# Glasgow Kelvin College

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

**For 8 months ended 31 March 2014**

Scott-Moncrieff
business advisers and accountants

# Glasgow Kelvin College

## Annual External Audit Report to the Board of Management and the Auditor General for Scotland 2013/14

# Executive Summary

Our audit of Glasgow Kelvin College ("the College") for the 8 month period to 31 March 2014 is complete. We have audited the financial statements of the College under the Further and Higher Education (Scotland) Act 1992 and Section 44(1) (c) of the Charities and Trustee Investment (Scotland) Act 2005.

## Finance

North Glasgow College merged with Stow and John Wheatley Colleges on 1 November 2013 to form Glasgow Kelvin College. Senior management from across the three colleges worked together to ensure a smooth transition. A Partnership Board consisting of members from the three predecessor colleges was established to oversee the merger process.

In 2012, the Scottish Government announced that a decision by the UK Office for National Statistics to reclassify Further Education Institutions as central government bodies would come into force on 1 April 2014. This reclassification led to all Scottish colleges, excluding UHI incorporated colleges, changing their year ends to 31 March and therefore the College is reporting on its financial performance from 1 August 2013 to 31 March 2014.

The College reported a deficit of £4.426 million for the 8 month period to 31 March 2014. The College's 2013/14 Financial Forecast Return (FFR) submitted to the Scottish Funding Council (SFC) projected a deficit of £1.953 million for the period. The variance between actual and projected results arises mainly from a £3.2 million gift to the Glasgow Kelvin Learning Foundation which was not anticipated when the FFR was completed, a reduction in overall grant income (more than the level that was predicted when the FFR was originally prepared), and an impairment loss in relation to the revaluation of the Springburn campus which again could not have been predicted.

## Governance

The College's Corporate Governance Statement confirms that the College has been fully compliant with the key principles of the UK Corporate Governance Code 2010 during 2013/14. We have reviewed the College's statement and can confirm that this is in line with the SFC's guidance and is consistent with our understanding of the College's governance arrangements based on the information gathered as part of our normal audit work.

## Looking forward

From 2015/16 a new Statement of Recommended Practice (SORP): Accounting for further and higher education will align UK Generally Accepted Accounting Practice with International Accounting Standards. Preparation for the transition to the new SORP will need to commence in 2014/15.

## Conclusion

This report concludes the audit of Glasgow Kelvin College for the 8 month period to 31 March 2014. We have performed our audit in accordance with the Code of Audit Practice published by Audit Scotland, International Standards on Auditing (UK and Ireland) and Ethical Standards.

# Introduction

1. This report summarises the findings from our external audit of Glasgow Kelvin College ("the College") in 2013/14. The scope of our audit was set out in our External Audit Strategy and Plan which was presented to the Audit Committee on 18 February 2014. Our audit has focused on the financial statements and governance arrangements at the College.

2. Our plan summarised seven key issues in relation to the 2013/14 audit:

- College merger during 2013/14;
- Merger accounting;
- Revenue recognition – change in year end;
- Voluntary severance scheme;
- Revaluation of fixed assets;
- Completeness and occurrence of income; and
- Management override.

3. This report includes our findings in relation to these key issues and any other significant findings from the audit.

4. Our procedures are carried out solely for the purpose of our audit so that we can form and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Our audit does not necessarily disclose every weakness and for this reason the matters referred to may not be the only shortcomings which exist.

5. The report has been discussed and agreed with the Principal and the Vice Principal – Finance & Corporate Services.

6. We would like to thank all members of staff who were involved in the audit for their kind co-operation and assistance.

7. The report is also addressed to the Auditor General for Scotland and will be published on Audit Scotland's website, www.audit-scotland.gov.uk.

# Financial statements

## Introduction

8. The annual financial statements are the principal means of accounting for the stewardship of the resources made available to the College. In this section we summarise the issues arising from our audit of the financial statements for the 8 month period to 31 March 2014.

## ONS Reclassification

9. In 2012, the Scottish Government announced that a decision by the UK Office for National Statistics to reclassify Further Education Institutions as central government bodies would come into force on 1 April 2014. This reclassification led to all Scottish colleges, excluding UHI incorporated colleges, changing their year ends to 31 March and therefore the College is reporting on its financial performance from 1 August 2013 to 31 March 2014.

## Management responsibilities

10. Within the terms and conditions of the financial memorandum between the Scottish Funding Council (SFC) and the Board of Management of the College, the Board, through the Principal, is required to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the College and the surplus or deficit for that period. In preparing the financial statements the Board is required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare financial statements on the going concern basis unless it is inappropriate to assume that the College will continue in operation.

11. The Board is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the College and enable it to ensure that the financial statements comply with the Further and Higher Education (Scotland) Act 1992 together with the Financial Memorandum issued thereunder and are presented in accordance with the Accounts Direction issued by the SFC.

## Auditor responsibilities

**12.** We audit the financial statements and give an opinion on whether they:

- give a true and fair view of the state of the College's affairs as at 31 March 2014 and of its surplus or deficit 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.

**13.** We also confirm whether, in our 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.

**14.** We express an opinion that the information in the Operating and Financial Review is consistent with the financial statements.

**15.** We are also required to report to you if, in our opinion:

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

## Confirmation of auditor independence

**16.** Ethical Standard 1 – *Integrity, objectivity and independence*, issued by the Auditing Practices Board (APB), requires that external auditors ensure that the Audit Committee is appropriately informed on a timely basis of all significant facts and matters that bear upon the auditor's objectivity and independence.

**17.** We confirm that we have complied with APB Ethical Standards throughout our audit and that, in our professional judgement, we have remained independent and our objectivity has not been compromised in any way. In particular:

a) There are and have been no relationships between Scott-Moncrieff and the Board of Management or senior management that may reasonably be thought to bear on our objectivity and independence,

b) Scott-Moncrieff has not provided significant consultancy or non-audit services to the College. During 2013/14, we provided advice in relation to the creation of an arm's length foundation, particularly in relation to considerations of dominant and significant influence. This was general advice to the College on accounting terminology. No opinion was given, and the College was provided with the facts to allow it to assess its own risk position.

