Angus College

Annual audit report to the Board of Management of Angus College and the Auditor General for Scotland

Year ended 31 July 2012

31 January 2013

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Audit status and key audit issues

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice* ("the *Code*"). This specifies a number of objectives for the audit; our audit strategy set out our responsibilities in respect of the audit. The board of governors' responsibilities are set out in appendix one.

This report summarises our work for the year ended 31 July 2012. It also provides information required by International Statements on Auditing (UK and Ireland) 260: *Communication with those charged with governance.*

We wish to record our appreciation of the co-operation and assistance extended to us by College staff during the course of our work.

Issue	Summary	Page
Audit status	Our audit is now complete and we have issued unqualified audit opinions for the year ended 31 July 2012, following the approval of the financial statements by the Board of Management.	9
Financial position	The surplus for the year was £13,000 (2010-11 deficit: £9,000). The increase is mainly due to a decrease in grant income and lower staff costs as a result of voluntary severance schemes in prior years.	10
Audit issues identified	Under the requirements of ISA (UK and Ireland) 260: *Communications with those charged with governance*, we are required to report any material adjusted and unadjusted audit differences arising from our work. Adjustments were required in respect of accounting for the College's participation in the local government pension scheme on a defined benefit basis, an element of unfunded pension liabilities which had been double counted, the classification of cash and investments and deferred income. Pension assumptions adopted by management, on the basis of advice of their actuaries Barnett Waddingham, in the draft financial statements were outside our generally acceptable range as at 31 July 2012, particularly in respect of the net discount rate of 1.9% compared to our central assumption of 2.5%. Our calculation of the most likely difference arising in the gross pension liabilities as a result of this difference was not material and management confirmed that no adjustment would be processed.	4, 6, 23
Performance improvement observations	We have identified four performance improvement observations which we are required to bring to your attention. All observations are 'low' graded observations. We have raised recommendations in regard to identifying expenditure against specific grants, enhancement to the corporate governance statement, receipt and distribution of circulars and evidence of review of reconciliations.	17

Introduction

Background

The purpose of this report is to set out certain matters which came to our attention during the course of our audit of the financial statements of Angus College ("the College") for the year ended 31 July 2012.

The purpose of our audit

The main purpose of our audit which is carried out in accordance with International Statements on Auditing (ISAs) (UK and Ireland) issued by the Auditing Practices Board, is to report to the board of governors and Auditor General for Scotland on whether in our opinion the financial statements:

- give a true and fair view of the state of the affairs of the College as at 31 July 2012 and of the College's income and expenditure, recognised gains and losses and cash flows for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice;
- have been prepared in accordance with the Statement of Recommended Practice: Accounting for Further and Higher Education; and
- the expenditure disbursed and income received during the year ended 31 July 2012 have been applied to purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Management letter

Our objective is to use our knowledge of the College gained during our routine audit work to make useful comments and suggestions for you to consider. However, you will appreciate that our routine audit work is designed to enable us to form the above audit opinions on the annual financial statements of the College and should not be relied upon to disclose errors or irregularities which are not material in relation to those financial statements. All issues raised in the report have been discussed with management and we have included responses where appropriate in the action plan. In order to provide an indication of the level of importance of the recommendations made, we have prioritised our recommendations on the basis shown in the action plan.

Independence

ISA (UK and Ireland) 260:*Communication with those charged with governance'* requires us to communicate at least once a year regarding all relationships between KPMG and the College that may be reasonably thought to have bearing on our independence.

KPMG conforms to the highest governance standards at all times and we will ensure that any additional services are approved by the audit committee to ensure transparency. No additional services have been provided in respect of the year ended 31 July 2012.

Accounting policies; accounting matters

The financial reporting framework, as required by the Scottish Funding Council's Accounts Direction, remains the Statement of Recommended Practice: *Accounting for Further and Higher Education* (2007).

An audit adjustment was required in respect of deferred income.

