merger talks with Stevenson College Edinburgh and Jewel and Esk College. The decision to move towards merger is subject to satisfactory due diligence and satisfactory outcomes from a full consultation process with students, staff and key stakeholders.

HENDERSON LOGGIE

Background

1. 2010/11 was the last year of our five year appointment as external auditors of Edinburgh's Telford College ('the College'). This report summarises our opinion and conclusions and highlights significant issues arising from our work. It covers the communication of findings from the audit required by ISA 260: Communication of Audit Matters with Those Charged with Governance.

2. The framework under which we operate under appointment by Audit Scotland is as outlined in our Strategic Planning Memorandum and 2010/11 Annual Audit Plan issued on 9 May 2011 and considered and approved by the Audit Committee on 16 May 2011. The scope of the audit was to:

   - provide an opinion on, to the extent required by the relevant authorities, the financial statements and the regularity of transactions in accordance with the standards and guidance issued by the Auditing Practices Board;
   - review and report on the College's corporate governance arrangements in relation to systems of internal control, the prevention and detection of fraud and irregularity, standards of conduct, and prevention and detection of corruption; and the College's financial position; and
   - review and report on the College's arrangements to manage its performance, as they relate to the economy, efficiency and effectiveness in the use of resources.

3. Our audit approach focused on the identification of the significant risk areas facing the College and the significant classes of transactions, estimates, other account balances and disclosures impacting upon the financial statements. These include:

   - compliance with legislation and financial regulations;
   - estates capital expenditure and the appropriateness of the accounting entries;
   - recoverability of debtors;
   - achievement of the SUMs target and the impact of the current economic climate on the achievement of the College's forecast result;
   - recognition of funding provided for specific purposes and the regularity of corresponding expenditure;
   - potential issues with the student records system including the completeness and accuracy of student fee invoicing;
   - compliance with FRS 17 Retirement Benefits; and
   - compliance with the SORP on Accounting for Further and Higher Education.

Basis of Information

4. External auditors do not act as a substitute for the College's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

5. As our audit is designed primarily to enable us to form an opinion on the financial statements taken as a whole, our report cannot be expected to include all the possible comments and recommendations that a more extensive special examination would bring to light.

Acknowledgement

6. Our audit has brought us in contact with a range of College staff. We wish to place on record our appreciation of the co-operation and assistance extended to us by staff in the discharge of our responsibilities.

Corporate Governance

Financial Position

7. SFC circular SFC/31/2009, issued on 16 October 2009, defines a sustainable college as one which 'continually develops the quality of its learning activities to meet the changing needs of its customers, society and the economy, controls its costs, and year on year secures sufficient income to resource its planned activities and enable a level of current and future investment necessary to maintain its assets.'

8. Table 1 provides a summary of the College's planned and actual financial results, based on the formal FFRs submitted by the College to the Funding Council.

Table 1: Comparison of planned and actual financial results

	2009/10 Actual £000	2010/11 Planned £000	2010/11 Actual £000	2011/12 Planned £000
Financial outturn (Deficit)/Surplus	2,155	782	1,185	20
Income and expenditure reserves	27,267	26,702	29,442	27,834
Cash balances	9,619	9,883	11,849	3,444

Source: Audited accounts and 2010 and 2011 FFRs

9. Overall, College income in 2010/11 has increased by £2.403 million (7.4%) over 2009/10 to £34.670 million. The main movements are a significant increase of £1.147 million (4.6%) in SFC income; an increase in tuition fees and education contracts £0.564 million (10.6%); an increase in other grants of £0.346 million (58.0%); and an increase in Nursery income of £0.241 million (42.3%).

10. Funding Council grants have increased largely because of additional economic downturn funds being provided to the College totalling £0.907 million. There was also an increase of £0.130 million in deferred capital grants released to offset depreciation; and an increase of £0.169 million in capital formula funding released to the Income and Expenditure Account to set against bank interest, building maintenance, and minor building works.

11. Tuition fees and education contracts income has increased by £0.564 million over 2009/10 to £5.883 million largely due to increased international and higher education student numbers.

