Lews Castle College

Year ended 31 July 2017

Annual Audit Report

15 December 2017

Building a better working world

Contents

About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Auditor General for Scotland has appointed us as external auditor of Lews Castle College (the College) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Further and Higher Education (Scotland) Act 1992 and section 44(1)(c) of the Charities and Trustee Investment (Scotland) Act 2005 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the College and is made available to the Auditor General and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) 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, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Executive summary

Purpose of this report

In accordance with section 21 of the Public Finance and Accountability (Scotland) Act 2000, the Auditor General for Scotland appointed EY as the external auditor of Lews Castle College (the College) for the five year period 2016/17 to 2020/21. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both the members of the College and the Auditor General for Scotland, and presented to both College management and those charged with governance, identified as being the Board and the College's Audit Committee. It will be published on Audit Scotland's website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the College. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

Scope and responsibilities

The Code sets out the responsibilities of both the College and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the Audit Committee on 13 June 2017. We summarise the responsibilities of the College in Appendix A.

Our Annual Audit Plan also provided you with an overview of how we intended to carry out our responsibilities as your auditor. We carried out our audit in accordance with this plan.

We planned our procedures using a materiality of £60,000 and a Tolerable Error of £45,000. We reassessed this using the actual year-end figures, to confirm that the materiality remained appropriate for the audit. No adjustment was made to materiality amounts communicated in our Annual Audit Plan. The threshold for reporting audit differences was £3,000.

Status of the audit and audit opinion

We have issued an unqualified opinion that the financial statements:

- give a true and fair view in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council (SFC) of the state of the affairs of the College as at 31 July 2017 and of its deficit for the year 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 (as amended).

Key contacts

Stephen Reid, Partner
sreid2@uk.ey.com

Keith Macpherson, Head of GPS Audit, Scotland
kmacpherson@uk.ey.com

Rob Jones, Audit Manager
rjones9@uk.ey.com

Ernst & Young LLP, Atria One, 144 Morrison Street, Edinburgh, EH3 8EB

Acknowledgement

We would like to thank all members of the College's management and staff who have been involved in our work for their co-operation and assistance during our audit work.

Accounting and audit matters – our reporting on the College’s financial statements

Preparation of financial statements

- While the core financial statements were provided during the audit process the performance, accountability, remuneration reports and the corporate governance statement were provided after the onsite audit work was completed.
- The draft financial statements presented for audit required a number of amendments to comply with the SORP disclosure requirements. The most significant presentational adjustment required was the disclosure of a college only statement of comprehensive income and expenditure.
- There were two of audit differences above our stated reporting threshold identified throughout the audit process. All differences have been adjusted by management.

Significant risks

- Our testing identified one misstatement from revenue and expenditure recognition above our reporting threshold, which was corrected by management. Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Group or College’s financial position based on manipulation of revenue or expenditure transactions.
- We have not identified any material weaknesses in the design and implementation of controls tested as part of our audit, or evidence of material management override through inappropriate judgements being applied.

Other inherent risks

- We are satisfied that management has adequate arrangements to ensure that property, plant and equipment is appropriately valued within the financial statements. We have noted one audit difference in relation to deferred capital grants released in the year which has been corrected by management.
- The LGPS defined pension scheme liabilities were estimated using actuarial assumptions which we consider to be reasonable. We have undertaken appropriate testing of underlying data to support the calculation of the liability.
- Amendments were required to the pension notes in the draft financial statements to ensure appropriate disclosure of the movement in the defined benefit pensions scheme assets and liabilities.

Other matters and reporting requirements

- Our testing on opening balances was completed satisfactorily. We have no matters to bring to your attention in respect of our work on the qualitative aspects of the financial statements.
- We have concluded that the financial statements give a true and fair view in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council (SFC) of the state of the affairs of the College and its Group as at 31 July 2017 and of the College and Group surplus for the year then ended.
- We have concluded that the College has properly prepared its financial statements in accordance with the requirements of the Further and Higher Education (Scotland) 1992 and directions made thereunder by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005, regulation 14 of the Charities Accounts (Scotland) Regulations 2006 (as amended), and FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland (UK Generally Accepted Accounting Practice).
- We have concluded that 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 Scottish Ministers In respect of our ‘Opinions on other prescribed matters’, which includes the Performance Report, the auditable part of the remuneration report and the Governance Statement we have concluded that our opinion is unqualified. We have not identified any other matters on which we are required to report by exception.