Accounting policies	The accounting policy relating to pensions was updated during 2011-12. Financial reporting standard 17 *Retirement benefits* ("FRS 17") paragraph nine states that '*Where more than one employer participates in a defined benefit scheme the employer should account for the scheme as a defined benefit scheme*'. Previously, the College's board of governors accounted for its participation in the scheme on a defined contribution basis, as they believed they were unable to identify the College's share of the underlying assets and liabilities in the fund on a consistent and reasonable basis and could therefore apply the multi-employer exemption. Following consideration of the actuary's analysis and discussions, management has confirmed that the exemption was not valid. A summary of the College's share of the scheme assets and liabilities was received which has been used to restate the balances in the financial statements in respect of 2010-11 and to account for the College's participation in the scheme on a defined benefit basis in 2011-12. We reviewed the College's basis for excluding Angus College Charitable Trust ("the Trust") from the financial statements based on materiality. The basis of accounting policy was enhanced to clarify the College's role in respect of the Trust and its exclusion from the financial statements. A number of minor enhancements were made to existing policies to ensure full compliance with the Statement of Recommended Practice: *Accounting for Further and Higher Education* (2007) ("SORP"). In our view, the accounting policies for the College remain appropriate.
Financial reporting framework	The College prepares financial statements in accordance with the Accounts Direction issued by the Scottish Funding Council. In turn, this requires application of the SORP.

Accounting policies; accounting matters

Deferred income	Deferred income as at 31 July 2012 was £0.5 million. This primarily comprises grant income received from the Scottish Funding Council and other bodies which has not yet been applied. Included within deferred income is capital funding, together with Scottish Funding Council grants received in 2003-04 and 2004-05 relating to financial security which have yet to be fully utilised. Following the College's review of deferred income balances, the draft financial statements were amended to recognise additional income of £27,000 in respect of Scottish Funding Council financial security grants received in 2002. As part of our audit we considered the controls and processes in respect of significant sources of grant income, including inspecting original award documentation and review of the expenditure incurred and reported to the awarding bodies. As a result of the above procedures an audit adjustment was processed by management to transfer £0.13 million from deferred capital grants to deferred income (appendix two). Management's process for recording income and expenditure against specific grants includes allocating a separate financial ledger code to each grant, with associated expenditure also entered against this code. While this process is reasonable and, on an annual basis an overall review of deferred income balances is completed, this process could be enhanced by ensuring the annual review is evidenced as subject to independent review by senior management. ***Recommendation one***

Accounting policies; accounting matters (continued)

The College has changed accounting policy in 2011-12 in respect of its participation in the Tayside Superannuation Scheme. The multi-employer exemption is no longer applied and the scheme is accounted for on a defined benefit basis.

Retirement benefits

In 2011-12, the board of governors changed the accounting policy in respect of participation in the Tayside Superannuation Scheme. The multi-employer exemption is no longer applied as the board of governors are content that the College's actuaries are able to identify the College's share of scheme assets and liabilities on a consistent and reasonable basis. The College has therefore recognised the actuarial valuation of the pension liabilities in respect of its share of the scheme within the financial statements and accounted for its participation in the scheme on a defined benefit basis.

No such requirement exists for Scottish Teachers' Superannuation Scheme obligations as this is a multi-employer scheme where the individual assets and liabilities cannot be separately identified for each employer and therefore accounted for as a defined contribution scheme under the provisions of FRS 17.

In the draft financial statements, the College continued to account for unfunded liabilities forming part of the scheme under FRS 12, included within provisions for liabilities and charges. The College's actuaries also valued the unfunded liabilities which were therefore included in the FRS 17 liabilities. An audit adjustment was processed to remove £1.02 million from provisions for liabilities and charges.

Balance sheet (£ 000)	2012	Movement in deficit (£ 000)	2012
Assets	6,918	Employer contributions	(390)
Liabilities	(11,410)	Income & expenditure account charge	389
Net (liabilities)	(4,492)	Past service (costs)/gains	0
		Net interest cost on pension asset	92
		Actuarial loss	175

Source: 2011-12 financial statements

Total pension cost for the year, including Scottish Teachers' Superannuation Scheme contributions and the net interest cost, was £854,000, compared to £952,000 in 2010-11. The net FRS 17 pension liability has increased by £266,000 at 31 July 2012 compared to 2011. The movement in the pension deficit over 2011-12 is largely due to a reduction in the value of the schemes' assets.

Accounting policies; accounting matters (continued)

Pensions assumptions adopted by the College as at 31 July 2012 are strong than we would expect but we have agreed that the most likely difference in the net pension liability as at 31 July is not material.

Retirement benefits	Pension assumptions adopted by the College are selected by the board of governors, based on the advice of their actuarial advisors, Barnett Waddingham. During the course of the audit we challenged the actuarial assumptions used. Overall, the assumptions adopted by the College in the draft financial statements, were outwith our generally accepted range. In particular, the net discount rate (comprising the difference between the discount rate and consumer price index) was lower than we would expect. This results in a higher pension liability. Following discussion with management, we agreed with management's view that the difference arising in the net pension liability, based on the assumptions adopted by the College compared with our expected range, did not result in a material difference in the liability as at 31 July 2012. Based on our calculations the most likely difference arising in the net liability is £228,000. Further analysis of the College's assumptions is provided in appendix three.

