cutting through complexity

Dundee and Angus College

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

Audit: period ended 31 July 2015

17 December 2015

Contents

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About this report

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 and Angus College and is made available to Audit Scotland and the Auditor General for 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 circumstances set out in the executive summary: scope and responsibilities.

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.

Headlines

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.

In accordance with ISA (UK and Ireland) 260: *Communication with those charged with governance,* this report summarises our work in relation to the financial statements for the period ended 31 July 2015.

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

Area	Summary observations	Analysis
Strategic overview		
Key business issues and update	The College accounting reference date changed, for the second time in two years; from 31 March back to 31 July. The College has prepared its financial statements for the 16 month period ended 31 July 2015 with comparatives for the eight month period ended 31 March 2014. The College continues to face challenges in the management of costs, due to real terms reduction in funding from the Scottish Government in the period 2011-12 to 2015-16. The recent Financial Forecast Return for 2015-16 reported a £750,000 forecast deficit, with further deficits forecast in the five years to 2020. The College recognises 'failure to achieve financial sustainability' as its highest and only 'red' rated risk and is developing action plans to address the forecast deficits. In the period to 31 July 2015 the College continued to run a voluntary severance scheme, and incurred £0.8 million of costs in relation to awards made.	Page 7
Financial position	The College reported a deficit of £0.5 million in the 16 month period to 31 July 2015. The College's net assets increased by £1.4 million to £55.4 million. This is primarily the result of a £2.3 million reduction in the pension liability calculated by the independent actuary and the revaluation movement in the period; offset by a £0.4 million reduction in deferred capital grants and the deficit on continuing operations of £0.5 million. Gardyne Theatre Limited achieved a break-even position in the period with turnover of £0.34 million (2013-14: £0.08 million loss; turnover £0.21 million).	Pages 8 - 9
Financial statements and accounting		
Audit conclusions	We have issued unqualified audit opinions on the 2014-15 financial statements for the College and for Gardyne Theatre Limited and on the regularity of financial transactions, following their approval by the Board of Management in December 2015. The financial statements were received by the start of audit fieldwork and overall were supported by high quality working papers. The narrative information, remuneration report and fixed asset valuation information was received later in the audit process as some supporting information was not immediately available to management.	Page 11

Headlines (continued)

Area	Summary observations	Analysis
Financial statements and accounting		
Audit focus areas	The areas highlighted below are the specific audit focus areas identified within our audit strategy document: - Assumed ISA significant risk in respect of income recognition fraud risk and management override of controls; - voluntary severance payments; - fixed asset valuation and treatment of net depreciation; and - retirement benefit obligations. The areas of audit focus were agreed with the management as part of our planning procedures and audit work was completed to satisfy the requirements of ISA 330 *The auditor's procedures in response to assessed risks*, including tests of key financial controls. We discussed management proposed treatment of the revaluation of fixed assets and in that respect and in respect of each other matter, we are content with management's judgements and accounting treatment.	Page 12
Accounting policies	From April 2014 all Scottish colleges were reclassified by the UK office for national statistics ("the ONS") as public bodies. This has led to greater accountability for the use of public money in the college sector through additional financial reporting, since colleges must now comply with the requirements of the government financial reporting manual ("the FReM"), as well as the statement of recommended practice: *accounting for further and higher Education* (2007) ("the SORP"). Colleges must therefore make additional disclosures, including a remuneration report and additional information about their estates strategy and resource outturn within the financial review; and from April 2014 onwards colleges were required to adopt the current value basis for reporting their land and buildings. A new SORP that draws on the principles of FRS 102, will be applied in respect of the year ending 31 July 2016. The College will need to prepare a transitional balance sheet as at 1 April 2014 and a comparative balance sheet at 1 August 2015, together with restated comparative statement of comprehensive income for the period to 31 July 2015.	Page 14
Going concern	Management has considered the funding available to the College in 2015-16 and considers it appropriate to adopt a going concern basis for the preparation of these financial statements. We have reviewed management's cash flow forecast for 2015-16 and are satisfied with management's assessment.	Page 15

Headlines (continued)

Area	Summary observations	Analysis
Governance and narrative reporting		
Governance	The College must demonstrate compliance with the Code of Good Governance for Scottish Colleges, issued in December 2014 ("the code of good governance"). The statement of corporate governance and internal control identifies no major weaknesses in governance or internal control arrangements. In the opinion of the new Principal and Board of Management, the College is compliant with its requirements under the code of good governance. Management has identified no significant fraud or irregularities. We reviewed the statement of corporate governance and consider it consistent with our understanding of the process followed by the College during the period.	Page 17
Internal controls	Testing of the design and operation of financial controls over significant risk points was undertaken as part of our year-end testing. Our work concluded that controls relating to financial systems and procedures are designed appropriately and operating effectively. We raised one control recommendations, detailed at appendix four, in respect of journal source information.	Pages 20 - 21
Performance management		
Performance management	The College produces management accounts which compare actual expenditure to budget, and seeks to use the most advantageous supplier that is available when making purchasing decisions. Efficiency savings are planned and ongoing as part of the implemented merger business case. Performance against relevant indicators is measured by the College.	Page 23
Regularity	We have issued an unqualified opinion in respect of regularity of expenditure and receipts shown in the 2014-15 financial statements, following their approval by the Board of Management on 15 December 2015.	Page 24
Financial capacity	Our review in response to the request for data collection identified that there is some strain on financial capacity within the organisation to ensure effective management due to increasing demands on senior finance staff however there has been no indication of weakening of key financial controls or processes.	Page 24

Scope and responsibilities

Purpose of this report

The Auditor General for Scotland ("the Auditor General") has appointed KPMG LLP as auditor of the Board of Management of Dundee and Angus College ("the College") under the Public Finance and Accountability (Scotland) Act 2000 ("the Act"). The period of appointment is 2013-14 to 2015-16, inclusive.