12. Other grants increased by £0.346 million to £0.943 million due to a number of factors. The Joint Information Systems Committee (JISC) was previously hosted by the College but has now been transferred to Glasgow University. As a result a number of staff took voluntary severance and deferred income of £0.186 million was released to match the costs arising. A number of grants (totalling £0.278 million) received in prior years, which were included in deferred income, were also released to income as grant terms and conditions were considered met and there was no liability for clawback. The remainder of the movement was due to changes in miscellaneous grants.

13. Nursery income increased by £0.241 million to £0.810 million (2009/10: increase of £0.162 million (39.8%)). This was due to increases in occupancy, a full year of the Nursery extension having been in place and an increase in childcare rates charged.

Financial Position (Cont'd)

14. Expenditure in 2010/11 has increased by £3.370 million (11.2%) over 2009/10 to £33.482 million. Payroll changes made up the major movements and included:
    - an exceptional FRS17 non-cash adjustment in the 2009/10 figures relating to the Government's decision to link future pension increases to CPI rather than RPI which gave rise to a past service gain, reducing 2009/10 expenditure by £1.844 million;
    - an increase in severance costs of £0.444 million as part of further College restructuring and JISC voluntary severances;
    - an increase in staff costs of £0.835 million due mainly to the 1% pay rise and 1% bonus awarded to staff during the year; and
    - a decrease in exceptional pension costs of £0.274 million because in 2009/10 the discount rate on the early retirement provision decreased which increased the exceptional pension cost. There was no such change in discount rate in 2010/11.

15. Other major movements included:
    - £0.694 million (7.7%) increase in other operating expenses. This was due largely to £0.500 million termination costs for the College's two swap agreements which were terminated because they were no longer considered to provide long-term value to the College. In addition, £0.240 million was provided for obligations under a guarantee for occupancy of residences.
    - £0.282 million (49.8%) decrease in interest payable, mainly because interest on the FRS17 net pension liabilities was an interest credit of £0.029 million rather than an interest expense (2009/10 expense of £0.196 million) and reduced interest because of lower outstanding balances and termination of the interest rate swap agreements in May 2011.

16. The main reasons for the variance between the actual financial outturn for 2010/11 of £1.185 million and the budget of £0.782 million (difference of £0.403 million) was the better than expected tuition fee income (£0.8 million) and other income (£0.6 million) less higher than expected operating expenditure (£0.5 million), higher restructuring and exceptional pension costs (£0.5 million) and lower than expected interest (£0.2 million).

17. The SFC requires external auditors to check that any severance payments to senior staff, classified as those earning more than £0.050 million per annum, meet the requirements set out in SFC guidance. We checked payroll records and noted that there were no severance payments made to staff who fell into this category.

18. The College's cash balance at 31 July 2011 was £11.849 million, an increase of £2.230 million on the previous year. This was largely as a result of the operating surplus £1.185 million along with non-cash depreciation charges (£2.702 million) being greater than capital expenditure (£0.971 million). The Board of Management is considering the best use for these funds, which may include early repayment of the College's long-term loan, which totalled £7.025 million at 31 July 2011.

2010/11 SUMs outturn

19. The College's outturn against its 2010/11 SUMs offer is shown in table 2. The 2010/11 target includes the delivery of 3,896 additional WSUMs funded by the SFC via economic downturn monies.

Financial Position (Cont'd)

Table 2: 2010/11 SUMs outturn

	2006/07	2007/08	2008/09	2009/10	2010/11
SUMs target	117,784	119,197	119,197	120,771	123,093
SUMs actual	113,126	117,673	120,203	121,470	123,746
(Shortfall) / Excess	(4,658)	(1,524)	1,006	699	653

Source: Audited SUMs returns.

20. College management has regularly monitored the level of SUMs throughout 2010/11 to ensure that the SUMs target would be achieved or was at least within the 2% leeway for under-provision against target allowed by SFC.

21. The College's internal auditors carried out the audit of the SUMs return for 2010/11. They concluded that the student data returns have been compiled in accordance with all relevant guidance, that adequate procedures are in place to ensure the accurate collection and recording of data; and, on the basis of testing, reasonable assurance can be taken that the FES return contained no material mis-statement.