Accounting policies; accounting matters (continued)

The College has indicated that it supports the regionalisation reforms and is committed to merging with Dundee College.

Sector, organisational and structural changes	Building on its pre-legislative paper, 'putting learners at the centre', the Scottish Government initiated a joint consultation process together with the Scottish Funding Council in November 2011 which outlined a vision for regional groupings of colleges, focussed on achieving set outcomes. The College's longer term 2020 Vision of Achieving Excellence was to be delivered against three forecast economic contexts, each calling for different approaches: ■ 2010-11 to 2012-13 – a period of resilience; ■ 2013-14 to 2015-16 – a period of growing ambition; and ■ 2016-17 to 2019-20 – a period of realising ambition. During 2011-12 the process of regionalisation has begun and on 19 September the board of governors agreed that the preferred option in respect of regionalisation was to progress merger talks with Dundee College. The key principle of taking forward this merger will be to build on the individual strengths of the colleges and create a new ambitious institution aimed at enhancing the opportunities for future learners in the Dundee and Angus regions. The colleges are in the process of undertaking due diligence prior to the merger, including the appointment of a project manager. Both College executive teams meet regularly and future meetings are planned between respective managers. It is envisaged that the merger will be concluded by November 2013.
Compliance with tax authorities	Consistent with our understanding of the College, no significant activities were undertaken by the College which we would expect to be subject to tax. We liaised with our tax compliance colleagues and have not identified any significant matters relevant to the audit which have not been appropriately reflected.
Opening balances	International Standard on Auditing (UK and Ireland) 510: *Initial audit engagements – opening balances ("ISA 510")* requires us as auditors to obtain sufficient appropriate audit evidence about whether: ■ opening balances contain misstatements that materially affect the current period's financial statements; and ■ appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes are appropriately accounted for, presented and disclosed in accordance with the applicable financial reporting framework. We have undertaken a number of specific procedures to allow us to confirm a selection of opening balances per ISA 510. Following discussion with management the presentation of cash and short-term investment balances were adjusted, together with the prior year comparative figures. There was no net impact on the balance sheet as at 31 July 2011 or 2012.

Financial statements preparation and audit process

Draft financial statements were provided on the agreed start date for on-site fieldwork. A comprehensive auditor's file was provided in support of the draft financial statements.

Area	Comments
Financial statements preparation process	■ Draft financial statements and supporting documentation were provided on 30 September 2012, in line with the agreed timetable. ■ Finance staff responded to our questions quickly and provided high quality information to support the financial statements. ■ Overall, management adopts an efficient approach to preparing the financial statements.
Corporate governance statement and operating and financial review	The draft corporate governance statement was provided on 1 October 2012 together with the operating and financial review ("OFR"). We reviewed these documents in line with the requirements of the SORP and the Accounts Direction and suggested a number of enhancements, which were accepted by management. ***Recommendation two***
Audit differences	
Under the requirements of ISA (UK and Ireland) 260: *Communication with those charged with governance*, we are required to report any adjusted audit differences arising from our work. During the course of our audit we identified audit differences summarised in appendix two. The net impact of these adjustments was to decrease the College's surplus by £233,000. Management identified one adjustment related to deferred income which increased the College's surplus by £27,000.	

Financial position

This section of our report summarises the main features of the financial statements and key movements from the prior financial year.

Income and expenditure account

Income and expenditure account		
£000	**2012**	**2011**
Income		
Funding council grants	8,589	9,720
Tuition fees and education grants	2,128	2,338
Other grant income	246	243
Other operating income	736	675
Interest receivable	109	81
Total income	**11,808**	**13,057**
Expenditure		
Staff costs	8,375	9,134
Other operating expenses	2,591	3,067
Depreciation	741	790
Pension scheme net interest cost	90	79
Total expenditure	**11,797**	**13,070**
Surplus/(Deficit) for the year	**11**	**(13)**
Disposal of fixed assets	2	4
Surplus/(Deficit)	**13**	**(9)**

Source: 2011-12 draft financial statements

Result for the year

The College made an overall surplus of £13,000 (2010-11: £9,000 deficit).

Total income decreased by £1.25 million.

- This decrease was predominantly due to a reduction in Scottish Funding Council grants which have decreased by £1.13 million, compared with the prior year. The majority of this decrease was in relation to the recurrent grant.
- Tuition fee and education grants have declined primarily due to timing of income received in respect of education contract income.

