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Dundee College

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

Year ended 31 July 2012

8 March 2013

Contents

The contacts at KPMG in connection with this report are:

Stephen Reid
Director, KPMG LLP

Tel: +44(0)131 572 6795
Fax: +44(0)131 572 6666
stephen.reid@kpmg.co.uk

Michael Wilkie
Manager, KPMG LLP

Tel: +44(0)141 300 5890
Fax: +44(0)141 204 1584
michael.wilkie@kpmg.co.uk

Fiona Irving
Audit In-charge, KPMG LLP

Tel: +44(0)141 300 5605
Fax: +44(0)141 204 1584
fiona.irving@kpmg.co.uk

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the *Code*"). This report is for the benefit of the Board of Management of Dundee College and is made available to Audit Scotland (together "the beneficiaries"), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes, but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

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

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

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the beneficiaries) for any purpose or in any context. Any party other than the beneficiaries that obtains access to this report or a copy and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the beneficiaries.

We also draw your attention to the following:

- management of Dundee College is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems;
- weaknesses or risks identified by us are only those which have come to our attention during our normal audit work in accordance with the Code, and may not be all that exist; and
- communication by us of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve the Board of Management of Dundee College from its responsibility to address the issues raised and to maintain an adequate system of control.

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 managements' 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	Following approval of the financial statements by the board of management, we issued an audit report expressing a qualified opinion on the financial statements. The board of management believes that the College cannot identify its share of assets and liabilities in the Tayside Superannuation Fund on a consistent and reasonable basis and that the College is therefore entitled to use the multi-employer exemption permitted by Financial Reporting Standard 17 *Retirement benefits* ("FRS 17"), which allows the College's participation in the Tayside Superannuation Fund to be accounted for on a defined contribution basis. In our view, taking into account the work of our actuarial staff and the analysis prepared by the College's actuaries, the College's share of the underlying assets and liabilities in the Tayside Superannuation Fund can be identified on a consistent and reasonable basis and its participation should therefore be accounted for as a defined benefit scheme as the exemption currently taken is not valid. In the absence of FRS 17 valuations of the College's share of the assets and liabilities in the Tayside Superannuation Fund having taken place it is not practicable for us to quantify the effect of the departure from FRS 17 on the financial statements as a whole. In view of the effect of the failure to account for and disclose pension costs as required by FRS 17 in respect of the Tayside Superannuation Fund, in our opinion the financial statements do not give a true and fair view, in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction, of the state of affairs of the College as at 31 July 2012 and of its surplus, total recognised gains and losses and cash flows for the year then ended. In all other respects, in our opinion the financial statements have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction made thereunder. Our opinion on the regularity of transactions is also unqualified. Excepting for our commentary above, we do not have any other matters we wish to bring to your attention.	5

Audit status and key audit issues (continued)

Issue	Summary	Page
Financial position	The surplus for the year was £285,000 (2010-11 deficit: £2.532 million), representing 0.99% of total income. The increase is mainly due to lower staff costs as a result of voluntary severance costs in the prior year, partially offset by a reduction in Scottish Funding Council grant income.	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. An adjustment was required in respect of the presentation of cash and bank in hand and short-term investments. There was no net impact on the College's net assets as a result of the adjustment.	4, 6, 23
Performance improvement observations	We have identified three performance improvement observations which we are required to bring to your attention. Of these, two are 'medium' graded observations and one is 'low' graded. We have raised recommendations in regard to enhancement to the corporate governance statement, segregation of duties over journals and controls over payroll starters and leavers.	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 Dundee 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 Management 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).