Wider scope audit dimensions – our judgements and conclusions on the College's arrangements

Financial management

- The College reported a deficit of £396,000 for the year (2015/16: deficit of £274,000). The main reason for the year on year movement is an increased staff costs in relation to social security and pensions. The underlying position in line with the SFC Accounts Direction reconciliation equates to an underlying deficit on operations of £19,000 (2015/16: surplus of £23,000) before accounting for non-cash items.
- The College has well established financial management arrangements, and we are satisfied that these are adequate for the management of its financial activities.

Financial sustainability

- The revised targets for student activity is now broadly in line with delivery since 2015/16. While there still remains a risk of under delivery, in our view this has reduced the challenge facing the College around achievement of student activity targets. Given the revision to target levels there could be an increased risk that under delivery could result in clawback of funds, unlike in recent years.
- Future financial forecasts for the College continue to be challenging reflecting the cost pressures facing the sector and the challenge in diversifying and strengthening the income base.

Governance and transparency

- We have concluded that the College arrangements for demonstrating good governance and transparency in its operational activity are continuing to develop. The final report on the Board Effectiveness Review has not yet been received.
- We have made three recommendations in respect of governance and transparency, in relation to ensuring actions from the Board effectiveness review are addressed, completion of registers of interest and other key policies and procedures, and review of standing committee structures.

Value for Money

- The College is in the process of reviewing its strategic aims as the current Strategic Plan ran from 2013-17. The College reports on its website in terms of annual performance, but as the Board develops and finalises its strategy, there is an opportunity to enhance current performance information reporting to provide a view of how performance compares to targets, and how those targets are expected to change over the period of the strategic plan.

Appendices

We have confirmed our independence to act as auditor of the College. Auditor remuneration of £19,600 was agreed with management.

We have made three recommendations for action by management which have been accepted.

1. Financial statements and accounting

1. Financial statements and accounting

The College's annual financial statements enables the Board to demonstrate accountability for its resources and its performance in the use of those resources during the year. They are prepared in accordance with applicable law and UK Generally Accepted Accounting Practice.

Audit opinion

In respect of the financial statements, we report on the truth and fairness in accordance with the requirements of the Further and Higher Education (Scotland) 1992 and directions made thereunder by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005, regulation 14 of the Charities Accounts (Scotland) Regulations 2006 (as amended), and United Kingdom Generally Accepted Accounting Practice, including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

The detailed form and content of our audit report, plus the requirements underpinning the report, are contained in the Audit Scotland guidance at http://www.audit-scotland.gov.uk/uploads/docs/um/tgn_2017-7_further_education.pdf (Appendix 1).

We have issued an unqualified opinion based on the satisfactory completion of our work.

Financial statements preparation

As part of our oversight of the Board's financial reporting process, we report on our consideration of the quality of working papers and supporting documentation prepared predominantly by the finance team to support the audit.

The financial statements were prepared in accordance with the 2015 Statement of Recommended Practice for Further and Higher Education (SORP) alongside the Government Financial Reporting Manual (FReM) 2016/17.

While the core financial statements were provided during the audit process the performance, accountability, remuneration reports and the corporate governance statement were provided after the onsite audit work was completed. The draft financial statements presented for audit required a number of amendments to comply with the SORP disclosure requirements.

Materiality

We planned our procedures using a materiality of £60,000. We reassessed this using the actual year-end figures, to ensure that our level of materiality remained appropriate. We did not change our assessment of materiality as a result of this reassessment. Our Tolerable Error for the audit was £45,000 and the threshold for reporting audit differences was £3,000. We also identified one area where misstatement at a lower level than materiality might influence the reader of the financial statements and developed a specific audit strategy for it. These include:

- Remuneration report – we considered at a materiality appropriate to the banding of disclosure in the remuneration report
- Related party transactions - we considered the nature of these disclosures individually.

Audit differences

There were no unadjusted audit differences above our stated reporting threshold identified throughout the audit process.

We identified a number of audit differences through the course of our work, all of which management has adjusted.

1. Financial statements and accounting

Our Audit Plan identified key areas of focus for our audit of the College's financial statements, including significant risks. This report sets out the results of our audit procedures plus relevant observations, including our views on areas which might be conservative, and where there may be potential risk and / or exposure.

Significant risk – risk of fraud in revenue recognition

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

We rebutted the presumed revenue recognition risk in relation to SFC core funding to the College. This was based on the fact that the funding is clearly allocated for delivery of activity within the financial year. While the College has a history of under-delivery against targets, clawback of funds by SFC is determined at Regional Strategy Body level and at this level there has been no under-delivery, and hence the College has not been subject to any recent clawback. However we recognise a revenue recognition risk for tuition income and other material income in respect of possible manipulation of cut-off around the financial year end. We also recognise the same risk around incorrect recognition of non-pay expenditure in line with Practice Note 10.