# Qualitative aspects of accounting practices and financial reporting

**18.** During the course of our audit, we consider the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided in the financial statements. The following observations have been made:

| Qualitative aspect considered | Audit conclusion |
|---|---|
| The appropriateness of the accounting policies used. | We have reviewed the significant accounting policies, which are disclosed in the financial statements, and we consider these to be appropriate to the College. |
| The timing of the transactions and the period in which they are recorded. | We did not identify any significant transactions where we had concerns over the timing or the period in which they were recognised. |
| The appropriateness of the accounting estimates and judgements used. | The accounting estimates and judgements used by management in preparing the financial statements are considered appropriate. Estimates and judgements have been applied in respect of depreciation rates, the valuation of the defined benefit pension scheme deficit, the valuation of land and buildings and the valuation of provisions. Where available, the College has utilised the work of independent experts or industry practice to support the estimate applied. |
| The potential effect on the financial statements of any uncertainties including significant risks and disclosures such as pending litigation. | All significant uncertainties and risks have been reflected in the financial statements. |
| The extent to which the financial statements have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed in the financial statements. | From the testing we performed, we identified no unusual transactions in the period. |
| Apparent misstatements in the Operating and Financial Review and inconsistencies with the financial statements. | There are no misstatements or material inconsistencies between the financial statements and the Operating and Financial Review. |

| Qualitative aspect considered | Audit conclusion |
|---|---|
| Any significant financial statement disclosures to bring to your attention. | The significant disclosures included in the notes to the financial statements that we consider should be brought to your attention are in respect of higher-paid employees, senior post-holders and merger accounting. All disclosures made are required by relevant legislation and applicable accounting standards, and require to be disclosed as a result of the merger undertaken within the reporting period. |
| Disagreement over any accounting treatment or financial statement disclosure. | There was no disagreement during the course of the audit with regards to any accounting treatment or disclosure. |
| Difficulties encountered in the audit. | See paragraph 22 below. |

# Overall conclusion

### An unqualified audit opinion on the financial statements

**19.** The annual accounts are due to be approved by the Board of Management on 22 September 2014. Our independent auditor's report will include an unqualified opinion on the financial statements for the 8 month period ended 31 March 2014.

**20.** We are satisfied that the information given in the Operating and Financial Review is consistent with the financial statements.

### An unqualified audit opinion on the regularity of transactions

**21.** The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors to confirm that, in all material respects, the expenditure and receipts shown in the accounts was incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers. We have issued an unqualified opinion on the regularity of transactions in the College's accounts.

# Financial statements preparation

22. This was a particularly difficult period for Glasgow Kelvin College, largely due to the mid-period merger on 1 November 2013, three separate accounting systems in operation and the change in reporting date to 31 March 2014. As a result of the merger the College has experienced significant staff turnover due to rationalisation of services. This often made it difficult for us to obtain the required information and explanations in support of our audit work. However, we worked closely with the College and in particular with the Vice Principal – Finance & Corporate Services and the Head of Finance to ensure we obtained all information we required to perform our audit. We are grateful to all within the College Finance Team for their assistance and support during the course of the audit.

# Audit adjustments

23. Two audit adjustments were made by the finance team to the financial statements initially presented for audit. For completeness the effect of these journals are detailed below:

| **Journal** | | **I & E Account** | | **Balance Sheet** | |
|---|---|---|---|---|---|
| | | **DR** | **CR** | **DR** | **CR** |
| 1 | Trade Debtors | | | £ 6,460 | |
| | Trade Creditors | | | | £ 6,460 |
| | *Being grossing up of credit balances within the trade debtors listing* | | | | |
| 2 | Released of deferred capital grants - SFC (JWC) | | £ 16,000 | | |
| | Released of deferred capital grants - Non-SFC (JWC) | £ 16,000 | | | |
| | *Being reallocation of deferred capital grant release between SFC and non-SFC categories* | | | | |

24. The adjustments above had no impact on the reported deficit.

# Potential adjustments

25. We identified six potential adjustments during the course of the audit. It was agreed with the Vice Principal – Finance & Corporate Services that these amounts are not considered material and thus have not been incorporated into the financial statements. The effect of these potential adjustments is detailed below:

| | | I & E Account | | Balance Sheet | |
|---|---|---|---|---|---|
| **Journal** | | **DR** | **CR** | **DR** | **CR** |
| | | | | | |
| 1 | Income | £ 10,709 | | | |
| | Deferred Income | | | | £ 10,709 |
| | *Being the correction of deferred capital grant released. The grant release was for 12 months rather than 8 months.* | | | | |
| | | | | | |
| 2 | Expenditure | £ 17,476 | | | |
| | Accruals | | | | £ 17,476 |
| | *Being purchase invoices received post period-end, which related to goods/services received pre period-end, but the costs had not been accrued at 31 March 2014.* | | | | |
| | | | | | |
| 3 | Expenditure | £ 18,806 | | | |
| | Trade Creditors | | | | £ 18,806 |
| | *Being adjustment in respect of debit balances contained within the trade creditors listing, where the refund has been deemed to be irrecoverable* | | | | |
| | | | | | |
| 4 | Lennartz VAT Creditor | | | £ 16,724 | |
| | Expenditure | | £ 16,724 | | |
| | *Being a difference between the VAT creditor per the financial statements and the workings from the VAT Advisor.* | | | | |
| | | | | | |
| 5 | Debtors | | | £ 30,000 | |
| | Expenditure | | £ 30,000 | | |
| | *Being instances where the College has been charged VAT on fuel and power at 20% when it should have been charged at a reduced rate of 5%.* | | | | |
| | | | | | |
| 6 | Accruals | | | £ 49,751 | |
| | Expenditure | | £ 49,751 | | |
| | *Being adjustment to reverse voluntary severance cost accruals for one individual which had been accrued twice in error.* | | | | |
| | | | | | |

The overall impact of the potential adjustments would be a reduction in the reported deficit of £49,484.