FRS 17 Retirement Benefits

22. The College accounted for its participation in the local government pension scheme as a defined benefit scheme and accordingly this has resulted in the College's share of the net pension liabilities within the Lothian Pension Fund (LPF) being provided for in the balance sheet. This is consistent with the accounting treatment adopted in 2009/10.

23. Note 26 to the financial statements highlights the College's net pension liability position of £3.539 million within the LPF. This has moved significantly in the year from a net pension liability of £4.576 million at 31 July 2010. This change in financial position results from a number of changes in assumptions which are shown in table 3 below. The amount recognised in the income and expenditure account in relation to the LPF includes a net interest income on pension assets and liabilities of £0.029 million (2009/10 – £0.196 million interest expense).

Table 3: LPF financial assumptions

	31 Jul 11 % p.a.	31 Jul 10 % p.a.
Pension increase rate	2.7	2.9
Salary increase rate	5.0	4.9
Expected return on assets	6.5	6.7
Discount rate	5.3	5.4

Source: LPF actuarial valuation for FRS 17 purposes at 31 July 2010 and 31 July 2011

24. With the exception of liabilities arising from early retirement provision costs, the College is unable to separately identify its share of assets and liabilities in the Scottish Teachers' Superannuation Scheme as the scheme is notionally funded. The College has applied the concession allowed by FRS 17 and has accounted for the scheme as a defined contribution scheme.

Financial Position (Cont'd)

Capital Income and Expenditure

25. The College's new campus was completed in May 2006 with the College moving its operations to it in July 2006. A number of construction snagging issues affecting the new campus remained to be fully addressed however during the year the College came to an agreement over the defects and retention issues with the contractor which resulted in a Final Account of £0.400 million being paid out. The remaining amount of the retention held (£0.401 million) was used to reduce the value of fixed assets, as the amount of the retention had previously been capitalised.

26. During 2010/11 £0.971 million (2009/10 £0.923 million) of capital expenditure was incurred. This included £0.688 million spent on fixtures and fittings, the majority being related to the dance studio, strengthening the sports hall and refurbishment of the spa. There was also £0.120 million spent on ICT equipment and £0.117 million on equipment. Of the capital expenditure, £0.747 million was funded by Capital Grants.

Provisions

27. The College has a provision of £2.955 million at 31 July 2011 (2009/10 - £3.005 million) for early retirement pension costs. The provision relates to unfunded liabilities as a result of early retirements approved by management in previous years. The provision has been calculated using SFC approved calculation tables at a real discount rate of 2.0% (2009/10 - 2.0%).

28. The College entered into a 25 year contract (with a break option at 15 years) with Alumno Miller Telford Limited in December 2009 for the provision of student accommodation, which included an occupancy guarantee. In May 2011 the College took a case to court to have the contract reviewed and is currently awaiting the outcome of this case. The College has included a provision for £0.240 million relating to costs that may arise under this guarantee but the final amount payable will not be known until the decision of the court case is available.

Contingent liability

29. The financial statements disclose that the College has no contingent liabilities.

Systems of Internal Control

Control environment

30. We identified no material control weaknesses in the accounting and internal control systems during the 2010/11 financial statements audit which would adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

31. We found that there had been improvements made to reduce certain control weaknesses noted in the fee income system in previous years. We found that these improvements, along with the manual checks that are normally in place to ensure that fees are fully and accurately invoiced, provided reasonable assurance that the figures in the financial statements are not materially misstated.

32. Furthermore, we found that the high level of credit balances on the debtors listing reported in last year's Annual Report have reduced significantly to 564 balances (2009/10: 1,150; 2008/09 - 450). The majority of these balances relate to international students' fee deposits and an accounting adjustment has been made to correctly allocate these from Trade Debtors to the creditors section of the balance sheet.