Expenditure has decreased by £1.27 million when compared to 2010-11:

- Staff costs have decreased by £0.76 million as a result of annual savings arising from the voluntary severance exercises carried out in 2010-11. This is despite exceptional staff costs relating to severance of £0.3 million in 2011-12.
- Other operating expenses have decreased by £0.48 million. This is primarily due to a decrease in other expenses, mainly relating to unfunded pension costs which are £0.41 million higher in 2011-12 than in 2010-11.

Financial position (continued)

Adjusted result for the year

A number of significant items have had an impact on the surplus for both 2011-12 and 2010-11; these are analysed in the table below, which shows the adjusted operating surplus after removing them, on a consistent, comparable basis.

£'000	2012	2011
Surplus/(Deficit) for the year	13	(9)
Restructuring costs	304	431
Net FRS 17 pension costs	91	103
Operating surplus for the year	**408**	**525**
Adjusted operating surplus as a % of total income	**4.1%**	**4.0%**

The College has generated a strong adjusted surplus as illustrated above. The adjusted position for 2011-12 is marginally higher than the 2010-11 position, however total income was lower in 2011-12.

Financial position (continued)

Balance sheet

Balance sheet as at 31 July		
£000	**2012**	**2011**
Fixed assets		
Tangible assets	13,504	13,529
Current assets		
Stocks	3	4
Debtors: Amounts falling due within 1 year	1,149	1,189
Cash at bank and in hand	953	1,039
Short term investments	3,542	3,545
Creditors: Amounts falling due within 1 year	(2,040)	(1,905)
Total assets less current liabilities	**17,111**	**17,401**
Net pensions liability	(4,492)	(4,226)
Net assets including pension liability	**12,619**	**13,175**
Deferred capital grants	7,384	7,778
Reserves		
Income and expenditure reserve (including pension reserve)	1,080	1,115
Revaluation reserve	4,155	4,282
Total funds	**12,619**	**13,175**

Source: 2011-12 draft financial statements

The balance sheet shows a fall in net assets, including pension liability of £0.56 million.

The key changes in the balance sheet were as follows:

- Fixed asset additions of £0.72 million were offset by the annual depreciation charge (£0.74 million). Additions include £0.25 million in respect of assets in course of construction.
- Cash at bank and in hand has decreased by £0.09 million; short-term investments remained relatively consistent.
- Debtors include £0.79 million in prepaid property leases (2010-11: £0.82 million). This relates to the 30 year lease agreement between the College and Angus Council for the use of the sports facility in the Saltire Leisure Centre in Arbroath. There are 25 years remaining under this lease and the prepayment will continue to reduce over the remaining term.

Financial position (continued)

Budget 2012-13

The financial statements have been drawn up on the basis that the College is a going concern and will continue as such for the foreseeable future.

The following table summarises the actual 2011-12 and forecast 2012-13 income and expenditure .

Forecast (at October 2012)		
£000	**2011-12**	**2012-13**
Income	11,808	10,810
Expenditure	(11,797)	(10,699)
Surplus/(Deficit) on continuing operations	**13**	**111**

The original budget prepared by the College for 2012-13 forecast a surplus of £6,000. The increase in the forecast outturn is primarily due to an increase in expected funding from Skills Development Scotland new college learning programme.

While the College is forecasting an increase surplus in respect of the year ending 31 July 2013, there remains uncertainty over future Scottish Funding Council grant allocations, which, despite improvement in the percentage of income from non Scottish Funding Council sources (2011-12: 27.3%, 2010-11: 25%), form the most significant element of the College's income.

The College has a capital allocation in 2012-13 of £340,000, around 50% of the approved capital plan. The College has made good progress in completing capital projects which are around 70% complete following the summer works programme.

Performance against targets

Performance indicators

In accordance with Scottish Funding Council requirements, the College is required to publish and report progress against national priorities. These indicators monitor the implementation of the College's financial objectives.

KPI	Purpose	Actual 2010-11	Actual 2011-12
WSUMs	Number of wSUMS per year	49,500	48,000
Prompt payment to suppliers	Measures the average time taken to pay supplier invoices	38 days	49 days
Non SFC income a % of income	Measures non SFC income as a % of total income	25.5%	27.3%
Gearing	Measures the reliance on debt finance	0%	0%
Current assets : current liabilities	Measures the College's ability to pay its current liabilities	3:1	2.9:1
Days cash	Cash divided by total expenditure less depreciation expressed in days	136	152

Source: 2011-12 draft financial statements

Student numbers / Weight Student Units of Measurement ("wSUMs")

The activity target set by the Scottish Funding Council for 2011-12 was 38,776 wSUMs. This target was achieved. The College delivered around 48,000 wSUMs in 2011-12, significantly more than the target set by the Scottish Funding Council.