# Review of accounting systems

26. During our audit work we have considered the College's accounting systems and internal controls. In general, the College's systems of internal financial control appear to be adequate, well designed and operating effectively. Please refer to the action plan for details of control improvements identified during audit fieldwork.

# Key areas of audit focus and significant findings

27. As noted in our audit plan presented to the Audit Committee on 18 February 2014, the following audit risk areas were considered in detail during our audit fieldwork.

### College merger during 2013/14

28. Glasgow Kelvin College was established on 1 November 2013 from the merger of North Glasgow College, John Wheatley College and Stow College. The merger model adopted was the host model, with North Glasgow College acting as the host. In legal terms this meant that North Glasgow College continued as the sole surviving college, changing its name to Glasgow Kelvin College on 1 November 2013, with the other two colleges being abolished on the same date.

29. The merger had a number of implications for the audit, most notably the process for preparing and auditing the balance sheets and results of the merged colleges. In addition, there were a number of disclosure implications for the 2013/14 financial statements, as follows:

- The Corporate Governance and Internal Control Statement within the accounts was required to disclose the governance arrangements that applied during the whole accounting period, both before and after the merger.
- Senior post holders and Principals' emoluments disclosures had to take into account all Principals and senior management in post during the period, as well as any severance payments incurred during the period.
- Related party transactions disclosures needed to reflect any related parties both before and after the merger.

30. We worked closely with the College to ensure that all relevant implications of the merger were correctly accounted for and disclosed in the financial statements. We are satisfied that the College has made the appropriate disclosures in respect of this identified audit risk.

### Merger accounting

31. The merger of the three colleges qualifies for merger accounting, as defined by accounting standards. One of the principles of merger accounting is that the financial statements for the first period are prepared as if the newly merged entity had always been merged. This is to allow the results for the first period to be comparable with those of previous years.

32. As the implementation of the College's new finance system did not take place until 1 April 2014, the separate trial balances from each of the three systems as at 31 March 2014 required to be consolidated by finance personnel, and inter-college transactions eliminated to arrive at the end position for Glasgow Kelvin College, which was then used to draft the financial statements subject to audit. A similar exercise had to be performed by the College to identify the 2013 comparative figures for disclosure within the financial statements.

33. We have audited each of the three individual college trial balances and the consolidation to ensure that this process has been undertaken completely and accurately. We have gained assurance that the

College has correctly applied the merger accounting principles and that the results of the three legacy colleges have been accurately consolidated in the financial statements.

### Revenue recognition – change in year end

34. Following the change in year-end date from 31 July to 31 March, we recommended that College management consider the impact of this change in respect of the College's revenue recognition policy.

35. UK generally accepted accounting practice requires revenue to be recognised as it is earned, i.e. as courses are delivered rather than when the course starts, completes or cash is received. In previous years the financial year was aligned with the academic year, with limited activity that spanned two years, and thus almost all academic income had been earned by the financial year end. However, following the change in year-end, the academic year and the financial year are no longer aligned, and therefore careful consideration had to be given to the period in which income was recorded.

36. Scottish Funding Council issued guidance notes for the completion of the 2013/14 financial statements, however the guidance did not state any specific methodology that should be used in recognising income, but stated that "it is for individual colleges to demonstrate that they have applied an appropriate methodology to arrive at an acceptable estimate."

37. We have reviewed the College's accounting treatment for income recognition in respect of the period ended 31 March 2014. The College calculated the income to be recognised in respect of each course, based on the percentage of the course that was completed as at 31 March 2014. This was calculated based on the number of teaching days delivered over the duration of a course.

38. All SFC grant in aid which was received up to 31 March 2014 was recognised, and the College included an accrual for the income earned, but not yet received, as at 31 March 2014. We confirm that the College has applied an appropriate methodology to arrive at an acceptable estimate of income earned within the 8 month reporting period.

### Voluntary severance scheme

39. The College undertook a voluntary severance scheme during the 8 month period to 31 March 2014. Like most publicly funded organisations, staff costs are the largest area of expense for the College and therefore they offer the greatest opportunity for making cost savings, which we understand are required in order to deliver a breakeven budget for 2014/15.

40. From our review of the College's corporate governance arrangements, with reference to "Guidance on severance arrangements to senior staff in Scottish further education colleges", produced by the Scottish Funding Council and "Managing early departures from the Scottish public sector" produced by Audit Scotland, our audit work was directed to ensure that best practice in relation to Board review and approval of voluntary severance agreements, particularly in relation to those for senior post holders, was being applied. The guidance states that Board members should approve early departure schemes ensuring that proposals represent value for money, as well as specifically approving proposals affecting senior managers to ensure that each application is independently authorised.

41. As part of our standard audit testing we identified that voluntary severance for two staff members did not follow best practice, including one for a senior staff member. In the first instance, a senior staff member of North Glasgow College was awarded voluntary severance in October 2013 (with the payment being made through the 31 October 2013 payroll run). Although the individual left the College on 10 November 2013, the compromise agreement was not formally signed until 14 November 2013. We were unable to obtain any evidence to illustrate that this severance package had been approved by North Glasgow College in advance of the settlement being agreed. A Remuneration Committee of Glasgow Kelvin College was convened at the first available opportunity, 9 December 2013, to bring the Committee up to date with this issue inherited on merger, and to formally approve the business case.

42. In the second instance we identified that another individual received a voluntary severance package in September 2013, but the business case was not approved by the John Wheatley College Remuneration Committee until October 2013. In future the College should ensure the voluntary severance process is undertaken in a chronological order.