Our annual audit report is designed to summarise our opinion and conclusions on significant issues arising from our audit. It is addressed to both those charged with governance at Dundee and Angus College and the Auditor General. The scope and nature of our audit were set out in our audit strategy document which was presented to the audit committee at the outset of our audit.

In addition to the audit of the College, this report also sets out certain matters which came to our attention during the course of our audit of the financial statements of Gardyne Theatre Limited ("GTL") for the period ended 31 July 2015.

Accountable officer responsibilities

Audit Scotland's *Code of Audit Practice* ("the Code") sets out the College's responsibilities in respect of:

- preparation of financial statements that show a true and fair view;
- systems of internal control;
- prevention and detection of fraud and irregularities;
- standards of conduct and arrangements for the prevention and detection of bribery and corruption;
- financial position; and
- Best Value.

Auditor responsibilities

This report reflects our overall responsibility to carry out an audit of the College in accordance with our statutory responsibilities under the Act and of GTL in accordance with the Companies Act 2006 and, in both cases, in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board and the Code.

The Code sets out the wider dimensions of public sector audit which involves not only the audit of the financial statements but also consideration of areas such as financial performance and corporate governance.

Scope

An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. Weaknesses or risks identified 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. 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.

Under the requirements of International Standard on Auditing (UK and Ireland) ('ISA') 260 *Communication with those charged with governance*, we are required to communicate audit matters arising from the audit of financial statements to those charged with governance of an entity.

This annual audit report to members of the College and the directors of GTL, along with our presentation to the audit committee, together with previous reports to the audit committee throughout the year, discharges the requirements of ISA 260.

Strategic overview

Our perspective on key business issues and financial position

Key business issues

The Scottish further education sector continues to undergo significant structural reform. Scotland's colleges were reclassified as public bodies, which has led to changes in accounting periods in each of the last two periods. This change restricts the scope for colleges to build up financial reserves.

Funding for the college sector has decreased in recent years and the College has faced increasing challenges in monitoring costs.

This context informed our audit strategy and audit focus areas, as detailed on pages 12-16.

Sector organisation and structural changes

In October 2010 the ONS reclassified incorporated further education colleges throughout the UK, so that from 1 April 2014 they would be treated as part of central government for financial budgeting and reporting processes. This also had the effect of requiring the College to prepare financial statements to 31 March 2014.

The Colleges of Further Education (Financial Year) (Scotland) Order 2015 came into force on 31 March 2015 with the effect of changing the College year end back to 31 July. The College has therefore prepared financial statements for a 16 month period, running from 1 April 2014 to 31 July 2015. The change also impacted the College in a number of other respects:

- the College must continue to break-even, in resource terms, within each Scottish Government financial year (to 31 March), which results in reduced working capital balances and an increased focus on cash flow monitoring throughout the year, and in particular at 31 March 2015;
- additional accounting measurements and disclosures continue to be required to comply with the HM Treasury Financial Reporting Manual; the College had to revalue its land and buildings as at 31 July 2015; and
- management had to consider accounting entries required in respect of income recognition, which were more complex in respect of the shortened period in 2013-14 and the release or adjustment of which impacted on the longer accounting period in 2014-15.

Overall we are satisfied with management's response to the accounting impacts of these. The the full impact of these changes to the business will become apparent in 2015-16 once they are more fully embedded. The degree of changes, reporting requirements and complexity within the sector continues to place key members of the finance team under pressure.

Voluntary severances

As part of the College's response to ongoing funding cuts and to staffing following the merger, a college-wide voluntary severance scheme was continued in the period. The scheme was approved by the Scottish Funding Council ("SFC"), and the College has agreed applications from over 72 employees, recognising costs of £836,000 in respect of those applications not already approved, during 2014-15.

We would not expect the cost benefits of a staff restructuring exercise to be realised immediately. The annualised average number of full time equivalent staff in the period increased slightly compared to the period-ended 31 March 2014. The staff cost budget for 2015-16 is expected to increase marginally.

The full impact of the changes in achieving value for money from the staff restructuring exercises to date should be reviewed before any further restructuring plans are put in place.

Future financial position

The College continues to face increasing challenges in the management of its costs due to real terms reduction in funding from the Scottish Government in the period 2011-12 to 2015-16. The recent Financial Forecast Return for 2015-16 reported a £750,000 forecast deficit with further deficits forecast in the five years to 2020. The College recognises 'failure to achieve financial sustainability' as its highest and only 'red' rated risk and is developing action plans to address the forecast deficits.

Financial position

The College reported a deficit of £0.5 million for the 16 month period (2013-14 restated: £9.4 million).

Payments of £0.8 million were awarded under the voluntary severance scheme (2013-14: £2.9 million).

The revaluation of land and buildings resulted in recognition of a credit in respect of the reversal of impairment of the Gardyne Campus; recognised as a prior year adjustment, and additional depreciation charged to the income and expenditure account in respect of revalued assets.

GTL broke even in the period with turnover of £0.3 million.

Financial position

The College reported a deficit for the 16 month period to 31 July 2015 of £0.5 million. This compares to a restated deficit of £1.5 million in the previous eight month period after removal of a transfer of £8 million to the arms length foundation. There were no such transfers during 2014-15. The final outturn compares to a budgeted deficit of £0.7 million, before FRS 17 adjustments and increased depreciation following revaluation of land and buildings.