Corporate governance framework and supporting arrangements

Over-arching and supporting corporate governance arrangements continue to provide a sound framework for organisational decision-making.

Corporate governance and internal control arrangements	The College has made a compliant corporate governance statement. We are required to review this to assess whether the description of the process adopted by the College in reviewing the effectiveness of the system of internal control is consistent with our understanding of the process and report any inconsistencies in our opinion. We are not required to provide an opinion on the College's system of internal control.
Standards of conduct and prevention and detection of corruption	The College has established appropriate processes for the prevention and detection of corruption.
Statement of corporate governance and internal control	The statement of corporate governance and internal control provides detail on the governance framework, the system of internal control, internal audit, internal financial controls and risk management arrangements, and analyses the effectiveness of these elements of the framework. It describes a number of sources of assurance for the accountable officer. We have reviewed the statement of corporate governance and consider it consistent with our understanding of the process followed by the College during the year. We reviewed the report in line with the requirements of the SORP and the Accounts Direction and proposed a number of enhancements, which were accepted by management. The statement could be further enhanced to ensure disclosure is fully in compliance with the UK Corporate Governance Code by including details of members' attendance at individual board and committee meetings.
Internal audit	As set out in our audit plan and strategy, we reviewed the work of internal auditors, Henderson Loggie, in 2011-12. The content of the internal audit plan is, in our view, appropriate for the size and nature of the College. Internal audit completed their planned audit work for the year and concluded that "*In our opinion the College operates adequate and effective internal control systems as defined in the ANA. Proper arrangements are in place to promote and secure value for money.*" Due to the areas of focus of internal audit in the year, we did not place specific reliance on any the reports issued in the year, but they assisted our understanding of the College's operations and overall systems of internal control.

Corporate governance framework and supporting arrangements (continued)

Prevention and detection of fraud	■ Procedures and controls related to fraud are designed and implemented effectively. Expenditure is reviewed and authorised by appropriate finance personnel and senior management. ■ In 2011-12 no significant or other fraud or irregularity was identified by management, internal audit, or through the course of our external audit work. ■ Policies and procedures have been updated in response to the Bribery Act 2010.

Observations arising from our audit

#	Risk	Issue, impact and recommendation	Management response/ responsible officer/due date
1	Low	Management's process for recording income and expenditure against specific grants includes allocating a separate financial ledger code to each grant, with associated expenditure also entered against this code. The College's deferred income balances are significant and their application and release can be subject to an element of judgement which could affect the outturn in the financial statements. We recommend that this process is enhanced by ensuring that the annual review of deferred income which is completed, is evidenced as subject to independent review by senior management.	Agreed. Finance Manager. July 2013.
2	Low	The Statement of Corporate Governance could be further enhanced to ensure compliance with best practice. We recommend that, in line with the UK Corporate Governance Code, information is updated to include details of members' attendance at individual board meetings and committees.	Agreed. Finance Manager. Immediate.
3	Low	The College receives SFC circulars on a regular basis, which may require management action or should be distributed to ensure staff are aware of any relevant guidance. The College has a set process for receiving and actioning circulars, but does not maintain a formal register, there is a risk relevant guidance is not circulated and the College fails to adhere to the terms of funding. We recommend that all circulars received should be logged and the log used as a checklist to confirm their distribution and audience within the College.	The existing procedure will be subject to review, to consider the feasibility of the use of a register. Depute Principal. January 2013.
4	Low	Student fees invoices are raised in the SITS system. These are entered into the ledger via an import initiated by staff. On completion of the import, an error report summarises data which has not been correctly processed which is reviewed by staff. No evidence of management's review is retained. We recommend that the reconciliation between SITS and the general ledger is completed and evidenced as such.	Agreed. Finance Manager. Immediate.

Key:

- Low risk – matters that merit attention and would improve overall control.
- Medium risk – matters that are considered significant, that should be addressed within three to six months; and
- High risk – matters that are considered fundamental, against which management should take action as soon as possible;

Best Value

We have considered arrangements to achieve Best Value and regularity of income and expenditure.