*Action Plan: Point 1*

## Revaluation of fixed assets

43. Following guidance issued by SFC, the college sector has been directed that land and buildings should be valued on a Depreciated Replacement Cost (DRC) basis. North Glasgow College previously accounted for such assets on a cost basis, with John Wheatley College and Stow College applying the DRC basis.

44. The College appointed a firm of Chartered Surveyors to perform a revaluation exercise of the whole Glasgow Kelvin College estate as at 31 March 2014 to ensure compliance with SFC guidance.

45. Under UK accounting practice, moving to a revaluation model represents a change in accounting policy and therefore required a prior year adjustment to be reflected within the financial statements. The effect of this for the former North Glasgow College estate was that three valuations were required (closing as at 31 March 2014, comparative as at 31 July 2013 and opening as at 1 August 2012). As the merger of the three colleges qualified for merger accounting, the financial statements as at 31 March 2014 have been prepared as if Glasgow Kelvin College had always been in existence, hence why three valuations were required.

46. During our audit, we reviewed the College's accounting for the revaluation to ensure that the 2013/14 financial statements reflect the correct accounting and disclosure requirements. We have gained assurance that the College made the correct accounting entries and prior year adjustment disclosures in relation to the revaluation of land and buildings. In particular, the College has correctly recognised the impairment in relation to the Springburn campus.

## Completeness and occurrence of income

47. There is a presumption under International Standard on Auditing 240 that the recognition of income is a significant risk in all financial statements.

48. We have performed sufficient testing in respect of income capture to provide assurance on the completeness and occurrence of income recognised in the financial statements and we are satisfied that income is correctly stated in the financial statements. In particular, as described above, we considered the impact on revenue recognition of the change to the College's financial year end.

### Management override

49. Additionally, in accordance with International Standard on Auditing 240, management override is a presumed audit risk. We performed sufficient audit testing to gain assurance in respect of this risk. Our audit work included a review of journal entries processed in the period and around the period end, 31 March 2014. We are satisfied that there are no indications of management override in the period.

## Fraud and irregularity

50. Responsibility for preventing and detecting fraud and other irregularities lies with the Board of Management. We are not required to search specifically for such matters and our audit should not be relied upon to disclose them. However, we planned and conducted our audit so as to give a reasonable expectation of detecting any material misstatements in the financial statements resulting from improprieties or breach of regulations.

51. We are pleased to report that we did not identify any issues of concern in relation to fraud and irregularity.

## Legality

52. We planned and performed our audit recognising that non-compliance with statute or regulations may materially affect the financial statements.

53. We are pleased to report that we did not identify any instances of concern with regard to the legality of transactions or events.

## Management representations

54. We have requested that a signed representation letter, covering a number of issues, be presented to us at the date of signing the financial statements.

# Use of Resources

**55.** This section of the report summarises our findings in relation to the College's financial performance for the 8 month period ended 31 March 2014.

**56.** It is the responsibility of the College to conduct its financial affairs in a proper manner. It is our responsibility to audit the financial statements and to consider the College's governance arrangements in relation to the College's financial position.

## Financial position

**The College has reported a deficit of £4.426 million which included a gift of funds to the Glasgow Kelvin Learning Foundation totalling £3.2 million**

**57.** As from 1 April 2014, the College is classified as a central government entity. As a government body, the College is no longer able to utilise retained income and expenditure reserves in future years. The Board of Management took the decision, prior to the reclassification, to transfer its retained income and expenditure reserves to a foundation independent to the College. A total of £3.2 million was donated to the Glasgow Kelvin Learning Foundation. In the absence of this one-off donation, the College would have reported a deficit of £1.226 million in respect of the 8 month period to 31 March 2014, which is less than the deficit projected within the original merger business case. It is also worth highlighting that this is after incorporation of £548k of net costs associated with the merger.

**58.** In line with the rest of the sector, the College suffered a reduction in core teaching and fee waiver income from the SFC. £20.709 million was received in 2012/13, reducing to £20.575 million in 2013/14, a reduction of 0.6%.

**59.** Overall non-SFC income remained broadly consistent with the prior year at around 20% of total income.

**60.** As mentioned previously, the College has undertaken a voluntary severance programme in the 8 month period to 31 March 2014. The programme was undertaken in order to generate efficiency savings and reduce operating costs to support the delivery of a balanced budget in future years. The voluntary severance scheme for 2013/14 resulted in a cost of £1.792 million, although the College utilised £1.782 million of Scottish Funding Council merger support funding to meet these costs. Due to the timings of the severance programme the College did not generate any savings from a reduction in staff costs in the current period. However it is expected that savings will be achieved, which will outweigh the costs incurred.

# Balance sheet

**The College balance sheet remains strong, despite the reduction in current assets and total reserves following the donation to the Glasgow Kelvin Learning Foundation of £3.2 million**

**61.** The College has reserves of £11.428 million at 31 March 2014 (£13.420 million as at 31 July 2013) and holds £44.343 million of deferred capital grants (£44.963 million at 31 July 2013). The decrease in the reserves balance during the period is in part due to the transfer of £3.2 million to the Glasgow Kelvin Learning Foundation. In addition, the College has seen an increase in the defined benefit pension scheme liability from £2.517 million at 31 July 2013 to £4.726 million at 31 March 2014.

# Financial forecasts

**SFC funding has been confirmed for 2014/15 and a break even outturn has been forecast**

**62.** The SFC uses the Financial Forecast Return (FFR) to assess the financial position and performance of individual colleges and the sector as a whole. The College's 2013 FFR forecast a deficit of £1.953 million for the 8 month period to 31 March 2014. The College's actual deficit, as reported in the financial statements, was £4.426 million. The increase in the reported deficit versus budget was primarily due to the gift of £3.2 million to the arm's length foundation. In the absence of this one-off donation, the College would have reported a deficit of £1.226 million, which is significantly less than the deficit projected within the original merger business case.