Total income increased by £24.8 million when compared to 2013-14 but this is largely as a result of the change in accounting periods. Overall on a like for like basis:

- SFC recurrent grants awarded for the 2014-15 academic year were £24.6 million, a slight decrease on the £25.2 million awarded for the 2013-14 academic year.
- Other SFC grant income increased proportionately from additional grant for ESF priority five funding during 2014-15 of £1.0 million (2013-14: £0.09 million). Also from an allowable change in the accounting treatment of SFC estates grants (2014-15: £1.1 million; 2013-14: nil). This is offset by proportionately reduced merger transitional funding from the SFC to contribute to the costs of severance and reduced deferred capital grant released.
- Total expenditure is proportionately broadly in line with the prior period with the exception of the donation of £8 million in 2013-14 to the Dundee and Angus Foundation not recurring in 2014-15 and restructuring costs incurred under the severance scheme across both periods being £2.0 million less in 2014-15.
- On a pro-rated basis, staff costs decreased slightly from the prior period. Average staff costs, calculated from full period staff costs, excluding severances, fell approximately 2% from £2.16 million to £2.11 million per month.

Consolidated income and expenditure account

	2014-15 (16 months) £'000	2013-14 (8 months, restated) £'000
Scottish Funding Council grants	41,432	21,286
Tuition fees and education contracts	7,580	4,713
Other grants and contracts	1,460	639
Other income	2,436	1,453
Endowment and investment income	42	110
Total income	**52,950**	**28,201**
Staff costs	33,817	17,299
Restructuring costs	836	2,845
Other operating expenses	13,661	6,723
Depreciation	5,781	2,878
Reversal of previous impairment	(1,011)	(413)
Interest and other finance costs	347	183
Donation	-	8,000
Total expenditure	**53,431**	**37,515**
	(481)	(9,314)
Gain/(loss) on disposal of assets	27	(150)
Deficit on continuing operations after depreciation and disposal of tangible assets at valuation and before taxation	**(454)**	**(9,464)**

Source: Dundee and Angus College 2014-15 financial statements - consolidated

Land and buildings were revalued in the period as required by the FReM. This resulted in a gain of £1.1 million recognised in the income and expenditure account, to the extent it reversed previous impairment of the Gardyne campus which was included in a prior year adjustment. Prior year adjustments in respect of the revaluation included impairment of the Gardyne Campus (£2.4 million) and increase in value of other assets of £7.2 million.

GTL broke even in the period with turnover of £0.3 million (2013-14: £0.2 million; with deficit of £0.07 million).

Financial position (continued)

The College had net assets (including pension liability) at 31 July 2015 of £55.4 million (31 March 2014: net assets of £54.0 million).

Balance sheet

The College had net assets (including pension liability) at 31 July 2015 of £55.4 million (restated 31 March 2014: £54.0 million). The key elements of the movement are set out below.

Assets

Fixed assets decreased by £1.6 million. This is the result of depreciation of £5.8 million exceeding capital additions of £3.3 million. The revaluation increase of £0.9 million is offset by increased depreciation. Land and buildings will continue to be revalued on a regular basis according to FReM requirements.

Debtors decreased by £1.7 million, primarily due to lower amounts receivable from the SFC with the realignment of the accounting year end with the academic year end.

Cash decreased by £1.3 million. This is due to loan capital and interest payments of £0.9 million in the period, £3.3 million spent on capital additions (2013-14: £1.4 million) and £0.4 million cash outflow from operations; offset by increased capital grants received of £3.1 million (2013-14: £2.1 million).

Liabilities

Short term creditors decreased by £3.4 million, reflecting the re-alignment of the academic and financial year ends; resulting in lower accruals and deferrals of income and expenditure. Long term creditors consist entirely of a bank term loan repayable over 15 years. This decreased by £0.6 million as a result of the annual loan capital repayments which commenced on 1 August 2014.

Net pension liabilities in respect of participation in the Tayside Pension Fund decreased by £2.3 million, as a result of changes in demographic and financial assumptions. This movement is considered in appendix three.

Consolidated balance sheet

	31 July 2015 £'000	31 March 2014 (as restated) £'000
Fixed assets		
Tangible assets	71,771	73,370
Current assets		
Assets held for disposal	-	160
Stocks	15	20
Debtors: Amounts falling due within 1 year	3,470	5,163
Cash	2,961	4,274
Creditors: Amounts falling due within 1 year	(4,703)	(8,085)
Net current assets	**1,743**	**1,532**
Creditors: Amounts falling due after 1 year	(6,858)	(7,429)
Provisions for liabilities and charges	-	-
Net pensions liability	(11,209)	(13,502)
Net assets including pension liability	**55,447**	**53,971**
Deferred capital grants	42,125	42,550
Endowments	70	83
Reserves		
Income and expenditure reserve	(336)	(3,713)
Revaluation reserve	13,588	15,051
Total funds	**55,447**	**53,971**

Source: Dundee and Angus College 2014-15 financial statements - consolidated

Reserves

The overall reserves position improved by £1.5 million in 2014-15. This is primarily a result of the decrease in the pension liability of £2.3 million and £0.9 million revaluation uplift, offset by a £0.4 million reduction in deferred capital grants and the deficit on continuing operations of £1.5 million.

Financial statements and accounting

Our perspective on the preparation of the financial statements and key accounting judgements made by management

Audit conclusions

We have issued an unqualified audit opinion on the financial statements of the College and GTL, the regularity of transactions reflected in those financial statements and the College's remuneration report.

The financial statements were accompanied by high quality working papers.

Audit conclusions

We have issued an unqualified opinion on the truth and fairness of the state of the affairs of the College as at 31 July 2015 and of the College's income and expenditure, recognised gains and losses and cash flows for the period then ended. We have also issued an unqualified opinion on the regularity of the transactions reflected in those financial statements.

We issued an unqualified opinion on the truth and fairness of the state of the affairs of GTL as at 31 July 2015.

In gathering the evidence for our opinion we have:

- performed controls testing and substantive procedures to ensure that key risks to the financial statements have been covered;
- reviewed estimates and accounting judgements made by management and considered these for appropriateness;
- considered the potential effect of fraud on the financial statements through discussions with senior management to gain a better understanding of the work performed in relation to prevention and detection of fraud; and
- attended the audit committee to communicate our findings to those charged with governance, and to update our understanding of the key governance processes.