Results of audit procedures

We undertook the following procedures as part of our audit:

- Reviewed and tested revenue and expenditure recognition policies against the relevant accounting standards and the SORP.
- Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias.
- Developed a testing strategy in respect of material revenue and expenditure streams. For tuition fees and education contracts, we have substantively tested a sample of transactions to third party supporting evidence to ensure appropriate recognition. For SFC and other funding body grant income we reviewed all material grant funding recognised in the year for any indicators of either claw-back or that the terms and conditions of the financial memorandum have not been complied with in all material respects. For other income, we performed substantive testing over a sample of transactions to gain assurance.
- For non-pay expenditure we reviewed the key management procedures around approval of expenditure throughout the year, and substantively tested a sample of transactions throughout the year to third party supporting evidence.
- We performed focused additional testing around income and expenditure transactions posted at the year end to gain comfort that key items are recorded in the correct accounting period. In particular we focused on any transactions incurred after 31 July, but included in the 2016/17 financial ledger.
- We reviewed and tested a sample of debtor and creditor balances at the year end, including material balances. We undertook an assessment of aged balances held on the balance sheet at year end including investigation of unusual items, such as those past payment due date.

We identified one audit difference in relation to recognition of income in 2016/17 in respect of £12,800 where income was recognised in 2017/18 but should have been accrued into the 2016/17 financial year. This has been adjusted by management. No other differences were identified through the course of our work.

Significant Risk, fraud in income and expenditure recognition – what have we concluded?

- Our testing identified one misstatement from revenue and expenditure recognition during the financial year, which was corrected by management.

Significant risk – management override
What is the risk?
As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.
Results of audit procedures
Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements We obtained a full list of journals posted to the general ledger during the year, and used our bespoke data analysers to identify any unusual journal types or amounts based on our identified risk areas for the audit. We then tested a sample of these journals, understood their purpose and agreed and corroborated them to supporting documentation. **Review accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates** We identified and considered the appropriateness of key accounting estimates, including provisions, and their susceptibility to bias. Management has disclosed their consideration of the critical accounting judgements and key estimates in the financial statements. We have reviewed these and agree with the detail of the assessment performed. **Evaluate the business rationale for any significant unusual transactions** We did not identify any significant unusual transactions. We have not identified any material weaknesses in the design and implementation of control arrangements tested as part of our audit, or evidence of material management override through inappropriate judgements being applied.

Significant risk, Management override – what have we concluded?
• We have not identified any material weaknesses in the design and implementation of control arrangements tested as part of our audit, or evidence of material management override through inappropriate judgements being applied.

Other inherent risks
Valuation of property, plant and equipment
The College's property portfolio totals £12 million as at 31 July 2017, with the major elements of this being in respect of land and buildings. Land and buildings are revalued to fair value with a full revaluation taking place at least every five years. Given the size of this balance and the fact that a number of assumptions are made in the valuation, we assign a higher inherent risk to property, plant and equipment.
Results of audit procedures
In response to the inherent risk we performed the following audit procedures: • We agreed the carrying value of assets held to source data and enquired of management as to the procedures used to establish whether the source data is complete. • We reviewed the basis of asset valuations that have been rolled forward from previous years. • We reviewed the property valuation and challenged management on the possibility of any impairment to the estate in the year that should be recognised prior to the next revaluation. • We re-calculated depreciation charges in the year to ensure they were correct and reflected in the release of related deferred capital grants in the year. We noted no audit differences in the recalculation of depreciation or the release of deferred capital grants. No revaluations were undertaken during 2016/17 or 2015/16, with the last full revaluation being as at 31 July 2015. We have discussed with management the requirement for an interim valuation to ensure the College complies with the requirements of both the SORP and the FReM in 2017/18.

Other inherent risk, valuation of property, plant and equipment – what have we concluded?
• We are satisfied that management has adequate arrangements to ensure that property, plant and equipment is appropriately valued within the financial statements. We have noted one audit difference in relation to deferred capital grants released in the year which has been corrected by management.