Systems of Internal Control (Cont'd)

33. As noted in last year's Annual Report, the student records system implementation also gave rise to issues with the completeness and accuracy of attendance registers. This has the potential for significant overpayments in terms of the national guidance for bursary / EMA awards. Improvements were noted in our 2009/10 EMA audit with some system issues remaining to be addressed. Testing during our EMA audit for 2010/11 showed that these same issues remained to be addressed and we recommend that resolution of these should be given a high priority.

Internal Audit

34. Audit Scotland's Code of Audit Practice directs us to maintain effective co-ordination with internal audit and place the maximum possible reliance on their work. Scott-Moncrieff provided internal audit services to the College in 2010/11. We have reviewed the scope and extent of work performed by internal audit during the year and considered the impact of their findings and conclusions on our work, where appropriate.

35. In their annual internal audit report Scott-Moncrieff concluded that: 'In our opinion Edinburgh's Telford College has a framework of controls in place, in the areas which we have reviewed, that provides reasonable assurance regarding the effective and efficient achievement of the College's objectives and the management of key risks, except for the issues identified in our March 2011 report on the residences contract. In our opinion, there were fundamental weaknesses with the College's arrangements for planning, implementing, reporting and approving this contract. Since the appointment of the new Principal and Chair of the Board, actions have been taken to address these weaknesses'. See further comment in the Corporate Governance section below.

Corporate Governance Arrangements

36. The College has established corporate governance arrangements, with committees operating within a culture of risk management. Regular meetings of the Board of Management and its committees are held during the year at which strategic and operational matters are addressed. The College's corporate governance arrangements are described in its Corporate Governance Statement contained with the financial statements and discussed below.

37. From the start of 2010/11 the College's committee structure was amended with a Shadow Governance Council being formed and the number of committees reducing from eight to three (Audit, Nominations and Remuneration Committees). The Board of Management now meets almost monthly, with twelve meetings in 2010/11, which allows members to have a more in-depth understanding of issues facing the College.

38. A revised Code of Governance was produced by the College in June 2011. This sets out the role and remit of the Board of Management, Board committees and the Principal and Chief Executive. It also sets out the Board's constitution, membership and arrangements for performance and evaluation of Board performance.

39. A review of corporate governance failures regarding the residence contract entered into in December 2009 was undertaken by the College's internal auditors and completed in March 2011. This identified a number of areas for improvement including ensuring that business cases are robust, ensuring that challenge and monitoring is effective and adequate reporting is made from management to the Board. The College has created an action plan to address the issues noted in the report and progress is being reported to the Board on an ongoing basis.

Corporate Governance

Corporate Governance Arrangements (Cont'd)

40. An internal audit review covering College corporate governance was undertaken in August 2011 and found that adequate and effective controls were in place and operating satisfactorily in relation to the following key control objectives: the new Board, committees and Shadow Governance Council worked effectively and efficiently, with clear mechanisms in place to evaluate the revised arrangements; the revised role, remit and responsibilities of the Board, its committees and the Shadow Governance Council have been clearly articulated and communicated to all relevant stakeholders; and standards of behaviour and codes of conduct, policies and procedures are in place for Board members and staff and are duly adhered to. It also found that there was scope for improvement regarding the Board undertaking a formal and rigorous annual evaluation of its own performance and ensuring Board members have an appropriate balance of skills, experience, independence and knowledge, supplemented by induction and ongoing training.

41. On 30 September 2010 Audit Scotland published a report on The Role of Boards, which looks at the role boards play in overseeing the performance of different types of public bodies and will be of interest to College Board members. In September 2011 we completed an Audit Scotland Impact Assessment on how the College had responded to the report. We noted that the Chair of the Board and the Clerk to the Board considered the findings in the report and found that the College is now following all of the applicable recommendations made for public bodies.

42. Other sector-wide developments include the working group convened by Scotland's Colleges, the SFC and the Chartered Institute of Public Finance and Accountancy to support the development of a bespoke framework of governance for the College sector. In May 2010 the working group produced a consultation draft of a document entitled 'Delivering Good Governance in Scotland's Colleges: A Framework'. The framework is based on 'The Good Governance Standard for Public Services' and incorporates the elements of the Financial Reporting Council (FRC) 'UK Corporate Governance Code' that are relevant to the sector. It was originally envisaged that the framework would replace the 'Guide for College Board Members' published by the Association of Scotland's Colleges in 2006 however a new Guide is currently being developed as part of a separate exercise. At the present time the framework document has not been finalised and no timescale has been set for this.

