Banff and Buchan College

Report on the 2013/14 audit

Audit Scotland

Prepared for Board of Management of North East Scotland College
and the Auditor General for Scotland
September 2014

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Government and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

Contents

Summary

Key messages from the 2013/14 audit

1. We have issued an unqualified opinion on the final set of financial statements of Banff and Buchan College, covering the 3 month accounting period ending 31 October 2013. With effect from 1 November 2013, Aberdeen College merged with Banff and Buchan College to form North East Scotland College.

2. Over the three month period, the college reported a surplus of £8,000 representing 0.3% of income. An unrestricted reserve balance of £608,000 was transferred to North East Scotland College following the merger on 1 November 2013.

3. A change in accounting policies was made in respect of the valuation of fixed assets in preparation for the merger on 1 November 2013 to ensure consistency with the accounting treatment of Aberdeen College. The measurement basis was changed from a historic cost to a valuation basis reflected as at 31 October 2013. This is permitted by Financial Reporting Statement 15 (FRS15) - Tangible Fixed Assets and does not require to be implemented retrospectively.

4. The college operated a severance scheme from June 2013 which was intended to facilitate the transition to a new management structure for the merged college. Following a review of exit payments to senior staff, we identified that the severance policy could have been tighter with regard to the treatment of enhanced payments and that supporting evidence in respect of payments needed to include a business case and formal minutes of approval.

5. Overall the college's arrangements for the prevention and detection of fraud were satisfactory during the period. From our review of the key controls within the main financial systems, we concluded that the college's systems of internal control were operating effectively.

Introduction

6. The purpose of this report is to summarise the auditor's opinions and conclusions, and to report any significant issues arising. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan presented to the Audit Committee of North East Scotland College in January 2014, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.

7. The Board of Management is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems. The auditor is responsible for auditing and expressing an opinion on the financial statements. Weaknesses or risks identified by auditors are only those which have come to their attention during their normal audit work, and may not be all that exist. Communication by auditors of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve

management from its responsibility to address the issues raised and to maintain an adequate system of control.

Financial statements Audit opinion & representations

8. We have issued an unqualified opinion on the financial statements of Banff and Buchan College for the period ended 31 October 2013 and on the regularity of the financial transactions reflected in those financial statements. The auditor's report is included at Appendix A.

9. The merger with Aberdeen College to form North East Scotland College took place on 1 November, and from that date, Banff and Buchan College ceased to have a separate identity. All staff, assets, liabilities, rights and obligations transferred to the new entity.

10. There were no significant monetary errors arising from the audit. An adjustment of £8,000 in respect of a non-domestic rate rebate has not been made. This would have increased the surplus by £8,000. While more than clearly trivial, this error was immaterial to the accounts as a whole and therefore we agreed with finance not to adjust the accounts.

11. As part of the completion of our audit we seek written assurances from the Principal on aspects of the accounts and judgements and estimates made. A draft letter of representation under International Standard of Auditing (ISA) 580 was provided to the Principal and this was signed and returned prior to the independent auditor's opinion being certified.

Key Judgements

Acquisition accounting

12. From 1 November 2013, Banff and Buchan College merged with Aberdeen College to form North East Scotland College. Financial Reporting Standard (FRS) 6 covering acquisitions and mergers provides criteria to determine whether merger or acquisition accounting should be applied. The criteria includes the:

- role of the respective parties in the combination of the bodies
- dominance of management including the board and senior management structures
- the relative size of the parties combining.

13. Following management review of the criteria, acquisition accounting was considered appropriate for the combination of Banff and Buchan College with Aberdeen College. This meant that audited accounts were required for the period from 1 August 2013 to 31 October 2013 i.e. the 3 month period between the last financial year end and the vesting date for North East Scotland College. In our view the approach was appropriate and met the requirements of FRS 6.

Accounting policies

14. **Income**: Recurring grant income from the Scottish Funding Council has been reflected in the accounts on the basis of service rendered which is generally equivalent to the level of expenditure incurred during the period. In previous years, grant income was received in respect of the academic year. As 2013/14 is a 3 month accounting period, it was necessary to give particular consideration to the approach to income recognition. Having considered how income accrues to the college, links with student activity and forecasts and the profile of expenditure during the 3 month period, we are satisfied with the college's approach to income recognition.