Accounting policies	Accounting for 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*'. This indicates that there is a presumption that a defined benefit scheme will be accounted for on a defined benefit basis unless one of the two possible exemption criteria is met, which are: ■ employers contributions are set in relation to the current service period, i.e. not impacted by any past surplus or deficit of the fund; or ■ the employer is unable to identify its share of the underlying assets and liabilities in the fund on a consistent basis. The College's board of management accounts for its participation in the Tayside Superannuation Fund ("the Scheme") on a defined contribution basis, as they believe they are unable to identify the College's share of the underlying assets and liabilities in the fund on a consistent and reasonable basis and can therefore apply the multi-employer exemption. Consequently, in respect of current service, the financial statements have been prepared on the basis of an accounting policy of charging pension costs to the income and expenditure account on the basis of contributions made during the financial year. We have discussed this opinion with management who have consulted the College's actuaries and it is our view, based on the evidence provided by the College's actuaries, that the exemption taken is not valid as the College's share of the Scheme assets and liabilities can be identified on a consistent and reasonable basis, and its participation should therefore be accounted for as a defined benefit scheme. The conclusion is based on consideration of the facts presented by the College's actuaries and their analysis of the profile of the fund membership and history of experience (comparing the College with the Scheme average) over the three year inter-valuation period to the most recent triennial valuation as at 31 March 2011. As a result, in our opinion pension costs should be charged to the income and expenditure account on the basis of reflecting the cost of benefits earned in the period and its share of assets and liabilities in the Scheme should be included within the balance sheet of the College. In the absence of FRS 17 valuations of the College's share of the assets and liabilities in the Scheme having taken place it is not practicable for us to quantify the effect of the departure from FRS 17 on the financial statements as a whole. In view of the effect of the failure to account for and disclose pension costs as required by FRS 17 in respect of the Scheme, in our opinion the financial statements do not give a true and fair view, in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction, of the state of affairs of the College as at 31 July 2012 and of its surplus, total recognised gains and losses and cash flows for the year then ended. In all other respects, in our opinion the financial statements have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction made thereunder. Our opinion on the regularity of transactions is also unqualified.

Accounting policies; accounting matters

Accounting policies	Gardyne Theatre Limited During 2011-12, the College established the subsidiary company Gardyne Theatre Limited ("GTL"), the company has no share capital and is limited by guarantee. This company was established with the principal objective of promoting performing acts. Prior to commencement of the final audit fieldwork we considered the articles and memorandum of association, together with a summary of GTL transactions and agreed with management's assessment that GTL should be consolidated in the College's financial statements, under the requirements of FRS 2 *Accounting for Subsidiary Undertakings*. 2011-12 is the first year that the College has prepared consolidated group accounts which include the results of both the College and GTL. 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, subject to the matter in respect of FRS 17 above, 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 (continued)

The College has indicated that it supports the regionalisation reforms and is committed to merging with Angus 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 strategic plan 2012-13 was approved by the board of management in June 2012, comprising seven strategic aims, including property and financial plans. During 2011-12 the process of regionalisation has begun and on 17 September the board of management agreed that the preferred option in respect of regionalisation was to progress merger talks with Angus 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 Angus and Dundee 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 non-business activities were undertaken by the College. 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 a week after our audit fieldwork commenced.

A comprehensive auditor's file was provided in support of the draft financial statements.

Area	Comments
Financial statements preparation process	■ Schedules designed to support the financial statements, prepared by management were provided on 15 October 2012, with draft financial statements received on 23 October 2012. ■ 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 23 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 one***

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 one audit difference detailed in appendix two. The adjustment had no net impact on the College's income and expenditure account or balance sheet.

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	22,864	23,197
Tuition fees and education contracts	3,761	4,479
Other grants and contracts	865	1,872
Other income	1,194	1,104
Interest Income	106	117
Total income	**28,790**	**30,769**
Expenditure		
Staff costs	17,347	21,263
Restructuring costs	827	1,563
Other operating expenses	6,711	7,811
Depreciation	3,636	2,589
Interest and other finance costs	178	75
Total expenditure	**28,699**	**33,301**
Surplus/(deficit) after depreciation of tangible assets at valuation and before taxation and disposal of assets	**91**	**(2,532)**
Disposal of assets	194	-
Surplus/(deficit) on continuing operations after depreciation and disposal of assets at valuation and taxation	**285**	**(2,532)**

Source: 2011-12 draft financial statements

Result for the year

The College made an overall surplus of £285,000 (2010-11: £2.532 million deficit), equating to 0.99% of total income

Total income decreased by £1.98 million.