43. In addition, Scottish Ministers have commissioned an Independent Review of College Governance. The review is being chaired by Professor Russel Griggs, chair of Dumfries and Galloway College board. The Review will develop recommendations which will help bring a new focus to further education governance while maintaining the important balance between accounting for public funds and preserving the benefits of an autonomous sector. The Review is expected to conclude by the end of 2011

Corporate Governance Statement

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

45. We are required to review the statement to assess whether the description of the process adopted in reviewing the effectiveness of the system of internal control appropriately reflects the process. We are not required to provide an opinion on the College's systems of internal control.

Corporate Governance Statement (Cont'd)

46. The College's corporate governance statement for 2010/11 states that the College complies with all the provisions of the June 2010 UK Corporate Governance Code, and it has complied throughout the year ended 31 July 2011, 'except in the College's arrangements for planning, implementing, reporting and approving a contract with a third party, the residences project. Since the appointment of the new Principal and Chair of the Board, actions have been taken to address these weaknesses.'

47. Our audit opinion on the statement is covered by our auditors' report and is unqualified in this respect.

Fraud and irregularity, standards and conduct, and prevention and detection of corruption

48. During 2010/11 we had regard to ISA 240: The Auditor's Responsibility to Consider Fraud in the Audit of Financial Statements.

49. The College has a Fraud Policy, Standing Orders, Financial Regulations, a Procurement Strategy and a Whistle-blowing Policy. These together with internal controls and internal audit help ensure that the College has adequate arrangements in place for the prevention and detection of fraud and corruption.

Outlook

2011/12

50. SFC funding to the College for 2011/12 is significantly lower than in previous years and has been the subject of Board discussion on several occasions, including at the Board strategy day in March 2011. As part of the budgeting process the Board considered updated information about the College's funding allocation for 2011/12. This identified revenue funding (Grant in Aid and Fee Waiver) of £20.738 million and capital funding of £0.888 million, a reduction in total of £2.606 million or 10.8%.

51. The 2011 FFR shows a budgeted 2011/12 surplus of £0.020 million (2010/11 – £0.782 million). This is based on total budgeted income of £29.379 million (2010/11 – £32.101 million) and expenditure of £29.359 million (2010/11 – £31.319 million). The actual position for the two months to the end of September 2011 shows that income is ahead of budget by £1.113 million mainly due to income being received earlier than expected and expenditure below budget by £0.386 million. Expenditure continues to be controlled across all areas.

52. In October 2009 the SFC issued guidance on developing a sustainability framework under cover of SFC/31/2009. The sustainability framework is a statement endorsed by the Board of Management to explain how and why they consider the College to be sustainable.

53. In 2009/10 the College set up a short life working group of the Senior Management Team to benchmark the College against the requirements of the circular. The working group concluded that the College was well placed in regards of having established a framework that will allow it to achieve institutional sustainability. Some areas for action were identified and a test of the underpinning theory of the College's sustainability framework and its approach to financial sustainability was undertaken by College management teams.

Corporate Governance

Outlook (Cont'd)

54. At the Board strategy day on 2 March 2011 the Board considered the College's position in light of a 10.4% funding cut for 2011/12 and further cuts in following years. The Board agreed that they would support the creation of a new sustainable model through realignment of the College. As a result of this decision the College's curriculum provision was reviewed and decisions made to remove certain courses. Managers were also asked to look at ways to reduce posts or expenditure which resulted in voluntary and compulsory severances for some staff. These changes, along with ongoing monitoring of financial information to ensure budgets are not overspent, will assist the College to remain sustainable in the future.

Beyond 2011/12

55. The future for all colleges will include change driven by funding constraints and Scottish Government plans for rationalisation of education provision to over 16s. A number of reviews and consultations are currently underway to inform change.