Financial statements preparation

High quality working papers and draft financial statements were provided on 22 September 2015 in line with the agreed timetable. The operating and financial review and statement of corporate governance and internal control were separately updated following the end of audit fieldwork. We suggested minor presentational adjustments to ensure they were in line with available guidance. Due to significant delays in obtaining fixed asset valuations and also pension disclosures for the remuneration report, the financial statements were updated by management in late November 2015.

As a consequence of the merger, there was some uncertainty in respect of staff numbers associated with the operation of multiple payrolls in respect of former Angus and Dundee college staff, transfer of staff following changes in contract and voluntary severance. A change to the prior year FTE was identified by management.

There are no unadjusted audit differences, and there was one adjusted audit difference in respect of the treatment of the impairment of the Gardyne Campus following adoption of a revaluation policy in respect of tangible fixed assets as required by the FReM.

Mandatory communications required by International Standards on Auditing are given in appendix one. There are no significant matters in respect of (i) audit differences; (ii) auditor independence and non-audit fees; and (iii) management representation letter content.

Significant risks and audit focus areas

The significant areas of risk identified in our audit strategy were in respect of:

- **management override of controls; and**

and other focus areas of:

- **revenue recognition fraud risk;**
- **retirement benefit obligations;**
- **fixed asset valuation and treatment of net depreciation; and**
- **voluntary severance payments.**

We summarise below the risks of material misstatement as reported within the audit strategy document. We set out the key audit procedures to address those risks and our findings from those procedures, in order that the audit committee may better understand the process by which we arrived at our audit opinion.

We have no changes to the risk or our approach to addressing the assumed ISA risk of fraud in management override of controls and focus areas of fraud in revenue recognition. We do not have findings to bring to your attention in relation to these matters. No control overrides were identified.

Focus area	Our response	Audit findings
Retirement benefit obligations The College accounts for its participation in the Tayside Superannuation Fund ("the Fund") in accordance with FRS 17: *Retirement benefits* on a defined benefits basis using valuation information prepared by actuarial consultants. The College's actuaries use membership data and a number of assumptions in their calculations based on market conditions at the period-end, including a discount rate to derive the anticipated future liabilities back to the period-end date and assumptions on future salary increases.	We performed the following procedures to assess the College's liability in respect of retirement benefits: ■ KPMG specialists reviewed the financial assumptions underlying the actuary's calculations and compared these to our central benchmarks; ■ assessed the objectivity of the College's actuary as a third party expert; ■ tested the level of contributions used by the actuary to those actually paid during the year; ■ tested the membership data used by the actuary; and ■ agreed the financial statements disclosures to the actuarial report.	As at 31 July 2015 the College's liability in respect of retirement benefits decreased by £2.3 million to £11.2 million. We found that the actuarial consultant as a third party expert was objective and had the appropriate experience and expertise to provide the information for use by the College. Overall the assumptions used by the actuary were within an acceptable range of KPMG's expectations and represent a reasonable and balanced approach, in accordance with the requirements of FRS 17. We found that contributions and membership data used by the actuary were accurate, and that the financial statements disclosures agreed to the actuarial report.

Significant risks and audit focus areas (continued)

Focus Area	Our response	Audit findings
Fixed asset revaluation In accordance with the FReM tangible fixed assets are required to be valued on the current value basis. Previously the tangible fixed assets were accounted for under the historical cost basis (with some assets inherited at nil cost previously recognised at depreciated replacement cost). As part of the valuation, the independent chartered surveyors identified revised economic useful life of the tangible fixed assets. Changes to the economic useful life are treated as a change in accounting estimate. As a prior year adjustment is recognised, the amendment to the depreciation charge has also been reflected in the comparative year.	We considered the approach to appointment and instructions issued to the valuer. We obtained the valuation report and considered the basis of valuation and assumptions inherent in the calculated values of the College's fixed assets. We reviewed the detailed adjustments made by management to reflect the revalued amounts in the financial statements, together with their revised useful economic lives. Significant work was required by management in order to obtain and process adjustments in respect of the third party valuation of tangible fixed assets as at 31 July 2013, 31 March 2014 and 31 July 2015 in order to comply with the FReM requirements.	We are satisfied that the valuer was objective and that the resulting adjustments, including prior year adjustments have been appropriately disclosed in the financial statements. Overall, the value of fixed assets increased by £5.6 million as a result of the valuation, as at 31 July 2015. Following discussion with management, the downward movement in the value of the Gardyne campus was reflected as an impairment as at 31 July 2013. The extent of impairment reduced in the period to 31 July 2015, resulting in corresponding credits to the income and expenditure account which reduced the College deficit. We are content with the valuation methodology, assumptions and presentation in the financial statements.
Voluntary severance payments Audit Scotland has previously identified weaknesses in how some colleges have managed and approved senior staff severance arrangements. In 2014-15 the College incurred £0.84 million in respect of voluntary severance payments. Awards were made under a College-wide scheme continued from the prior period. Awards made to senior staff members were to be made under the rules of these schemes.	We agreed the amounts recognised in respect of awards to senior staff members to source documentation, and confirmed that they were in line with the scheme rules. We reviewed governance around the approval of the scheme by the College and the SFC.	During the 16 month period to 31 July 2015, the College incurred £0.84 million in voluntary severance costs. This compares to £2.85 million in the previous eight month period to 31 March 2014. We found that payments to senior staff members were accurately recognised and awarded in line with scheme rules. The College sought approval from the SFC for the scheme prior to this opening. This was corroborated to the letter received from the SFC. We consider that the disclosure in the financial statements is appropriate.

Accounting policies

There have been no substantive changes to the financial reporting framework as set out in the *Statement of Recommended Practice: Accounting for Further and Higher Education (2007)* ("the SORP").