- Scottish Funding Council grants decreased on a recurring basis by £1.7 million in 2011-12. This reduction was off-set by additional deferred capital grants release of £1.3 million.
- Tuition fee and education contracts decreased by £0.71 million primarily due to a decrease in further education fees – UK & EU of £0.44 million compared with 2010-11.
- Other grants and contracts have decreased by £1.01 million. The majority of this decrease was due to a reduction in European Social Fund income from £1.24 million in 2010-11 to £0.37 million in 2011-12.

Expenditure has decreased by £4.6 million:

- Staff costs have decreased by £3.92 million, primarily as a result of annual savings arising from the voluntary severance exercise carried out in 2010-11. There has also been a reduction in restructuring costs of £0.74 million between 2010-11 and 2011-12.
- Other operating expenses have decreased by £1.1 million. This is primarily due to reduced premises costs, including utility cost reductions and Gardyne campus non-recurrent expenditure.
- Depreciation has increased significantly following the transfer of Gardyne campus assets under construction to operational fixed assets.

Financial position (continued)

The College awaits confirmation from the Scottish Funding Council in respect of its ability to retain the proceeds of disposal in respect of the Graham Street site of £1.3 million.

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	285	(2,532)
Restructuring costs	827	1,563
Surplus on disposal of assets	(194)	-
Non-recurring Gardyne campus development costs	450	725
Operating surplus for the year	**1,368**	**(244)**
Adjusted operating surplus as a % of total income	**4.8%**	**-0.8%**

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

The draft financial statements include £194,000 gain on disposal of assets, of which the majority relates to the sale of the Graham Street campus. This site, together with Melrose Terrace and Constitution Road were transferred to current assets held for disposal at 31 July 2011, following approval obtained from the Scottish Funding Council for their disposal.

The impaired value of the two unsold sites, recognised in the financial statements is £1 million and the College continues to pursue their disposal. Market conditions have contributed to a reduction in interest in the sites, but management remains confident over obtaining the value reflected within the financial statements.

During 2011-12, the first tranche of payments of £0.68 million of £1.3 million in respect of the disposal of Graham Street were received, leaving an outstanding debtor at 31 July 2012 of £0.62 million, this is due to be paid in early 2013. Initial indications from the Scottish Funding Council, in 2010-11, confirmed that up to £1.3 million of disposal proceeds from the sale of all three sites would be clawed back, with the remainder retained by the College for investment in the Kingsway campus.

In line with the Scottish Funding Council's instructions in their letter of 2 August 2011, the College contacted them in October 2012 regarding the concluded disposal of the Graham Street asset to confirm any claw back of the proceeds of sale. Confirmation received from the Scottish Funding Council on 19 November 2012 permitted the College to retain all of the proceeds from the disposal of Graham Street for future investment in the College's estate. The proceeds have accordingly been transferred to a restricted reserve. The College will need to seek similar permission in respect of the extent to which future sale proceeds can be retained.

Financial position (continued)

Balance sheet

Balance sheet as at 31 July		
£000	**2012**	**2011**
Fixed assets		
Tangible assets	59,908	62,127
Current assets		
Assets held for disposal	1,000	2,100
Stocks	10	13
Debtors: Amounts falling due within 1 year	2,504	2,159
Cash at bank and in hand	2,289	2,365
Short term investments	4,052	4,000
Creditors: Amounts falling due within 1 year	3,376	5,332
Total assets less current liabilities	**66,387**	**67,432**
Creditors: Amounts falling due after more than 1 year	8,000	8,000
Provisions for liabilities	4,382	4,342
Net assets	**54,005**	**55,090**
Deferred capital grants	38,874	40,279
Endowments	50	15
Reserves		
Income and expenditure reserve	6,443	7,277
Restricted reserve	1,288	-
Revaluation reserve	7,350	7,519
Total funds	**54,005**	**55,090**

Source: 2011-12 draft financial statements

The balance sheet shows a fall in net assets of £1.09 million.