56. Scottish Government proposals indicate that funding mechanisms will be simplified in future, possibly as early as 2012/13. Funding will follow regional need, based on demography and economy, rather than continue to follow previous patterns based on historic performance. Rationalisation of course provision and removal of duplication is expected to be achieved through closer working or mergers of institutions.

57. The College has taken several steps to prepare for the changes as noted above.

58. The Edinburgh Colleges collaboration project decided in 2009/10 against a merger of the three colleges involved in the project (Edinburgh's Telford College, Stevenson College Edinburgh and Jewel and Esk College). It was agreed to progress work in the areas of governance arrangements (identifying the structures to underpin collaboration activity), curriculum vision for 2015 and reviewing corporate services. At its 14 December 2010 meeting the Board discussed collaboration further and agreed that it would seek to develop partnerships with organisations, including the other two Edinburgh colleges, where mutual benefit exists to all parties and also to learners. However, the Board of Management, at its meeting on 21 November 2011, subsequently decided to enter into merger talks with Stevenson College Edinburgh and Jewel and Esk College. The decision to move towards merger is subject to satisfactory due diligence and satisfactory outcomes from a full consultation process with students, staff and key stakeholders.

Performance

Introduction

59. The terms of appointment from Audit Scotland include a requirement for a proportion of our audit time to be spent on performance audit work. Performance audit work covers a variety of areas, both financial and non-financial, including both Audit Scotland centrally directed studies and locally determined studies based on agreement between each organisation and their auditors.

60. No mandatory performance audit studies were identified by Audit Scotland for the College during 2010/11. Audit Scotland's planning guidance identified optional follow-up work on improving public sector purchasing and the use of consultancy services. This was discussed with management but neither follow-up was undertaken. One impact assessment was completed as required and noted in paragraph 41.

Strategic Plan

61. The College has a new Strategic Plan which was approved by the Board of Management on 9 November 2010. The College is also reviewing its strategic drivers.

Risk Management

62. The College's risk management framework is set out within the College's Governance Framework issued in June 2011. This includes setting out the roles and responsibilities of the Board of Management, College Principal and Chief Executive, and other key parties.

63. The system of internal control is designed to incorporate risk management, which together with other elements, facilitates the efficient and effective operation of the College and enables it to react to a variety of operational, financial and commercial risks.

64. In 2010/11 the risk management process was reviewed and amended as a result of suggestions made at the September 2010 Audit Committee. Prior to May 2011 risk management was part of the Shadow Governance Council where the risk register was reviewed quarterly and reported to the Audit Committee. The Audit Committee reviewed the risk management process and agreed that the new process would involve a Risk Assessment Monitoring Group that would meet monthly to review the Risk Register. The Shadow Governance Council and Audit Committee still review the Risk Register at their meetings.

65. The Corporate Risk Register before May 2011 was drawn up using links into the College's objectives through the four balanced scorecard categories. Risk ratings were provided, risks were ranked and mitigating controls were described. The new Corporate Risk Register is in a different format and is linked into the nine strategic drivers and a set of corporate risks. Identified risks are ranked based on likelihood and impact. Identified controls are documented and risks are assigned to risk owners.

Performance management

66. In developing their operational plans each department has agreed key performance indicators (KPIs) which they are responsible for reviewing progress against during the year.

67. The Board of Management receives reports on the College's performance in implementing its strategic aims and objectives. At the December 2010 Board of Management meeting the College produced it's first College Self-Assessment Report (SAR) to allow the Board and other stakeholders to review the College's strengths and identify areas for improvement. The SAR included a summary of all Course Team Self-Evaluations and key student data such as student retention rates.

68. Finance KPIs are reported as part of the management accounts which are provided to the Shadow Governance Council and the Board.

Performance

Financial management

69. Monthly management accounts were prepared and reviewed by the Finance team, except for the first two months of the year when the post of Financial Controller was vacant. A summary of the management accounts, including a variance analysis, was provided to the Shadow Governance Council and Board for review during 2010/11. The College's arrangements in relation to its key financial risks include the regular review of the Risk Register and performance against agreed financial KPIs. Reporting and tracking of the SUMs position is carried out on a regular basis.