Other inherent risks
Valuation of pension liabilities
The College participates in two pension scheme; the Local Government Pension Scheme (LGPS) administered by Highland Council and the Scottish Teachers Superannuation Scheme (STSS). While both are defined benefit pension schemes, the College is unable to identify its share of the underlying assets and liabilities of the STSS scheme on a consistent and reasonable basis and therefore, the scheme is accounted for as if it were a defined contribution scheme. The LGPS is accounted for as a defined benefit scheme. The net pension liabilities on the balance sheet as at 31 July 2017 arising from participation in the scheme were £2.9 million. In addition the College recognises a provision for future early retirement liabilities of £1.1 million.
Results of audit procedures
In response to the identified inherent risk we: • Obtained actuarial reports at the year end date for the LGPS scheme and considered the reasonableness and consistency of assumptions underpinning such reports, in light of guidance available ensuring compliance with funding agreements. • Utilised our in-house actuaries to assess the reasonableness of key assumptions such as discount rate, inflation and expected market return. • Performed substantive testing on the valuation of the College's share of the pension assets and audited the calculation of the College's valuation and disclosure in the financial statements. No matters were identified in respect of our testing over pension assets. In respect of the key assumptions around discount rates and inflation, our actuaries noted that the assumptions were within a range we consider acceptable for the year end date. However, they noted the underlying methodology used to obtain these assumptions was not as robust as they could be, in particular around the estimates of future cash flows for pension costs by the College. While we are comfortable with the assumptions used for the 2017 financial statements there is a risk that future assumptions are not considered appropriate. ***Action plan point 2***

Other inherent risk, valuation of pension liabilities – what have we concluded?
• The LGPS defined pension scheme liabilities were estimated using actuarial assumptions which we consider to be reasonable. We have undertaken appropriate testing of underlying data to support the calculation of the liability.

Our Audit Plan identified other aspects of our work which arise either in accordance with International Standards on Auditing (UK) or in accordance with the Code. These are set out below.

Other audit matters

Opening balances

International Standard on Auditing (UK) 510: *Initial audit engagements – opening balances* requires auditors to obtain sufficient, appropriate audit evidence that opening balances do not contain misstatements that materially affect the financial statements. The standard also requires auditors to verify that appropriate accounting policies are reflected in the opening balances and that they have been consistently applied in the current period's financial statements.

In response, we have:

- Reviewed prior year financial statements, annual audit reports and other reports issued by the former external auditor and held discussions with the former external auditor in respect of previous significant audit issues, corporate governance and as part of our audit risk assessment.
- Substantively tested material opening balances to ensure that they agree both to the prior year audited financial statements and closing trial balance.
- Undertaken a mix of testing on balances during 2016/17 which provides assurance on the judgements and estimates made as at 31 July 2016, in particular in relation to the realisation of estimates made at yearend 31 July 2016 in the 2016/17 financial statements.

No matters were noted through the course of our work.

Group financial statements

The College prepares group financial statements, consolidating the results of the College and its subsidiary undertakings, Lews Castle College (Trading) Limited. The subsidiary is dormant and does not affect the College`s financial position. We are therefore satisfied that the consolidated financial statements have been prepared appropriately.

Opening balances / group financial statements – what have we concluded?

- Our testing on opening balances was completed satisfactorily.
- We are satisfied that the consolidated financial statements have been prepared appropriately.

1. Financial statements and accounting

In accordance with Audit Scotland requirements, our independent auditor's report also covers the key narrative statements such as the Performance Report, the Accountability Report and the Remuneration and Staff Report which the College is required to include within its Annual Report and Accounts.

Other reporting requirements

Performance Report

In accordance with the Code, we review the information contained within the Performance Report and confirm that this is consistent with the information reported within the financial statements. As a new responsibility in 2016/17, under the Code, Audit Scotland requires us to also express an opinion on whether the Performance Report has been prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

We are satisfied that the information with the Performance Report is consistent with the financial statements and has been prepared in accordance with applicable requirements.

Accountability Report, including the Governance Statement

Audit Scotland requires us to read the information in the annual governance statement and express an opinion on whether Governance Statement is consistent with the financial statements and that report has been prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

We are satisfied that the information with the Governance Statement is consistent with the financial statements and has been prepared in accordance with applicable requirements.

Remuneration and Staff Report

Auditors are required by the Code to audit the disclosures of remuneration and pension benefit, pay bands, and exit packages and express a separate opinion within their independent auditor's report on whether they have been properly prepared in accordance with the Regulations.

We are satisfied that auditable part of the remuneration and staff report has been properly prepared in accordance with regulations.

Regularity opinion

The Board of Management is responsible for ensuring the regularity of expenditure and income. Auditors are responsible for expressing an opinion on the regularity of expenditure and income in accordance with the Public Finance and Accountability (Scotland) Act 2000.