15. **Fixed assets**: A change in accounting policies was made in respect of the valuation of fixed assets in preparation for the merger on 1 November 2013 to ensure consistency with the accounting treatment of Aberdeen College. The measurement basis was changed from a historic costs to valuation basis reflected as at 31 October 2013. This is permitted by Financial Reporting Statement 15 (FRS15) - Tangible Fixed Assets and does not require to be implemented retrospectively.

16. **Going concern**: Activities, assets and liabilities of Banff and Buchan College transferred to Aberdeen College on 1 November 2013 when the new college was formed. This is a transfer of functions within the public sector and accordingly, the financial statements have been prepared on a going concern basis. Appropriate disclosures have been included within the financial statements.

17. Management have considered the funding available to the merged college in 2013/14 and consider it appropriate to adopt a going concern basis for the preparation of these financial statements. I am satisfied that this basis is appropriate.

Financial position

18. Banff and Buchan College reported a surplus of £8,000 in respect of the three months to 31 October 2013, which represented 0.3% of income and held an income and expenditure balance of £608,000 at 31 October 2013.

19. Income and expenditure both increased primarily as a result of costs associated with voluntary severance offset by transformation funding receivable from the Scottish Funding Council. Management approved 12 voluntary severance applications in respect of Banff and Buchan College.

20. The Balance Sheets reflects an increase in net assets of £3.7 million which largely arose from an increase in the value of fixed assets following adoption of a revaluation accounting policy.

Governance and internal control systems

21. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all audited bodies, whether their board members are elected or appointed, or whether they comprise groups of people or an individual accountable officer.

22. Through its accountable officer or equivalent, each body is responsible for establishing arrangements for ensuring the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies usually involve those charged with governance (including audit committees or similar groups) in monitoring these arrangements.

23. Consistent with the wider scope of public audit, auditors have a responsibility to review and report on audited bodies' corporate governance arrangements as they relate to:

- corporate governance and systems of internal control
- the prevention and detection of fraud and irregularity.

Accounting and internal control systems

24. Scrutiny of the effectiveness of the internal control processes within Banff and Buchan College was undertaken by the Audit Committee. The terms of reference for the committee were largely in line with the UK Corporate Governance Code 2010 (the Code).

25. The Code and the Accounts Direction from the Scottish Funding Council require colleges to include a governance statement within their financial statements. The statement in the college's accounts for the 3 month period ended 31 October 2013 confirmed that in the opinion of the Board of Management, the college complied with the Code. We have reviewed the governance statement and have confirmed it is in line with the content required by the Accounts Direction and it reflects our understanding of Banff and Buchan College.

26. The auditor evaluates significant financial systems and associated internal controls for the purpose of giving an opinion on the financial statements and as part of the review of the adequacy of governance arrangements. However, the extent of this work should also be informed by an assessment of risk and the activities of internal audit.

27. Internal audit for the college was provided by Scott Moncrieff. Following the merger, Wylie & Bisset provided the internal audit service for North East Scotland College, with effect from 1 November 2013. Our testing combined with that of internal audit did not identify any material weaknesses in the accounting and internal control systems during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

Prevention and detection of fraud and irregularity

28. In our Annual Audit Plan we highlighted the responsibility audited bodies have for establishing arrangements to prevent and detect fraud and other irregularities. In our opinion, in Banff and Buchan College, the overall arrangements for the prevention of fraud are satisfactory, although it should be noted that no system can eliminate the risk of fraud entirely.

Risk management

29. The college's risk management policy and risk register were kept under regular review by the Audit Committee to ensure that risks were adequately managed by the college.

Performance

Severance payments

30. In spring 2013, the Boards of Management of Banff and Buchan College and Aberdeen College approved the introduction of a voluntary severance scheme (the scheme). The scheme allowed a maximum severance payment up to the equivalent of one year's gross salary. The payment could be taken as a lump sum or put towards the enhanced pension cost which would arise as a result of the early release of a member of staff. The policy was clear on the actions which could be taken if the severance payment was more than the enhanced pension cost but was silent on what could happen if it was a smaller amount.

31. We reviewed exit payments to three senior members of staff who had made applications under the severance scheme. This included two cases where enhanced payments totalling £158,300 were made and a further case amounting to £41,200 where the severance payment was in line with the number of years' service. In considering the enhanced payments, we noted that the college had paid more than the 12 months' salary limit set out in the policy and we had initially considered this to be in excess of the policy.