**63.** The College has completed its budget for 2014/15, which forecasts income and expenditure of £33.042 million. A comparison of the 2014/15 budget against the merger business case figures for 2014/15 and the 2014 FFR is provided below:

| | **Merger Business Case 2014/15 £'000** | **Financial Forecast Return 2014/15 £'000** | **Glasgow Kelvin Budget 2014/15 £'000** |
|---|---|---|---|
| Income | | | |
| SFC Grants | 24,723 | 25,334 | 25,830 |
| Non-SFC Income | 7,104 | 7,250 | 6,712 |
| Exceptional Merger Support Grant | 996 | 530 | 500 |
| **Total Income** | **32,823** | **33,114** | **33,042** |
| Expenditure | | | |
| Staff Costs | 19,514 | 20,713 | 20,783 |
| Other Operating Expenses | 8,498 | 8,901 | 8,796 |
| Depreciation | 3,157 | 2,970 | 2,963 |
| Exceptional Merger Restructuring Costs | 1,601 | 530 | 500 |
| **Total Expenditure** | **32,770** | **33,114** | **33,042** |
| **Surplus / (Deficit)** | **53** | **0** | **0** |

64. Total SFC income is slightly higher than the figures outlined in the original merger business case and in the 2014 FFR, as a result of an ESF project and reductions in core grant that were previously expected, but have not materialised. In contrast to this, the College has adopted a prudent approach in forecasting non-SFC income, as targets for 2013/14 have not been met in respect of international and Skills Development Scotland income.

## Going concern and subsequent events

65. We are required under International Standard on Auditing 570, "Going Concern" to consider the appropriateness of the Board of Management's use of the going concern assumption in the preparation of the financial statements, and to consider whether there are material uncertainties about the College's ability to continue as a going concern which need to be disclosed in the financial statements.

66. In order to gain assurance on these matters our work has included:

- reviewing bank facilities;
- performing a review of budgets and cash flow projections covering a period of 12 months from the expected signing of the audit report, together with post period-end management accounts;
- reviewing minutes of post balance sheet Board of Management meetings;
- enquiring of senior management and the College's solicitors concerning litigation, claims and assessments;
- consideration of future SFC funding; and
- performing sample testing of post balance sheet transactions.

67. The Board of Management considers that the College has adequate resources to continue its business activities for the foreseeable future.

68. In our opinion the going concern assumption remains appropriate. From the audit work performed and through discussions with the Vice Principal – Finance & Corporate Services and the Head of Finance, we are satisfied that all subsequent events have been disclosed.

# Governance

**69.** It is the College’s responsibility to ensure that it has adequate governance arrangements in place. It is our responsibility to review and report on these arrangements as they relate to:

- the College’s review of its systems of internal control, including reporting arrangements;
- the prevention and detection of fraud and other irregularities;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- the College’s financial position.

## Corporate Governance

**70.** Colleges are required to include in their financial statements a statement covering the responsibilities of their Board of Management in relation to corporate governance arrangements. The statement should describe the ways in which the College has complied with good practice in corporate governance, including the arrangements for risk management, and report on the College’s compliance with the UK Corporate Governance Code.

**71.** The College’s Corporate Governance Statement for 2013/14 states that the College was fully compliant with the UK Corporate Governance Code 2010 throughout the period.

**72.** We reviewed the Corporate Governance Statement by:

- checking the statement against Scottish Funding Council guidance;
- considering the adequacy of the process put in place by the Principal and Board of Management to obtain assurances on systems of internal control; and
- assessing whether disclosures in the statement are consistent with our knowledge of the College.

**73.** We are satisfied that the statement is consistent with the Scottish Funding Council’s guidance and that the contents are not inconsistent with information gathered during the course of our normal audit work.

## Risk management

**74.** Risk management is important to the establishment and regular review of systems of internal control. The College’s annual accounts outline the principal risks and uncertainties of the College and confirm that mitigating controls are in place in response to these risks.

75. The College has a risk register which is maintained by the Senior Management Team (SMT) and reviewed and updated on a regular basis. The Audit Committee considers the risk register at each committee meeting and the Board of Management reviews the risk register on a continuum and also every six months. However, we were informed that the College has not yet developed and embedded a formal Risk Management Policy. We have therefore raised a recommendation within our action plan that the College develops and embeds a policy as a matter of course during 2014/15.

***Action Plan: Point 7***

76. We have concluded that, subject to the issue referred to above, the College had adequate risk management systems in place.

# Internal audit

77. The internal audit service is a key component of the College's internal control framework. As part of our corporate governance responsibilities, we have considered the College's arrangements to ensure that the work of internal audit is sufficient in quality and volume and complies with best practice.

78. For 2013/14 the internal audit service has been provided by Wylie & Bisset LLP. To avoid duplication of effort and ensure an efficient audit process, we have made use of internal audit work where appropriate.

### Internal audit's annual opinion statement

79. Internal audit has concluded in its annual report that the College has adequate and effective risk management, control and governance processes to manage achievement of its objectives.

# Prevention and detection of fraud and irregularity

80. As part of our audit we consider how the College ensures compliance with all relevant guidance and regulations. This includes a consideration of the College's arrangements for the prevention and detection of fraud and irregularity.

81. The College has an anti-bribery policy and a code of practice on whistleblowing in place. There were no frauds identified during the period.

82. All SFC and other guidance and circulars are received by the Principal's secretary and the Vice Principal of Glasgow Kelvin College. The circulars are then forwarded on to the most relevant individual within the College. However, there is no formal system in place for ensuring that where a response to a circular is required, that this is obtained and submitted in a timely manner. We have therefore raised a recommendation within our action plan that the College develops and implements a formal system to manage circulars during 2014/15. ***Action Plan: Point 8***

# Standards of conduct

83. We are required to consider the arrangements made by management in relation to standards of conduct and prevention and detection of corruption.