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.

Other reporting requirements – what have we concluded?

- We reviewed the other information presented within the financial statements and provided management with comments to enhance the content, structure and presentation of these. These were amended by management.
- In respect of our 'Opinions on other prescribed matters', which includes the management commentary, the auditable part of the remuneration report, and the annual governance statement, our opinion is unqualified.
- We have not identified any other matters on which we are required to report by exception.

2. Wider scope audit

2. Wider scope audit

In accordance with the Code, we provide judgements and conclusions in respect of our work on the four audit dimensions of public sector audit: financial management; financial sustainability; governance and transparency; value for money.

Wider scope audit risks

The Code requires us to undertake work in respect of each of the four dimensions on an annual basis. The Code also sets out an expectation that 'significant' risks identified through our planning process that relate to the wider scope dimensions will be communicated with you. In undertaking our risk assessment in respect of the wider scope audit areas, we distinguish between the definition of 'significant risks' which apply to the audit of the financial statements, by referring to 'Wider Scope Audit Focus Areas'.

In our Annual Audit Plan we identified financial sustainability and governance as areas of wider scope audit focus based on our understanding from previous audit reports, Audit Scotland's section 22 report in 2017 and our initial discussions with management. We have outlined our considerations in respect of these below, in addition to our routine work in respect of each of the other wider scope audit dimensions, by considering the evidence available to us through various aspects of our work.

Financial management

The College reported a deficit of £396,000 for the year (2015/16: deficit of £274,000). The main reason for the year on year movement is an increased staff costs in relation to social security and pensions. The underlying position in line with the SFC Accounts Direction reconciliation equates to an underlying deficit on operations of £19,000 (2015/16: surplus of £23,000) before accounting for non-cash items.

Performance against budget

The College reported a £396,000 deficit in year against a £159,000 budgeted deficit. The level of SFC funding received was higher than projected due to additional allocations being received during the year, however this was offset by the cost of the nationally bargained pay awards for teachers which were finalised in the year and for which the funding was intended. There were also increases against budget in professional services and computing costs.

Funding aspect	Budget - £m	Actual - £m	Variance - £m
Income	5.034	5,726	0.692
Expenditure*	(5.193)	(6.122)	(0.929)
Total surplus (before tax)	**(159)**	**(396)**	**(237)**

*Includes net non-operational expenditure

Monitoring of expenditure

Financial performance is monitored through monthly management accounts and is subject to review by the Finance Manager. The reporting pack also includes an update on major capital projects. Financial performance is monitored by the Principal and Senior Management Team. Performance is monitored and scrutinised by the Board. We reviewed the financial information monitored by senior management, committees and the Board and we are satisfied that the information is sufficiently detailed, including explanation of material variances to provide meaningful information to allow scrutiny and challenge of performance.

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Internal control and internal audit

It is the responsibility of the College to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility, as auditor, is to consider whether the College has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Our first year audit has been predominantly substantive in nature, and therefore we have not tested the operating effectiveness of key controls. Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control.

Through the course of our audit work we noted a number of observations in respect of ensuring robust financial management arrangements are in place at the College, such as around the use of an appropriate register for recording and maintaining information around fixed assets purchased by the College. We noted that these observations were already included in internal audit recommendations due for follow up and so did not duplicate recommendations here. We will follow up on the implementation of these as part of our 2017/18 financial statements audit, coordinating with internal audit as appropriate.

Wylie & Bisset LLP provide internal audit services for the College. Within the 2017 annual report to the Board, internal audit concluded:

"In our opinion Lews Castle College did have adequate and effective risk management and governance to manage its achievement of the college's objectives".

Their annual report did note they could only provide weak assurance over room utilisation and its follow up review, however this did not have an impact on our consideration with regards to the audit of the financial statements.

We have considered the work performed by internal audit during the year and did not identify any material issues that would impact on our overall opinion on the financial statements or our consideration of the wider scope aspects.

Financial management - what have we concluded?

- The College reported a deficit of £396,000 for the year (2015/16: deficit of £274,000). The main reason for the year on year movement is an increased staff costs in relation to social security and pensions. The underlying position in line with the SFC Accounts Direction reconciliation equates to an underlying deficit on operations of £19,000 (2015/16: surplus of £23,000) before accounting for non-cash items.
- The College has well established financial management arrangements, and we are satisfied that these are adequate for the management of its financial activities.

Financial sustainability is focused on the medium to longer term financial viability, and considers how effectively an audited body is planning to delivers its services over the medium term.