New FReM reporting requirements, including the application of the revaluation model, have been applied appropriately. Accounting policies have otherwise been applied consistently with those introduced in the previous year.

A new SORP, that draws on the principles of FRS 102, will be applied in respect of the year ending 31 March 2016. The College will need to prepare a transitional balance sheet as at 1 April 2014.

Accounting framework and application of accounting policies

Area	Summary observations	Audit findings
Accounting policies and financial reporting framework	From April 2014 all Scottish Colleges were reclassified by the UK Office for National Statistics ("the ONS") as public bodies. This has led to greater accountability for the use of public money in the college sector through additional financial reporting, since Colleges must now comply with the requirements of the Government Financial Reporting Manual ("the FReM"), as well as the Statement of Recommended Practice: *Accounting for Further and Higher Education* (2007) ("the SORP"). This change impacted the College's accounting policies in a number of respects: ■ additional disclosures, including a Remuneration Report and details about the College's estates strategy and resource outturn, must be included in the Annual Report; ■ the revaluation model for fixed assets was adopted from 2014-15 onwards with restatement of 2013-14 balances; and ■ it introduced a higher degree of judgement in the recognition of income for 2013-14, a shorter period, and the release of which impacted on the longer accounting period to 31 July 2015. In March 2013, the Financial Report Council issued FRS 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland. This is the main part of the new UK GAAP regime and follows the issue in November 2012 of FRS 100 (overview of the framework) and FRS 101 (reduced disclosure framework). FRS 102 is applicable for accounting periods beginning on or after 1 January 2015. In response, the Further and Higher Education SORP Board developed a new SORP. Management will need to consider the accounting and reporting implications of the revised SORP and prepare a transitional balance sheet as at 1 April 2014. There are key differences to the existing SORP, particularly in respect of grant accounting, recognition of obligations arising from funding past deficits of multi-employer pension schemes, service concession arrangements and in respect of financial statement disclosures. Each of these will need careful consideration.	The College has prepared its accounts in line with the requirements of the SORP, the FReM, and the Scottish Funding Council's 2014-15 Accounts Direction for Scotland's colleges and universities. We are satisfied that accounting policies remain appropriate to the College, and have been applied consistently.

The financial statements have been prepared on a going concern basis.

Accounting framework and application of accounting policies		
Area	**Summary observations**	**Audit findings**
Going concern	The College had net assets of £55.4 million (2013-14 restated: £54.0 million) at the balance sheet date. This is primarily the result of a £2.3 million reduction in the pension liability calculated by independent actuary and a £0.9 million upward revaluation of land and buildings; offset by a £0.4 million reduction in deferred capital grants and the deficit on continuing operations of £1.5 million. The College has a £7.4 million outstanding loan balance on terms negotiated in 2010 and expects the facility to be sufficient for the foreseeable future. £8.0 million was transferred to the Dundee and Angus Foundation in 2013-14 and the College expects to make applications for future funding from the foundation. Management has considered the funding available to the College in 2015-16 and considers it appropriate to adopt a going concern basis for the preparation of these financial statements.	In assessing the College's ability to continue as a going concern we have reviewed the 2015-16 budget and cash flow forecast prepared by management. We concur with management's view that the going concern assumption remains appropriate for the reasons noted. Management should continue to monitor the cash position closely in the event of any unplanned expenditure.

Management reporting in financial statements

Our testing of the design and operation of financial controls over the production of the annual report and remuneration report are consistent with the financial statements.

Area	Summary observations	Audit findings
Annual report, including the financial review	The financial statements form part of the annual report of the College for the period ended 31 July 2015. We reviewed the contents of the annual report against the disclosure requirements and are content with the proposed reports. We provided management with some relatively minor suggestions relating to how the reports could be enhanced and where additional information disclosures should be made.	We are required to consider the annual report, and provide our opinion on the consistency of it with the financial statements. We are satisfied that the information contained within the annual report is consistent with the financial statements.
Remuneration report	The Scottish Funding Council's accounts direction set out the requirements of the remuneration report, to be included in the financial statements for the first time in 2014-15. Management has prepared a report in accordance with the template which is supported by reasonable quality information and working papers.	We are satisfied that the information contained within the remuneration report is consistent with the underlying records and the financial statements.
Senior post-holders' emoluments	The SFC's Accounts Direction sets out certain disclosures required in respect of senior post-holders' emoluments. We tested these disclosures to ensure that they were prepared in accordance with the requirements of the Accounts Direction.	No issues were identified with the accuracy of the disclosures.

Governance and narrative reporting

Our overall perspective on the narrative reporting, including the remuneration report and corporate governance statement