84. Propriety requires that public business is conducted with fairness and integrity. This includes avoiding personal gain from public business, being even-handed in the appointment of staff, letting contracts based on open competition and avoiding waste and extravagance. Guidance on standards of conduct, accountability and openness have been issued by the Scottish Government.

85. Our work in this area included a review of the arrangements for adopting and reviewing standing orders, financial instructions, registers of interest and schemes of delegation and complying with national and local Codes of Conduct. We also considered controls over ordering and procurement and disposal of assets.

86. We are pleased to report that our audit identified no issues of concern in this area.

# Looking forward

## FE College Statement of Recommended Practice (SORP)

87. Colleges are currently required to follow the Statement of Recommended Practice: Accounting for Further and Higher Education 2007 (‘the SORP’). The SORP reflects UK Generally Accepted Accounting Practice (UK GAAP) and aims to combine the requirements of further and higher education institutions and key stakeholders into recommended accounting practice.

88. Over the last ten years, the Financial Reporting Council has been working on a conversion programme to base all financial reporting in the UK on International Financial Reporting Standards (IFRS). As a result of this conversion programme the Financial Reporting Council has adopted into UK GAAP, Financial Reporting Standards 100, 101 and 102 for financial years beginning on or after 1 January 2015. These three standards effectively become the new UK GAAP, one which is IFRS based.

89. The FE/HE SORP Board, consisting of key stakeholders from Higher and Further Education bodies across the UK, accounting practitioners, as well as representatives from funding bodies, has developed a SORP which takes account of the key requirements of the new Financial Reporting Standards.

90. The SORP represents a significant change in financial reporting across the College sector. This includes changes in disclosure and terminology within the accounts including the names of the primary financial statements. There are also some fundamental changes to accounting practice.

91. The new accounting standards come into force for financial years commencing on or after 1 January 2015, which means 2015/16 will be the first reporting year for institutions. However, comparative figures for 2014/15 are required, which in turn will require an opening balance sheet as at 1 April 2014 to be prepared.

# Appendix 1 – Management action plan

We identified nine observations which we consider require management action.

We are pleased to report that all prior year management actions have been addressed in the current period.

| | | No of Audit Observations | |
|---|---|---|---|
| **Grade** | **Definition** | **Current period** | **Prior year** |
| **5** | Very high risk exposure - Major concerns requiring immediate attention | - | - |
| **4** | High risk exposure - Absence / failure of significant key controls | - | 1 |
| **3** | Moderate risk exposure - Not all key control procedures are working effectively | 5 | 3 |
| **2** | Limited risk exposure - Minor control procedures are not in place / not working effectively | 4 | 1 |
| **1** | Efficiency / housekeeping point | - | - |

# Management Action plan

| 1 | Governance |
|---|---|
| **Observation** | Our work identified that voluntary severance agreements for two individuals, including one senior member of staff, did not follow best practice. In both instances, the two individuals received their voluntary severance and left the employment of the College before the business case was approved by the Remuneration Committee.<br><br>In the case of a senior member of staff of North Glasgow College they left the College's employment in November 2013 and were paid their voluntary severance in October 2013. We were unable to obtain any evidence to illustrate that this severance package had been approved by North Glasgow College in advance of the settlement being agreed. A Remuneration Committee of Glasgow Kelvin College was convened at the first available opportunity, 9 December 2013, to bring the Committee up to date with this issue inherited on merger and approve the business case.<br><br>In the second instance we identified that another individual received a voluntary severance package in September 2013, but the business case was not approved by the John Wheatley College Remuneration Committee until October 2013.<br><br>In future the College should ensure the voluntary severance process is undertaken in a chronological order. |
| **Risk and recommendation** | There is a risk that the College has not fully complied with the SFC's guidance on voluntary severance arrangements.<br><br>We recommend that, in respect of any future voluntary severance schemes, the Board of Management or the Remuneration Committee approves the supporting business case before the individual leaves the College's employment and the individual is given their voluntary severance.<br><br>**Grade 3** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Principal<br><br>Due date: September 2014 |

| 2 | Journal back-up and segregation of duties |
| --- | --- |
| **Observation** | Audit testing in respect of journal entries identified instances where an individual had created, approved and posted the same journal, i.e. there was a lack of segregation of duties in operation.<br><br>Testing also identified that supporting documentation was not always attached to all journals. |
| **Risk and recommendation** | There is a risk that inaccurate or inappropriate journals are posted to the accounting system.<br><br>We recommend that arrangements in this area are reviewed in full to ensure that there is adequate segregation of duties in place going forward between those creating, approving and posting journals.<br><br>Additionally we recommend that finance staff retain documentation to support the raising of journal entries. Implementation of segregation of duties in this area will assist with the authorisation process.<br><br>**Grade 3** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Head of Finance<br><br>Due date: November 2014 |

| 3 | Grant funded assets |
|---|---|
| **Observation** | During the audit, the finance team was unable to provide us with any information in respect of which assets belonging to legacy Stow College were funded by capital grants. Therefore we were unable to conclude as to whether deferred capital grants are being released in line with depreciation for legacy Stow College assets. However, given that the value of legacy Stow College's depreciation charge for the period was immaterial, we are satisfied that the potential error could not be materiality misstated. |
| **Risk and recommendation** | There is a risk that the amount of deferred capital grant funding released during 2013/14 did not match the corresponding depreciation charge of the relevant fixed assets.<br><br>Management should identify during 2014/15 which assets of the legacy Stow College were grant funded, where the asset has not been fully depreciated, to enable audit testing to be performed in full next year.<br><br>**Grade 3** |
| **Management response** | College will review available records and address this issue<br><br>Responsible officer: Head of Finance<br><br>Due date: November 2014 |