Financial sustainability

Financial sustainability interprets auditors' requirements under ISA 570 *Going concern* and looks forward to the medium (two to five years) and longer-term (longer than five years) to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

Audit Scotland's sector report: Scotland's colleges 2016, highlighted that between 2011 and 2015/16 the Scottish Government funding to the sector reduced by 18% in real terms. While the College's core funding has remained relatively stable in the current year of £3.6 million (2016: £3.5 million) management recognise that savings will be required in future years with envisaged constraints on future public sector resources. This requires an ability to transform and deliver significant recurring efficiency savings, while at the same time ensuring that the impact on core delivery is minimised.

The College has in recent years failed to meet student number targets, putting itself at risk of clawback of SFC funding allocated by UHI, the regional funding body. In March 2017 Audit Scotland reported in its section 22 report significant financial challenges for the College. Subsequently the College agreed revised student number targets with UHI to, in management's view, more appropriately reflect the College's capacity. We have outlined 2013/14 to 2017/18 targets against actual performance (where appropriate), together with the level of any over /under delivery.

Year	Measure	Target	Actual	Over / (Under) deliver
2013/14	WSUMs	8,994	8,336	(7.3%)
2014/15	WSUMs	8,994	8,082	(10.1%)
2015/16	Credits	6,376	5,131	(19.5%)
2016/17	Credits	5,200*	5,210	0%
2017/18	Credits	5,376	TBC**	TBC**

*Initially target was set at 6,376 but was revised by UHI based on forecast output for the year.

**2017/18 activity still to be delivered but management has advised they are confident of meeting the target.

The revised targets for student activity is now broadly in line with delivery since 2015/16. While there still remains a risk of under delivery, in our view this has reduced the challenge facing the College around achievement of student activity targets. Given the revision to target levels there could be an increased risk that under delivery could result in clawback of funds, unlike in recent years.

Financial planning – 2017/18

The 2017/18 budget was approved in June 2017. The College is budgeting a £183,000 deficit and a £53,000 underlying operating deficit after accounting for £130,000 of depreciation. An important part of ongoing financial assurance is regular updates to the Board on monitoring of expenditure against budget and the forecast outturn for the year. Financial performance is scrutinised by the senior management team and the Board.

Financial sustainability is focused on the medium to longer term financial viability, and considers how effectively an audited body is planning to delivers its services over the medium term.

Medium term financial planning - *Financial Forecast Return (FFR)*

The College has prepared its five-year financial forecasts 2017 to 2022 and submitted these to the SFC. These forecast annual deficits between £180,000 and £320,000, totalling £960,000 over the five year period. The forecasts have been prepared based on roll forwards of existing activities while management develops its new strategy from 2017 onwards. These forecasts currently do not distinguish the underlying operating position for the College but indicate the continued challenge facing the sector going forward.

The College's latest FFR forecasts for academic years 2017/18 and subsequent years were based on the audited financial statements for 2015/16, the outturn forecast for 2016/17, the budget for 2017/18 and a combination of assumptions, guidance and best-estimates for future years.

The key assumptions from review of the financial forecasts are:

- Scottish Funding Council core funding is assumed to increase in line with the guidance provided by the SFC, above the already agreed 2017/18 position.
- Staff costs to increase by 1% on top of the agreed national pay award from 2016/17. Non-staff costs are assumed to remain consistent with 2016/17 levels as the College continues to seek further joint procurement arrangements to minimise costs.

The forecasts demonstrate a good understanding of the long term pressures facing the College. Long-term financial planning is an essential aspect of understanding and developing a degree of flexibility to enable the College to respond to its financial challenges. While it is not always possible to make accurate assessments of future funding, building in scenario planning and sensitivity analysis to future budgets allows some ability to respond appropriately and to enable the Board to take appropriately informed decisions.

Financial sustainability - what have we concluded?

- The revised targets for student activity is now broadly in line with delivery since 2015/16. While there still remains a risk of under delivery, in our view this has reduced the challenge facing the College around achievement of student activity targets. Given the revision to target levels there could be an increased risk that under delivery could result in clawback of funds, unlike in recent years.
- Future financial forecasts for the College continue to be challenging reflecting the cost pressures facing the sector and the challenge in diversifying and strengthening the income base.

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information.

Governance and transparency

The Board and management of the College are responsible for establishing robust governance arrangements. This includes ensuring effective systems of internal control, including arrangements to safeguard public money, and compliance with applicable laws and regulations. Through our discussions with management and former auditor we are aware of a number of gaps in the governance arrangements in 2015/16. In our audit plan we identified governance and transparency as a wider scope area of focus.