Corporate governance arrangements

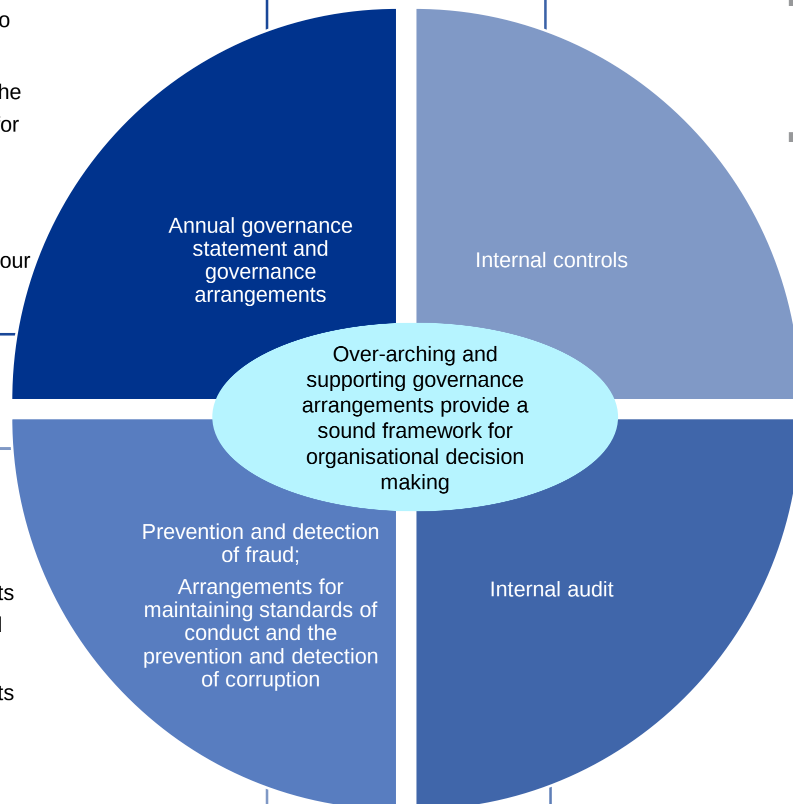
It is a condition of the SFC grant to institutions in the new Financial Memorandum, that the College complies with the principles of good governance outlined in *The Code of Good Governance for Scotland's colleges* ("the Code").

We considered the College's corporate governance arrangements against a number of key areas which we consider to make up an effective governance framework.

Our audit findings against each key area are provided opposite.

- The governance framework of the College is considered to be appropriate.
- The College has adopted the code of good governance for Scotland's colleges.
- The corporate governance statement is in accordance with guidance and reflects our understanding of the organisation.

- Controls relating to financial systems and procedures are designed appropriately and operating effectively.
- We raised one control recommendation in this report. We do not consider this to impact the overall control framework.



- The College's arrangements to prevent and detect fraud are appropriate.
- The College's arrangements to prevent and detect inappropriate conduct and corruption are appropriate

- Internal audit is compliant with the Public Sector Internal Audit Standards.

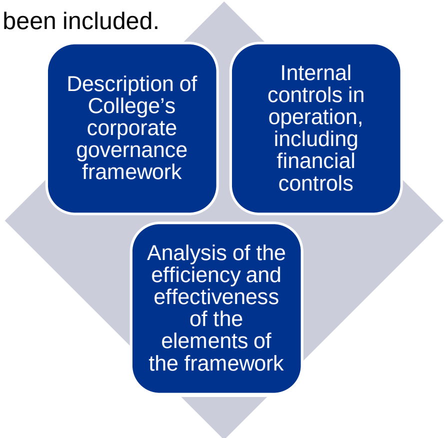
Corporate governance arrangements (continued)

Over-arching and supporting corporate governance arrangements remain primarily unchanged and provide a sound framework for organisational decision-making.

Corporate governance statement

The College accounts includes an annual governance statement. The College made a compliant corporate governance and internal control 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. We are not required to provide an opinion on the College's system of internal control.

The following elements have been included.



Governance arrangements

The College has a Board of Management ,supported by five committees, helps to ensure sound governance arrangements. A new Principal was appointed by the Board of Management during the year with no severance payments made to the former Principal.

GTL maintains its own governance arrangements which are appropriate for its size and complexity, however due to the administrative relationship between GTL and the College, there are a number of shared systems between the two bodies. The corporate governance and financial control frameworks that govern GTL are consistent with those of the College.

Compliance with the code of good governance for Scotland's colleges ("the code")

The code came into effect in December 2014, and since then the College's Board of Management has defined its overall responsibilities in accordance with the code. In the opinion of the new Principal and Chair of the Board of Management the College is compliant with its requirements under the Code.

Risk management

The Board of Management coordinates the College's risk management processes. Management is responsible for considering risks through the year at an operational level and escalating these to the Board as appropriate.

The College has internal auditors whose annual programme is approved by the Audit Committee and endorsed by the Board of Management.

We have updated our understanding of the governance framework and documented this through our overall assessment of the College's risk and control environment. We consider the governance framework to be appropriate for the College and that the governance statement is in accordance with guidance and reflects our understanding of the organisation.

Corporate governance arrangements (continued)

We raised a recommendation from our controls testing in respect of journals source information authorisation.

Systems of internal control continue to be integrated in the merger college.

The College has procedures in place for the prevention and detection of fraud and corruption.

Internal controls

Management is responsible for designing and implementing appropriate internal control systems to ensure a true and fair view of operations within the annual accounts. Our testing, combined with that of internal audit, of the design and operation of financial controls over significant risk points confirms that controls relating to financial systems and procedures are designed appropriately and operating effectively.

The findings of our controls testing relate only to those matters identified during our normal audit work, in accordance with the Code, and there may still be weaknesses or risks within the control environment which have not been identified through this work.

We raised one recommendation from our controls testing relating to journals source information authorisation.

Recommendation one

Prevention and detection of fraud

No material fraud or other irregularities were identified during the year.

Arrangements for maintaining standards of conduct and the prevention and detection of corruption

A key mechanism in the allocation of authority, accountability and responsibility and the prevention and detection of fraud is the existence and maintenance of strategic and financial documentation. We consider that the College has established appropriate processes for the prevention and detection of fraud.

The College has appropriate policies and codes of conduct for staff and members, including the use of a register of members' interests. These appear proportionate for the College's purposes.

Our testing, combined with that of internal audit, of the design and operation of financial controls over significant risk points confirms that controls relating to financial systems and procedures are designed appropriately and operating effectively.

We consider that the College has appropriate arrangements to prevent and detect fraud.

Corporate governance arrangements (continued)

The College's internal auditor supports management in maintaining sound corporate governance arrangements and internal controls. We have found internal audit to be compliant with the Public Sector Internal Audit Standards.

Internal audit

Internal audit supports management in maintaining sound corporate governance and internal controls through the independent examination and evaluation of control systems and the reporting of any weaknesses to management for action.