Audit area	Overview	Findings
Best Value	In April 2002 the Scottish Ministers introduced a non-statutory duty on accountable officers to ensure arrangements exist to secure Best Value. Audit Scotland has been committed to extending the Best Value audit regime across the whole public sector for some time now. Using the Scottish Executive's nine Best Value principles as a basis for audit activity, Audit Scotland previously selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working). A series of toolkits covering financial, performance and governance processes are available for public sector organisations and auditor to use, but auditors were not required to complete specific toolkit(s) in 2011-12.	We reviewed some of the processes management has established to ensure Best Value is achieved throughout the organisation. The College produces quarterly management accounts which compare actual expenditure to budget. The College has a procurement strategy and seeks to use the most advantageous supplier that is available.
Regularity	As part of our audit of the College's financial statements, we are required by the Public Finance and Accountability (Scotland) Act 2000 to give an opinion on the regularity of expenditure and receipts shown in the financial statements.	The executive team 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.

Appendices

Audit Scotland code of audit practice – responsibilities of the Board of Governors

Financial statements

Audited bodies' financial statements are an essential part of accounting for their stewardship of the resources made available to them and their performance in the use of those resources. Audited bodies are responsible for:

- ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority;
- maintaining proper accounting records;
- preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the relevant financial reporting framework (eg, the Financial Reporting Manual or an Accounting Code of Practice);
- preparing and publishing with their financial statements an annual governance statement, statement on internal control or statement on internal financial control and a remuneration report; and
- preparing consolidation packs and, in larger bodies, preparing a Whole of Government Accounts return.

Systems of internal control

Audited bodies are responsible for developing and implementing systems of internal control, including risk management, financial, operational and compliance controls. They are required to conduct annual reviews of the effectiveness of their governance, systems of internal control, or internal financial control, and report publicly that they have done so. Such reviews should take account of the work of internal audit and be carried out by those charged with governance, usually through bodies' audit committees.

Prevention and detection of fraud and irregularities

Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions;
- developing and implementing strategies to prevent and detect fraud and other irregularity;
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity; and
- participating, when required, in data matching exercises carried out by Audit Scotland.

Standards of conduct and arrangements for the prevention and detection of bribery and corruption

Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and should put proper arrangements in place for:

- implementing and monitoring compliance with appropriate guidance on standards of con duct and codes of conduct for members and officers;
- promoting appropriate values and standards; and
- developing, promoting and monitoring compliance with standing orders and financial instructions.

Summary of audit differences

There were three audit difference identified. This had the net affect of decreasing income by £233,000.

We identified a number of presentational matters during our audit and these have all been amended by management.

We are required by ISA (UK and Ireland) 260: *Communication with charged with governance* to communicate all uncorrected misstatements, other than those that we believe are clearly trivial, to the audit committee. We are also required to report all material misstatements that management has corrected but that we believe should be communicated to the audit committee to assist it in fulfilling its governance responsibilities.

This appendix sets out the audit differences that we identified during the course of our audit for the year ended 31 July 2012.

Misstatements that management have corrected

The following table shows differences identified during the course of the audit of the College's financial statements for which the statements have been adjusted.

College				
£000	**Income and expenditure account**		**Balance sheet**	
Unspent deferred capital grants	**Dr**	**Cr**	**Dr**	**Cr**
Deferred capital grants	-	-	130	-
Deferred income	-	-	-	130
Short term investment disclosure				
Cash and bank in hand	-	-	-	3,542
Short term investments	-	-	3,542	-
Removal of pension provision				
Provision for liability and charges	-	-	1,018	-
Income and expenditure reserve	-	-	-	1,251
Other operating expenses	233	-	-	-
Overall impact	**233**	**-**	**4,690**	**4,923**

Presentational adjustments

We identified a small number of presentational issues during our audit and these have all been amended by management.

Summary of audit differences (continued)

There was one unadjusted audit difference identified. This had the no net affect on income and expenditure and is not considered material.

Misstatements that are uncorrected

The following table shows differences identified during the course of the audit of the College's financial statements for which the statements have not been adjusted.

College				
£000	**Income and expenditure account**		**Balance sheet**	
Pension adjustments	**Dr**	**Cr**	**Dr**	**Cr**
Pension liability	-	-	228	-
Pension reserve	-	-	-	228

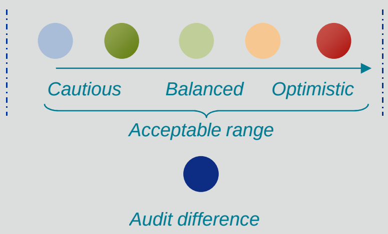
The above adjustment is in relation to pension assumptions within appendix three. We do not consider the above misstatement to be material.