Governance arrangements

Audit Scotland's section 22 report noted that the College had refreshed its Board membership in 2016/17, including providing inductions to its new members, addressing the issues raised in the prior year audit results report from the previous auditor. We confirmed this during our audit visit through review of key documents and meeting minutes. An external effectiveness review of governance arrangements was originally to be conducted by colleges no later than the 31 March 2017. The College decided to undertake their review to a later deadline, to reflect the fact that the Board members were not fully in place at the start of the financial and academic year. It was felt more appropriate to conduct the review when one full cycle of meetings had been completed.

We have reviewed the finalised effectiveness review provided by management in December 2017. The report conclusion states that substantial assurance has been provided over board effectiveness at the college. The body of the report identifies two areas of good practice but highlights 25 areas for improvement or continuing development. The areas for improvement have been agreed with management and included within an action plan, however at this time, the actions by management and timeframes for completion have yet to be confirmed. Some of the key areas for improvement included development of College KPI's for the Board's review, clarify over roles of the Board and senior management at the College, and completeness of key risks in the College's risk register.

We have noted through the course of our audit inquiries that the register of interest of members of the Board and key management personnel has not been updated since 2015. We have completed mitigating procedures to gain assurance over the disclosure of transactions in the year in the financial statements, however there remains a risk that without full disclosure of interests conflicts of interest may arise that should be considered by the College before making key decisions. We also note a number of other policies and procedures reviewed throughout the audit process had not been recently updated.

During the year management made the decision to restructure its standing committees, resulting in the Board of Management taking on greater responsibilities, with only the audit committee being retained as a standing committee. While this decision is a matter for the Board, we note this was made before the review of effectiveness was completed, and would consider it good practice to fully consider the structure of standing committees in light of the findings of the report.

The College has in place a number of the key requirements for good governance. We have reviewed Board minutes and papers and found these to set out clearly the matters considered and discussed. Standing Orders regulate how the business of the College is conducted.

Action plan points 2, 3 and 4

Governance and transparency – what have we concluded?

- We have concluded that the College arrangements for demonstrating good governance and transparency in its operational activity are continuing to develop.
- We have made three recommendations in respect of governance and transparency, in relation to ensuring actions from the Board effectiveness review are addressed, completion of registers of interest and other key policies and procedures, and review of standing committee structures.

Value for money is concerned with using resources effectively and continually improving services. This includes consideration of whether resources are being used effectively; services are improving and the College has appropriate arrangements to demonstrate Best Value.

Governance and transparency (continued)

Effective risk management

The risk management policy outlines the approach to risk management, the roles and responsibilities of the Board, the senior management team, and other key parties. It also outlines the key risk management processes and identifies the main reporting arrangements.

Transparency

The College had previously fallen behind on posting Board and standing committee agendas, minutes and papers on its website on a timely basis due to key staffing vacancies, however this process is now being managed more proactively. The College endeavours to make as much information available as possible, redacting for example certain financial information only where it would be considered to be reserved under freedom of information requests.

Value for Money

Strategic planning and performance reporting

The most recent College Strategic Plan ran from 2013-17 and was designed to align to the developing aims of the University of the Highlands and Islands. The plan period has come to an end in 2017 and the college is in the process of reviewing its strategic aims going forward.

The College publishes its performance information annually on its website as well as including key measures within the financial statements. As the Board develops and finalises its strategy, there is an opportunity to enhance current performance information reporting to provide a view of how performance compares to targets, and how those targets are expected to change over the period of the strategic plan.

Value for Money – what have we concluded?

- The College is in the process of reviewing its strategic aims as the current Strategic Plan ran from 2013-17. The College reports on its website in terms of annual performance, but as the Board develops and finalises its strategy, there is an opportunity to enhance current performance information reporting to provide a view of how performance compares to targets, and how those targets are expected to change over the period of the strategic plan.

Appendices

A. College responsibilities
B. Required communications with the Audit Committee
C. Auditor independence
D. Management representations
E. Action plan
F. Summary of audit differences

A. College’s responsibilities

The Code of Audit Practice summarises the responsibilities on all audited bodies falling within the public sector audit framework. We summarise these on this page.