Audit Scotland's Code of Audit Practice sets out the wider dimension of public sector audit. It requires external auditors to perform an annual assessment of the adequacy of the internal audit function. We considered the activities of internal audit against the requirements of Public Sector Internal Audit Standards ('PSIAS'), focusing our review on the public sector requirements of the attribute and performance standards contained within PSIAS. This included a review reporting lines and range of work carried out by internal audit. We also considered the requirements of International Standard on Auditing 610 *(Considering the Work of Internal Audit)*.

From this assessment, and considering the requirements of International Standard on Auditing 610 *(Considering the Work of Internal Audit)*, we can apply internal audit's work to inform our procedures, where relevant. The review of internal audit reports and conclusions did not indicate additional risks and there is no impact on our planned substantive testing.

Internal audit has completed its agreed plan for the period ended 31 July 2015. The Internal Audit Annual Report 2014-15 states that the College has adequate and effective arrangements for risk management, control and governance and proper arrangements to promote and secure Value for Money. The graphic opposite provides a summary of internal audit's work during the year.

Summary of internal audit work

- Agreed plan completed for the year.
- 10 reviews, follow up of prior year recommendations and opinion on student support funds and activity completed.
- All reviews 'good' or 'satisfactory'.
- Positive annual audit opinion.

We have concluded that the internal audit service operates in accordance with Public Sector Internal Audit Standards.

We can apply internal audit's work to inform our procedures, where relevant. The review of internal audit reports and conclusions did not indicate additional risks and there is no impact on our planned substantive testing.

Performance management

Our perspective on the performance management arrangements, including follow up work on Audit Scotland reports

Performance management

The College produces management accounts which compare actual expenditure to budget.

Our work identified that the College's Best Value and performance management arrangements are generally robust.

Performance against sector indicators is measured by the College.

Performance management and Best Value

Scottish Government guidance for Accountable Officers on Best Value in public services requires a systematic approach to self-evaluation and continuous improvement. The guidance identifies the themes an organisation needs to focus on in order to deliver the duty of Best Value, but notes that implementation should be appropriate and proportionate to the priorities, operating environment, scale and nature of the body's business.

The College produces monthly management accounts which compare actual expenditure to budget, and has a procurement strategy which seeks to use the most advantageous supplier that is available.

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	Target 2014-15	Actual 2014-15	Actual 2013-14
Weighted Student Units of Measurement (WSUMs)	148,703	149,742	145,951
Operating surplus/(deficit) as a % of income	n/a	(0.9%)	(33.6%)
Non SFC income as a % of income	23.7%	21.8%	24.5%
Staffing costs (excluding exceptional items) as a % of total income	n/a	63.9%	61.3%
Current assets: current liabilities	1:1	1.37:1	1.19:1
Gearing	60%	56%	71%
Days cash to expenditure	-	30	38

*Agreed to 2014-15 Outcome Agreement

While non-SFC income continues to grow proportionally, the College's cash balance is increasingly tight and continues to require close and careful management.

Performance management (continued)

We have prepared a return to Audit Scotland in 2014-15 in respect of our findings on financial capacity within the College.

We are required to provide an opinion on the regularity of expenditure and receipts shown in the financial statements.

Financial capacity in public bodies

Through the process of feedback through Annual Audit Reports, current issues reports and sector meetings, Audit Scotland has identified that overall reductions in staff numbers in public bodies may be affecting the capacity of back-office functions and specifically finance.

Audit Scotland has requested the collation of baseline data across the public sector to inform sector specific overview reports and may inform a follow-up to the joint report on the public sector workforce which was published in November 2013 or support the development of the future performance audit programme.

We have completed a return to Audit Scotland in respect of our findings. Our review in response to the request for data collection identified that there is some strain on financial capacity within the organisation to ensure effective management due to increasing demands on senior finance staff however there has been no indication of weakening of key financial controls or processes.

Regularity

As part of our audit of the College's financial statements, we are required by the Public Finance and Accountability (Scotland) Act 2000 to give an opinion on the regularity of expenditure and receipts shown in the financial statements.

The executive team considers all incoming correspondence relevant to its strategic management role from the SFC and other regulatory or advisory bodies, such as Audit Scotland to ensure it is appropriately aware of sector issues and developments and that it complies with the terms and conditions of funding.

Our review of expenditure throughout the course of our audit did not identify weaknesses in the control environment over regularity of expenditure and receipts, or instances of non-compliance with SFC terms and conditions.

We consider that the College has appropriate financial capacity to effectively manage the organisation but note that there are increasing demands on senior finance staff.

We intend to issue an unqualified opinion in respect of regularity of expenditure and receipts shown in the financial statements.

Appendices

Mandatory communications

There were no changes to the core financial statement and there are no unadjusted audit differences

Area	Key content	Reference
Adjusted audit differences Adjustments made as a result of our audit	There were no audit adjustments required to the draft financial statements which impacted on the net assets or net operating cost for the year. A small number of minor numerical and presentational adjustments were required to some of the financial statement notes and we agreed with management that the downward valuation of the Gardyne campus should be treated as an impairment and not a revaluation reserve movement.	-
Unadjusted audit differences Audit differences identified that we do not consider material to our audit opinion	We are required by ISA (UK and Ireland) 260 to communicate all uncorrected misstatements, other than those which are trivial, to you. There are no unadjusted audit differences identified above our materiality thresholds agreed with the audit committee.	-
Confirmation of Independence Letter issued to the Audit Committee	We have considered and confirmed our independence as auditors and our quality procedures, together with the objectivity of our Audit Director and audit staff, in our Audit Strategy document.	Appendix 2
Schedule of Fees Fees charged by KPMG for non-audit services	KPMG did not provide any non-audit services to the College in 2014-15	-
Draft management representation letter Proposed draft of letter to be issued by the College to KPMG	There are no changes to the standard representations required for our audit from last year.	-
Materiality The materiality applied to audit testing.	We assessed materiality based on our knowledge and understanding of the College's risk profile and financial statements balances. Materiality was determined at £1 million; approximately 2% of total expenditure, and is broadly consistent with the materiality identified in our audit strategy. We designed our audit procedures to detect errors at a lower level of precision, i.e. £0.75 million. We report identified errors greater than £50,000 to the audit committee.	-

Auditor independence

Auditing standards require us to consider and confirm formally our independence and related matters in our dealings with the College.