| 4 | Taxation |
|---|---|
| **Observation** | As part of our standard audit procedures we asked the finance team to complete our PAYE/VAT checklist. Following its completion we identified there are no controls in place to ensure that consultants hired by the College would be classed by HMRC as self-employed rather than employed. |
| **Risk and recommendation** | There is a risk that the College is not fully compliant with HMRC laws and regulations, exposing the College to potential fines and penalties for non-compliance in these areas.<br><br>We recommend that an assessment is performed for each new consultant engaged by the College to assess whether or not they would be classed by HMRC as employed or self-employed. The HMRC website has an Employment Status Indicator tool to allow the College to perform this assessment: http://www.hmrc.gov.uk/calcs/esi.htm<br><br>**Grade 3** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Director of HR<br><br>Due date: December 2014 |

| 5 | Related parties |
|---|---|
| **Observation** | We performed testing over related party relationships and transactions to ensure that the related party disclosures within the financial statements were complete, accurate and in accordance with Financial Reporting Standard (FRS) 8 "Related Parties". Our testing identified three related party relationships between Glasgow Kelvin College Board of Management members and external organisations which were not recorded on the relevant registers of interests. We also identified several further instances at each of the legacy Colleges.<br><br>Additionally we noted that the register of interests does not capture information in respect of the interests of Board members' close family. Under FRS 8 the definition of related parties includes those controlled, jointly controlled or significantly influenced by a close member of the family of a board member. |
| **Risk and recommendation** | There is a risk that the College fails to identify and disclose significant related party relationships and transactions.<br><br>We recommend that the College expands the register of interests process to capture interests held by close family members of each Board of Management member. The College should also ensure that Board members and Senior Management declare all potential interests.<br><br>**Grade 3** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Clerk to the Board<br><br>Due date: December 2014 |

| 6 | Information Technology |
|---|---|
| **Observation** | As part of our standard audit procedures we asked the finance team to complete our information technology checklist. On review we identified the following potential issues:<br>• Backups of the system data should be tested regularly to ensure successful restore would occur in the event of a critical failure;<br>• Employee mobile devices (i.e. lap-tops and mobile telephones) should have appropriate encryption installed to protect potentially sensitive data from loss or theft; and<br>• The preparation of financial management information should involve little manual intervention. |
| **Risk and recommendation** | There is a risk that the College's IT controls and processes are not sufficiently robust.<br><br>We recommend that the College addresses each of the points noted above.<br><br>**Grade 2** |
| **Management response** | <u>Backups</u><br><br>Recommendation accepted, this will be implemented as part of the College's Disaster Recovery plan<br><br>Responsible officer: ICT Manager<br><br>Due date: February 2015<br><br><u>Encryption</u><br><br>Recommendation accepted, the College will consider the feasibility of encrypting all staff mobile devices and will seek to implement encryption where possible by August 2015<br><br>Responsible officer: ICT Manager<br><br>Due date: August 2015<br><br><u>Management Accounts</u><br><br>Recommendation accepted<br><br>Responsible officer: Head of Finance<br><br>Due date: December 2014 |

| 7 | Risk Management Strategy |
|---|---|
| **Observation** | The College has not developed a formal risk management strategy and supporting policy in respect of Glasgow Kelvin College. |
| **Risk and recommendation** | There is a risk that the risk management arrangements are not sufficiently robust to identify, address, mitigate and control the College's most significant risks.<br><br>We recommend that the College develops and implements a formal Risk Management Strategy and supporting Risk Management Policy.<br><br>**Grade 2** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Vice Principal – Strategy, Planning and Quality Enhancement<br><br>Due date: December 2014 |

| 8 | Circulars |
|---|---|
| **Observation** | The College does not yet have a formal system in place for providing assurance that all relevant circulars are considered. |
| **Risk and recommendation** | There is a risk that the College does not provide appropriate and timely responses to the SFC on information requested within circulars.<br><br>We recommend that the College embeds a formal system to manage all communications from the SFC and other relevant bodies. This should include a log of all circulars received, who they have been sent to, when, what feedback has been received and timescales for formal responses to be submitted where required.<br><br>**Grade 2** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Administration Secretariat Manager<br><br>Due date: October 2014 |

| 9 | Credit control |
|---|---|
| **Observation** | We performed testing over the accounts receivable processes, including ensuring that where invoices had been outstanding for a significant length of time, that the debt was being actively pursued or was being considered for write-off, if recoverability was deemed unlikely.<br><br>Testing identified two invoices which had been outstanding since October/November 2013. One of the invoices related to a Stow College debtor and the other related to a John Wheatley College debtor. |
| **Risk and recommendation** | There is a risk that the College is not following appropriate credit control procedures. Given the income and cost pressures facing the College it is imperative that all income due to the College is received in a timely manner.<br><br>We recommend that the College agrees and implements formal credit control procedures. This should include a system log to note telephone calls made, reminder letters issued, and, if required, the debt being passed to a specialist debt recovery agency.<br><br>**Grade 2** |
| **Management response** | Recommendation accepted<br><br>Responsible officer: Head of Finance<br><br>Due date: November 2014 |