The key changes in the balance sheet were as follows:

- Fixed asset additions of £1.4 million were offset by the annual depreciation charge (£3.63 million), this was significantly higher in 2011-12 than 2010-11 following the transfer of Gardyne campus assets from assets under construction to operational assets in 2011-12.
- Assets held for disposal have decreased by £1.1 million as a result of the Graham Street property sale in 2011-12. Two further assets are currently held for sale.
- Creditors falling due within one year have decreased by £1.96 million since 2010-11. This is primarily due to significant balances relating to fixed assets and IT at the Gardyne campus being settled during 2011-12.
- Deferred capital grants received in year amounted £1.24 million, which was offset by the release in year, to match associated depreciation, of £2.64 million.
- The restricted reserve is in relation to the proceeds of sale that are restricted due to the requirement that they are spent on capital investment.

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	28,790	26,967
Expenditure	(28,699)	(26,967)
Surplus/(Deficit) on continuing operations	**91**	**-**

Source: Management accounts – quarter 3

The original budget prepared by the College for 2012-13 forecast a breakeven position. There are a number of risks associated with funding and these are individually presented in the risk register, with the first set of management accounts.

In relation to international fees, the College had originally budgeted for 30 places in 2012-13 but only 21 have been filled to date.

The College is anticipating a £1 million receipt on disposal of the two remaining sites unsold, to be realised in 2012-13.

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	113,550	104,037
Non SFC income a % of income	Measures non SFC income as a % of total income	24.6%	20.5%
Gearing	Measures the reliance on debt finance	54%	53%
Current assets : current liabilities	Measures the College's ability to pay its current liabilities	2:1	2.9:1
Days cash	Cash divided by total expenditure less depreciation expressed in days	76	92

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 103,837 wSUMs. This target was achieved in 2011-12. The wSUM target for 2012-13 is 96,072.

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. With the exception of the area noted in paragraph 1.6 above, proper arrangements are in place to promote and secure Value for Money.*" The exception noted above, was in related to an internal audit report on fleet management. 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.

Observations arising from our audit

#	Risk	Issue, impact and recommendation	Management response/ responsible officer/due date
1	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, the statement is updated to include details of members' attendance at individual board meetings and committees.	Agreed. Director of finance December 2012
2	Medium	While there are human resource meetings which include discussion of starters and leavers, there is no standard new start or leaver form used to initiate amendments to payroll. There is a risk that ghost employees are added to the payroll system or that leavers are not removed in a timely manner. We recommend that a combined starters and leavers form is produced which includes authorisation by an appropriate line manager to before amendment is made to the payroll system.	Agreed. Forms are currently being finalised for immediate implementation. Director of HR December 2012
3	Medium	There is no consistent process to ensure segregation of duties in relation to manual journals. Not all manual journals are subject to preparation and review by two separate parties. There is a risk that if segregation of duties does not exist that an error may not be identified or that fraudulent activities may not be detected. We recommend that a summary spreadsheet, of all manual journals posted by users who are not subject to review, is generated from the system and and a review is completed on a monthly basis, by an appropriate senior member of staff, at least in respect of journals by users not otherwise subject to independent review.	Agreed. Manual journals processed by senior staff will be collated monthly for approval. Director of finance December 2012

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. The College continues to participate in the procurement capability assessment exercise, next due to occur in December 2012.
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 management group 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 Management

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 conduct 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 was one audit difference identified. This had the net affect of nil on the income and expenditure account.

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**	
Short term investment disclosure	**Dr**	**Cr**	**Dr**	**Cr**
Cash and bank in hand	-	-	-	4,052
Short-term investments	-	-	4,052	-
Overall impact	**-**	**-**	**4,052**	**4,052**

Presentational adjustments

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

Misstatements that are uncorrected

There were no uncorrected misstatements identified.

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.

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.

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