We have appropriate procedures and safeguards in place to enable us to make the formal confirmation in our letter included opposite.

Auditor independence

Professional ethical standards require us to provide to you at the conclusion of an audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed. This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence.

We have considered the fees paid to us by Dundee and Angus College and its related entities for professional services provided by us during the reporting period. We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP Audit Partners and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the APB Ethical Standards. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Regular communications
- Internal accountability
- Risk management
- Independent reviews

Please inform us if you would like to discuss any of these aspects of our procedures in more detail.

There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed to the board of directors.

Confirmation of audit independence

We confirm that as of 17 December 2015, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This letter is intended solely for the information of the audit committee and should not be used for any other purpose.

Yours faithfully

KPMG LLP

Defined benefit obligations

In respect of employee benefits, each of the assumptions used to value the College's net pension deficit are within an acceptable range of KPMG's expectations, with the exception of pension increase rate which is considered to be overly prudent.

However, we are of the view that overall this represents a reasonable and balanced approach, in accordance with the requirements of FRS 17.

Defined benefit pension liability

2015 31 July £'000	2014 31 March £'000	KPMG comment
(11,209)	(13,502)	In line with our established practice and in advance of the audit fieldwork, our actuarial specialists reviewed the approach and methodology of the actuarial assumptions used in the FRS 17 pension scheme valuation. Details of key actuarial assumptions are included in the table, along with our commentary.

Assumption	Dundee and Angus College	KPMG central	Comment
Discount rate (duration dependent)	Less than 17 years: 3.80% Between 17 and 23 years: 3.80% More than 23 years: 3.80%	17 years: 3.65% 20 years: 3.65% 23 years: 3.65%	Acceptable. The proposed discount rates are within an acceptable range of KPMG's central rates as at 31 July 2015.
CPI inflation	RPI less 0.9%	RPI less 1.0%	KPMG's view is that the differential between RPI and CPI should be closer to 1%. The College's assumptions could therefore be considered prudent (higher liability), but lies within the acceptable range for FRS17 purposes.
Net discount rate (discount rate – CPI)	1.20%	1.20%	Acceptable. The proposed assumptions are within the acceptable range of +/- 0.3% from the KPMG central range.
Salary growth	RPI + 0.9%	Typically 0% - 1.5% above inflation	Acceptable. The proposed assumption is consistent with the latest triennial valuation and is acceptable under FRS 17.

The overall assumptions applied by management are considered to be reasonably balanced for a scheme with a liability duration of more than 23 years. The closing deficit decreased by £2.3 million compared to 2013-14, primarily due to changes in assumptions, driven by the decrease in the discount rate and increase in mortality rates. A reconciliation from opening to closing deficit is included on the next page.

Defined benefit obligations

The table opposite shows the reconciliation of the movement in the statement of financial position.

Decreases to the pension scheme deficit in the year have been driven by changes in financial and demographic assumptions.

	£'000	Deficit / loss	Surplus / gain	Impact	Commentary
	Opening pension scheme deficit			**(13,502)**	The opening FRS 17 deficit for the Scheme at 1 April 2014 was £13.5 million, consisting of assets of £34.0 million and defined benefit obligation of £47.5 million.
I & E	Service cost			(2,307)	The employees' share of the cost of benefits accruing over the period is £2.3 million.
I & E	Past service cost			(0)	No past service cost is recognised in the year.
I & E	Net interest			(191)	This is the interest on the opening deficit of £15.3 million. This is made up of £2.7 million expected return on plan assets, and £2.9 million interest cost on obligations.
Cash	Contributions			2,303	The College made contributions of £1.8 million and unfunded pension payments of £0.5 million. This is proportionately in line with contributions made in the previous period.
STRGL	Actuarial gains – demographic assumptions			2,488	There was an actuarial gain of £2.4 million, resultant mainly from changing mortality rates.
	Closing pension scheme deficit			**(11,209)**	The closing FRS 17 deficit on the scheme at 31 July 2015 is £11.2 million (consisting of assets of £38.0 million and defined benefit obligation of £49.2 million).

I&E – impacts on surplus /(deficit) within statement of comprehensive net expenditure
Cash – cash-flow impact
STRGL – charged through statement of total recognised gains and losses

Action plan

The action plan summarises specific recommendations arising from our audit work, together with related risks and management's responses.

Priority rating for recommendations		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the organisation or systems under consideration. The weaknesses may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the control to meet their objectives in any significant way. These are less significant observations than grades one or two, but we still consider they merit attention.

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
1 Journal source information not automated		**Grade three**
When journals are entered manually, the "journal source" is not automatically generated. The person entering the journals has to enter their own initials. This was identified as some journals had an invoice number as the source rather than their initials. This creates a risk of input errors (for example typing errors or putting in a project code instead of initials) or that an individual could enter someone else's initials.	We recommend that either the journal source should be automated or a column implemented which will automatically input the username of the journal poster. This would remove the risk that a user inputs their initials incorrectly.	Source of Journals processed to SUN Financials using its Q&A vision tool can, unfortunately, be manually overridden or omitted. Our normal practice is that this be referenced from a prominent cell on the journal workbook to mitigate error or omission. This will be reinforced. **Responsible officer:** Head of Finance **Implementation date:** Immediate

cutting through complexity