32. The Board however advised that its interpretation of the policy was to pay severance up to a maximum of one year's gross salary as standard but that, in exceptional circumstances, it believed the scheme enabled higher payments to be made, provided the associated costs were recovered within two years. Their actions were in accordance with this interpretation. In our view, the policy could have been clearer on this matter and the college has acknowledged this.

33. While the scheme required senior staff applications to be considered by the Board, the college advised that decisions on these applications were taken in August 2013 by the Chairs' Committee (comprising the chair of the Board and the chairs of the college's Human and Financial Resources Committee, the Learning and Teaching Committee, and the Audit Committee). While this committee had delegated authority to consider senior staff pay matters, there is no formal minute of this meeting.

34. The college provided us with emails that confirmed the chairs were invited to participate in a teleconference meeting on 23 August. The college also provided an options paper that had been circulated to the chairs in advance of the meeting. The options paper contained a breakdown of costs for each of the three members of senior staff, and indicated that savings to offset the proposed costs would be achieved over the subsequent 12-16 months. We were also provided with a brief file note kept by the principal recording the outcome of the meeting.

35. We met with the members of the Chairs' Committee and college staff to clarify the timeline and process for the severance payments. During this meeting, the attendees indicated that the main reason for approving voluntary severance was to facilitate the transition to a new management structure for the merged college. The college was also committed to avoiding compulsory redundancies if possible. The staff and Board members did not document these reasons in either the options paper or in any subsequent minute.

36. Senior managers and board members should be fully aware of the costs and benefits when making decisions. Before approving any early departures, those charged with governance must ensure that they represent a good use of public money, and a clear audit trail should be retained. In summer 2013, the college was preparing for the merger with Aberdeen College and whilst we recognise that severance applications were being considered during a period of significant change for the college, this increases the need for robust supporting evidence.

37. In summary, the college should take the opportunity to tighten its severance policy to clearly reflect the board’s intentions, the severance process should require the preparation of a business case setting out options, costs, anticipated savings and the rationale for recommending one option over another and checks should be put in place to ensure that all severance decisions are formally minuted.

Acknowledgements

38. We would like to express our thanks to the staff of North East Scotland College for their help and assistance during the audit of 2013/14 financial statements.

Appendix A

Independent Auditor’s Report

Independent auditor’s report to the members of the Board of Management of North East Scotland College, the Auditor General for Scotland and the Scottish Parliament

I have audited the financial statements of Banff and Buchan College for the three month period ended 31 October 2013 under the Further and Higher Education (Scotland) Act 1992 and section 44(1)(c) of the Charities and Trustee Investment (Scotland) Act 2005. The financial statements comprise the Income and Expenditure Account, the Statement of Historical Cost Surpluses and Deficits, the Statement of Total Recognised Gains and Losses, the Balance Sheet, the Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Auditor General for Scotland, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Board of Management and auditor

As explained more fully in the Statement of Responsibilities of the Board of Management, the Board of Management is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and is also responsible for ensuring the regularity of expenditure and income. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland. Those standards require me to comply with the Auditing Practices Board’s Ethical Standards for Auditors. I am also responsible for giving an opinion on the regularity of expenditure and income in accordance with the Public Finance and Accountability (Scotland) Act 2000.

Generic scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the body’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Board of Management; and the overall presentation of the financial statements. It also involves obtaining evidence about the regularity of expenditure and income. In addition, I read all the financial and non-financial information to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If

I become aware of any apparent material misstatements, irregularities, or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council of the state of the body's affairs as at 31 October 2013 and of its surplus for the period then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005, and regulation 14 of The Charities Accounts (Scotland) Regulations 2006.

Opinion on regularity

In my opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Opinion on other prescribed matters

In my opinion the information given in the Operating and Financial Review for the financial period for which the financial statements are prepared is consistent with the financial statements.

Matters on which I am required to report by exception

I am required to report to you if, in my opinion:

- proper accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- I have not received all the information and explanations I require for my audit; or
- the Statement of Corporate Governance and Internal Control does not comply with Scottish Funding Council requirements.

I have nothing to report in respect of these matters.

Anne MacDonald CA
Senior Audit Manager
Audit Scotland
Business Hub 11, 2nd Floor West
Marischal College
Broad Street
Aberdeen
AB10 1AB

xx June 2014

Anne MacDonald is eligible to act as an auditor in terms of section 21 of the Public Finance and Accountability (Scotland) Act 2000.