70. Due to vacancies in staff posts a consultant was used to set the 2010/11 budget. This was set using a historical cost basis. The 2010/11 budget was approved at the Board of Management on 15 June 2010.

71. As previously stated, the 2011 FFR to the SFC shows a surplus for 2011/12 of £0.020 million and small surpluses are expected in the following two years.

72. There is an ongoing material risk to the FE sector in relation to how the global economy will perform which could affect the College's commercial and international income. Furthermore, changes in the UK Border Agency requirements for international students means that international student numbers will decrease in 2011/12 and in future years.

73. A new Finance Strategy was approved by the Board on 14 December 2010. This aims to achieve long term financial sustainability through setting out specific objectives, the responsibility for undertaking key actions in support of these objectives, and setting out monitoring arrangements.

Value for Money (VFM)

74. A new Achieving Public Value Strategy, which sets out how the College will ensure value for money, was approved by the Board of Management on 14 December 2010. This includes sections on collaborative procurement, partnerships, student retention and efficient use of resources.

75. The College's internal auditors did not undertake any specific value for money reviews during 2010/11 however value for money aspects are built into each of their reviews.

76. The College has implemented the ordering module of PECOS from 2011/12. This software is used by the Scottish Government and has been rolled out to public sector bodies throughout Scotland in order to obtain greater VFM in purchasing.

Financial Statements

Audit Opinion

77. On 13 December 2011 we issued an audit report expressing an unqualified opinion on the financial statements of the College for the year ended 31 July 2011 and on the regularity of the financial transactions reflected in those financial statements. The audit report included an 'opinion on other matter' paragraph noting that the College did not seek the consent of the Scottish Funding Council prior to entering the occupancy guarantee arrangement with a third party, as required by the Financial Memorandum.

Audit Completion

78. An important measure of proper financial control and accountability is the timely closure and publication of audited financial statements. We have summarised in table 4 the three key elements of the audit process that we require the College to engage with.

Table 4: Key elements of the audit process

Completeness of draft financial statements A set of draft financial statements was received on 19 September 2011, seven days in advance of the final audit visit, with a number of financial disclosures still to be finalised. Overall, these financial statements were of a good standard, but required a number of changes because 10 audit journals proposed by the College had not been processed within the first draft. An updated draft of the financial statements incorporating the agreed audit adjustments was received on 28 October 2011.
Quality of supporting working papers In accordance with our normal practice, we issued a 'prepared by client' request that set out a number of documents required for our audit of the financial statements. A largely complete set of supporting working papers were provided in line with this list at the outset of the audit with the remaining working papers provided during the fieldwork. These were generally of a high standard.
Response to audit queries Most audit queries were dealt with in a timely manner, with a small number of matters taking longer than expected to receive answers to.

Audit Adjustments and Confirmation

79. Two potential adjustments were identified during the course of the audit which were discussed with the Head of Financial Services and the Financial Controller on 6 October 2011 and it was agreed to adjust the financial statements for one of these. In table 4 we draw your attention to this agreed audit adjustment. The value of the unadjusted misstatement was £57,059 which would have increased the surplus for the period by £57,059 and reduced provisions by £57,059.

Table 4: Audit adjustment

Description	**I&E DR £'000**	**I&E CR £'000**	**B/Sheet DR £'000**	**B/Sheet CR £'000**
Accruals – residences contract			240	
Provisions – residences contract				240
Presentation adjustment to disclose the residences contract provision under Provisions for Liabilities and Charges rather than Accruals				
	0	0	240	240

80. In addition, a number of disclosure and clarification adjustments were made to the accounts to ensure SORP and Accounts Direction compliance and improve the overall presentation of the accounts.

Confirmations and Representations

81. We confirm that as at 13 December 2011, in our professional judgement, Henderson Loggie CA was independent within the meaning of regulatory and professional requirements and the objectivity of audit staff was not impaired.

82. In accordance with auditing standards, we obtained representations from the College on material issues.