Pensions considerations

Presented below is a comparison of the assumptions used by Barnett Waddingham who advise the College in respect of the Tayside Superannuation Scheme, alongside the typical assumptions we would anticipate in relation to each aspect:

Assumptions	Employer	KPMG central	Assessment	KPMG comments
Overall				The overall assumptions proposed were stronger than we normally consider acceptable. The estimated impact of increasing the net discount rate by 0.1% to the bottom of our acceptable range (2.2%) would be a reduction in liabilities of £228,200.
Discount rate	3.90%	4.40%		The proposed discount rate is stronger (higher liability) than our central rate and is below the range we would normally consider acceptable. However, the assumption is not viewed in isolation, but considered as part of the net discount rate.
RPI inflation	2.60%	2.90%		The assumption is slightly weaker (lower liability) than our central rate, but is within a range we would normally consider acceptable.
CPI inflation / Pension increases	1.80% RPI less 0.8%	1.90% RPI less 1.0%		The assumptions is slightly weaker (lower liability) than our central rate and is outside the range we would normally consider reasonable.
Net discount rate (Discount rate – CPI)	2.10%	2.50%		The range we would normally consider reasonable for the purposes of FRS17 as at 31 July 2012 is 2.5% +/-0.3%, for a scheme with liabilities with a duration of 20 years. The net discount rate is stronger (higher liability) than we consider acceptable.
Salary growth	4% after March 2015, before then 1%	1-2% above RPI inflation		The assumptions is in line with the requirements of FRS17.
Life expectancy Current male pensioner (age 65) Future male pensioner (age 45)	 20.6 years 21.8 years	 22.1 years 23.4 years		The mortality assumptions proposed are those used for the most recent signed off formal actuarial valuation, which is a reasonable approach.
Expected return on equities	Estimated ERP 5.9%	ERP 2-4.5%		The proposed assumption gives a return (or 'equity risk premium' / 'ERP') of 4.5% above long term gilts, and is considered reasonable for the purposes of FRS17.

Level of prudence compared to KPMG central assumptions



Sector update

This section contains a brief update on topics which the College should be aware of.

Area	Issues
International Financial Reporting Standards (IFRS)	Draft Financial Reporting Standards (FRS) 100, 101 and 102 set out the future standards for UK GAAP. These standards are based upon International Financial Reporting Standards and anticipated to be effective for years commencing on or after 1 January 2015. For the further education sector this will require financial statements to be produced in line with the new standards for the year ending 31 July 2016 with restatement required to the comparative period. KPMG are acting as consultants to BUFDG FRG in developing the new FE HE SORP in relation to these standards. Draft FRS102 contains many similarities to UK GAAP. The key areas being considered by the SORP working group include: ■ the treatment and disclosures for restricted income, donations and endowments; ■ the accounting for service concession arrangements and application to typical accommodation schemes, an area that is also being considered by the Financial Reporting Council in revisions to FRS 102; ■ financial statement proformas; and ■ revenue recognition. During the development of the SORP there are a number of opportunities for further education colleges to be engaged in the process including commenting on the development of the SORP as topics are finalised, being part of the wider further education working group and attending seminars being arranged by BUFDG and KPMG to provide updates and training on the impact of the new standards and the SORP. Please contact us for further information.

Sector update (continued)

While these reforms apply to England, the College should be aware of the developments and trends which are likely to affect local government pension schemes.

Pensions Wider Considerations

Local Government Pension Scheme Reform

Earlier in 2012 the proposals for changes to the LGPS were issued as a joint statement from the Local Government Association, GMB, Unison and Unite. The trade unions are consulting with their membership and the LGA is consulting with employers. The formal consolation is expected to commence in the Autumn.

The main proposals for a new look scheme, “LGPS 2014”, are as follows:

- career average related earnings (CARE) scheme, with revaluation based on CPI;
- 1/49th accrual rate;
- each member’s Normal Pension Age will be equal to their State Pension Age;
- no change to average member contributions: the lowest paid to pay the same or less and the highest paid to pay more on a more progressive scale after tax relief;
- introduction of a 50/50 option - under some circumstances members can elect to pay half the contributions for half the pension;
- full protection of benefits for service prior to 1 April 2014 and full protection of all benefits for LGPS members who are over age 57 at 1 April 2014; and
- scheme members can stay in the scheme on first and subsequent transfers (if and when outsourced).

These proposals have now been approved by the membership of Unison and Unite.

Other Public Sector Pensions Reform

Changes are being planned or made to all public sector pension schemes along the principles outlined in Lord Hutton’s report published in 2011 .