# Follow up on prior year management action plan

| 1 | Governance (North Glasgow College) |
|---|---|
| **Observation** | As part of the route to merger, North Glasgow College undertook two voluntary severance programmes, one in July and the other in October 2013. Guidance on severance arrangements to senior staff in Scottish further education colleges produced by the Scottish Funding Council and Managing early departures from the Scottish public sector produced by Audit Scotland provide guidance to colleges on managing severance schemes. As part of our audit we reviewed severance settlements for senior staff to confirm that severance arrangements conformed to the guidance. From our review, we identified that there was insufficient evidence of the North Glasgow College Remuneration Committee reviewing and approving all severance proposals including discretionary pension enhancements and payments in lieu of notice paid to senior post holders and also early retirement proposals which included significant pension strain costs for the College. The guidance, as detailed above, provides good practice for the review and approval of these proposals. The guidance states that Board members should approve early departure schemes ensuring that proposals represent value for money as well as specifically approving proposals affecting senior managers to ensure each application is independently authorised. It also states that proposals should be supported by business cases, showing the full additional costs of early departures and their anticipated savings. We understand, from discussion with the previous Chair of the Board of Management of the College, that the proposed severance arrangements for both the then Principal and Vice Principal were considered and approved by the Remuneration Committee and we have seen evidence of legal advice received by the committee in support of these proposals. However, the Remuneration Committee minutes and papers held by the College do not provide sufficient documentary evidence that the business cases for these proposals were discussed and approved. Nor was the minute of the Remuneration Committee submitted to the full Board for approval. |
| **Risk and recommendation** | There is a risk that the College has not complied with the principles of good practice as described in the Scottish Funding Council and Audit Scotland guidance as sufficient documented evidence of the approval process has not been retained. We recommend that Glasgow Kelvin College establishes a robust governance framework to ensure that the guidance is adhered to in respect of any future severance arrangements.<br><br>**Grade 4** |
| **Management response** | Accepted.<br><br>Responsible officer: Principal Glasgow Kelvin College & Clerk to the Board. |

| | |
|---|---|
| **Follow up as part of 2013/14 audit** | Following our 2012/13 annual audit report on North Glasgow College, the Auditor General for Scotland prepared a report, highlighting the issues raised, to the Scottish Parliament Public Audit Committee under section 22 of the Public Finance and Accountability (Scotland) Act 2000. The College has taken positive action to address the issues raised by commissioning a detailed review of North Glasgow College governance and financial stewardship.<br><br>**Recommendation addressed.** |

| 2 | Budget forecasting (Stow College) |
|---|---|
| **Observation** | The college incurred a deficit for the 2012/13 year of £429,000. The deficit was incurred primarily through unfunded restructuring costs incurred late in the financial year with limited scope for remedial action to be taken by the Board to address the deficit in the year. |
| **Risk and recommendation** | Under ONS reclassification, from 1 April 2014 colleges will be required to deliver balanced budgets and will no longer be able to maintain reserves. Colleges will therefore need to strengthen their financial planning and budget monitoring processes in order to ensure they meet their annual financial targets.<br><br>We recommend that the College looks to enhance its budget monitoring arrangements. This may require more detailed reporting of financial forecasts. This should enable the College to respond to issues arising throughout the year.<br><br>**Grade 3** |
| **Management response** | This point will be taken forward into Glasgow Kelvin College as part of the formal handover. This point will be relevant for the new College as the merger presents a number of complex challenges and maintaining financial control will be a critical activity. |
| **Follow up as part of 2013/14 audit** | In respect of 2013/14 budget performance and monitoring arrangements, we have previously detailed within this report that the College has reported a deficit for the period (excluding the gift to the arm's length foundation), of significantly less than that forecast within the original merger business case. The College inherited a worse financial position on date of merger than had been anticipated, and steps were taken to reduce expenditure to protect the College's financial position going forward.<br><br>Following our audit work this period, we have no concerns to report in this area.<br><br>**Recommendation addressed.** |

| 3 | Transformation funding (North Glasgow College) |
|---|---|
| **Observation** | During 2012/13 North Glasgow College received £50,000 of transformation funding from SFC, and our fieldwork identified that sufficient evidence of how this funding had been utilised has not been documented. |
| **Risk and recommendation** | There is a risk that the College has not complied with the conditions attached to the funding where sufficient documentation evidencing the spend has not been retained.<br><br>We recommend that Glasgow Kelvin College establishes a robust process in relation to the documentation of expenditure in order to ensure compliance with conditions of funding.<br><br>**Grade 3** |
| **Management response** | The College will ensure it has detailed records in place in respect of all expenditure on the merger project.<br><br>Responsible officer: Vice Principal – Finance and Corporate Services |
| **Follow up as part of 2013/14 audit** | We have confirmed that periodic budget reports were presented to the Board of Management in respect of transformation funding received in 2013/14 and how this had been spent.<br><br>**Recommendation addressed.** |

| 4 | Capitalisation policy (North Glasgow College) |
| --- | --- |
| **Observation** | It was noted that 40 computers with individual costs of less than £5,000 had been capitalised. Although the overall value of the batch purchased was greater than £5,000, the College accounting policy states that assets will only be capitalised if the individual cost of the item is greater than £5,000. |
| **Risk and recommendation** | There is a risk that the accounts are not being prepared in line with the stated accounting policy in this area<br><br>It is recommended that the accounting policy is reviewed for reasonableness and that in future any capitalisation of fixed assets is performed in line with the accounting policy.<br><br>**Grade 3** |
| **Management response** | Accepted.<br><br>Responsible officer: Vice Principal – Finance and Corporate Services |
| **Follow up as part of 2013/14 audit** | Testing over fixed asset additions during 2013/14 identified no similar issues.<br><br>**Recommendation addressed.** |

| 5 | Year-end routine (North Glasgow College) |
| --- | --- |
| **Observation** | It was noted from review of opening balances that the year-end routine on Symmetry had not been performed for either the 2011 or 2012 year end. This means that the 2011 and 2012 results have not been rolled into the Income and Expenditure Reserve total per the trial balance. |
| **Risk and recommendation** | There is a risk that the Income and Expenditure reserve does not show the correct figure and that the ledger is therefore not accurate.<br><br>It is recommended that full year end procedures are performed on Symmetry at the end of every financial year to ensure that the Income and Expenditure Reserve is correctly stated to include all prior year results.<br><br>**Grade 2** |
| **Management response** | Accepted.<br><br>Responsible officer: Vice Principal – Finance and Corporate Services |
| **Follow up as part of 2013/14 audit** | Testing over opening balances brought forward to 2013/14 identified that all opening balances reconciled to the prior year signed accounts.<br><br>**Recommendation addressed.** |

# Appendix 2 – Your audit team

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