The principal ones in relation to the design of public sector pension benefits were:

- the scheme should move from a pension based on final salary to one based on the average salary of a member (after allowing for inflation);
- normal Pension Age should be linked to increasing life expectancy, through link to increasing State Pension Age;
- benefits already earned, including the link to final salary, should be unaffected;
- the benefits provided by public sector schemes should be the same across all income groups. However, to reflect higher life expectancy in higher income groups there should be higher member contributions for higher earners; and
- members should be given more choice at what age to take their benefits – pensions would be adjusted accordingly and flexible retirement should be encouraged.

With the increasing cost of final salary pension provision and the current pressures on government resources it is hard to see the status quo being maintained. A combination of lower benefits together with increased member contributions would seem to be the most likely outcome. This may be graduated across pay levels with the highest impact falling on the higher paid.

Sector update (continued)

Area	Issues
Pensions	**Pensions auto-enrolment** Organisations with around 4,000 to 6,000 employees will be required to be fully compliant by 1 May 2013. This means that most establishments will have to be compliant before the end of the 31 July 2013 year-end. You may have seen recent media advertisements from the DWP which will be increasing general awareness of the new auto-enrolment requirements amongst your workforce. All of your workforce will need to be communicated to at your staging date. Implementing automatic-enrolment strategy will involve balancing a complex range of financial, payroll, communications, IT and pensions considerations. There are a number of strategic decisions for you, as employer, to make which are likely to require input from the board. ***As with Real Time Information, it is essential that a process is put in place to ensure that the necessary workforce profiling, systems changes, employee communication strategies and planning for ongoing monitoring are undertaken in good time for the relevant go live date.***
Employment taxes and pensions compliance	**Real Time Information (RTI)** As you will be aware HMRC have proposed that all employers with more than 50 employees will implement RTI from 6 April 2013. RTI is a fundamental change in how PAYE and NIC operates and will provide information required to operate the new universal credit system. The level of increased information required is extensive and may not all be held centrally. ***It is essential that a process is put in place to ensure that the necessary data integration and cleansing is undertaken in good time in order to be ready for this radical change in reporting.***

Sector update (continued)

Area	Issues
Corporation tax, VAT & PAYE updates	**Rate of corporation tax** The standard rate of corporation tax decreased from 26% to 24% with effect from 1 April 2012, so that the effective rate of corporation tax for the year to 31 July 2012 is 25.33%. There will be subsequent annual reductions in the standard rate of 1 per cent per annum to 22% by 1 April 2014, but as these reductions are not yet substantively enacted, any deferred tax provision will need to use the current 24% rate. The small profits rate remains at 20%.
	Overseas agents HMRC are now of the opinion that overseas agents act as intermediaries and payments for their supplies to a further education college should now be subject to a VAT reverse charge which will significantly increase the cost of those supplies. There are challenges that are being made, and alternative structures that are being implemented to reduce this additional cost.
	Cost sharing exemption The VAT Cost Sharing Exemption is a provision in European law that allows businesses and organisations making VAT exempt and / or non-business supplies to form groups to achieve cost savings and economies of scale. Once formed the groups are relieved of a VAT charge on their supplies if all the conditions of the exemption are met. The UK Government has issued more detailed guidance is expected to be released imminently. A key interpretation by HMRC is that any entity that has an overall VAT recovery rate of less than 15% would be eligible to join a Cost Sharing group. Consideration is being given as to how this exemption can best be used to meet further education colleges' strategic needs.

Appendix four

Sector update (continued)

Area	Issues
Corporation tax, VAT & PAYE updates (cont.)	**Employment status** HMRC has been maintaining a watching brief on employment status at education institutions for a number of years, gathering information through regular s.16 enquiries. Whilst the removal of the burdensome Categorisation of Earners (CoE) rule from April 2012 is welcome, we expect that HMRC will further focus their efforts on reviewing educational establishments' overall status compliance, not just the lecturers and academics previously subjected to (CoE). The recently announced Whitehall review of self employment status within the public sector is also likely to institute a new rush of Freedom of Information requests. It is therefore important that colleges initially review the current arrangements to confirm that they are comfortable that they have no exposure. Colleges should also ensure that clear and robust procedures are implemented to ensure all future engagements are rigorously tested to avoid any potential exposure.
	Terminations HMRC is aware that the education sector remains in a period of restructuring and downsizing. As a result HMRC continues to focus on the untaxed elements of termination payments, including redundancy, severance, PILONS, restrictive covenants etc. Those enquiries often unearth other issues, such as the re-engagement of former employees as self-employed workers and these are of particular interest to HMRC. It is essential that College human resource, finance and payroll teams work together when dealing with the impact of termination payments, considering both Employment Tax and Employment Law implications and taking professional advice where there is any uncertainty.