Responsibilities of audited bodies	
Corporate governance	Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.
Financial statements and related reports	Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for: • preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. • maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures. • ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority. • maintaining proper accounting records. • preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body. Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.
Standards of conduct / prevention and detection of fraud and error	Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to: • such financial monitoring and reporting arrangements as may be specified • compliance with any statutory financial requirements and achievement of financial targets • balances and reserves, including strategies about levels and their future use • how they plan to deal with uncertainty in the medium and longer term • the impact of planned future policies and foreseeable developments on their financial position.
Best Value	The Scottish Public Finance Manual sets out that accountable officers appointed by the Principal Accountable Officer for the Scottish Administration have a specific responsibility to ensure that arrangements have been made to secure best value.

B. Required communications

There are certain additional communications that we must provide to the Audit Committee, in accordance with ISA (UK) 260 and other auditing standards, which are set out below.

<table>
<tr><th>Required communication - what is reported?</th><th>Our reporting to you</th></tr>
<tr><td>Terms of engagement

Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.</td><td>Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice</td></tr>
<tr><td>Planning and audit approach

Communication of the planned scope and timing of the audit, including any limitations.</td><td>Annual Audit Plan</td></tr>
<tr><td>Significant findings from the audit

• Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures
• Any significant difficulties encountered during the audit
• Any significant matters arising from the audit that were discussed with management
• Written representations we have requested
• Expected modifications to the audit report
• Any other matters significant to overseeing the financial reporting process
• Findings and issues around the opening balance on initial audits</td><td>This Annual Audit Report.</td></tr>
<tr><td>Going concern

Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:
• Whether the events or conditions constitute a material uncertainty
• Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements
• The adequacy of related disclosures in the financial statements</td><td>No conditions or events were identified, either individually or together to raise any doubt about the College's ability to continue for the 12 months from the date of our report.</td></tr>
<tr><td>Fraud

• Asking the Audit Committee whether they have knowledge of any actual, suspected or alleged fraud affecting the College
• Unless all those charged with governance are involved in managing the entity, any fraud identified or information obtained indicating that a fraud may exist involving:
(a) management;
(b) employees with significant roles in internal control; or
(c) others where the fraud results in a material misstatement in the financial statements.
► A discussion of any other matters related to fraud, relevant to Audit Committee responsibility.</td><td>This Annual Audit Report.</td></tr>
</table>

Required communication - What is reported?	Our reporting to you
Misstatements • Uncorrected misstatements and their effect on our audit opinion • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Significant corrected misstatements, in writing	This Annual Audit Report.
Significant deficiencies in internal controls identified during the audit • Significant deficiencies in internal controls identified during the audit.	This Annual Audit Report No significant deficiencies were identified in the course of our audit which required immediate communication to the Audit Committee.
Related parties Significant matters arising during the audit in connection with the College's related parties including, where applicable: • Non-disclosure by management • Inappropriate authorisation and approval of transactions • Disagreement over disclosures • Non-compliance with laws and/or regulations • Difficulty in identifying the party that ultimately controls the entity	We have noted in our report that registers of interest are not being maintained for those charged with governance and management. We have no other matters to report.
Subsequent events • Where appropriate, asking the Audit Committee whether any subsequent events have occurred that might affect the financial statements.	We have asked management and those charged with governance. We have no matters to report.
Other information • Where material inconsistencies are identified in other information included in the document containing the financial statements, but management refuses to make the revision.	We have no matters to report.
External confirmations • Management's refusal for us to request confirmations • We were unable to obtain relevant and reliable audit evidence from other procedures.	We have received all requested confirmations.
Consideration of laws and / or regulations • Audit findings of non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on "tipping off". • Asking the Audit Committee about possible instances of non-compliance with laws and/or regulations that may have a material effect on the financial statements, and known to the Audit ad Risk Governance Committee.	We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.
Independence • Communication of all significant facts and matters that have a bearing on EY's objectivity and independence.	This Annual Audit Report – Appendix C

C. Independence

Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the College.

What we are required to communicate?

Communicating key elements of the audit engagement partner's consideration of independence and objectivity such as:

- The principal threats
- Safeguards adopted and their effectiveness
- An overall assessment of threats and safeguards
- Information on the firm's general policies and processes for maintaining objectivity and independence
- Communications whenever significant judgments are made about threats to objectivity or independence and the appropriateness of safeguards.

Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan.

We complied with the Financial Reporting Council's Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that you and your Audit and Risk Management Committee consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the College Audit Committee on 5 December 2017.

Summary of fees

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 July 2017.

No non--audit fees were incurred in the year.

Auditor remuneration, outlined within our audit plan	£19,600
Fixed costs *	£1,970
Total fees	£21,570

* Fixed costs, which are determined by Audit Scotland, comprise £1,030 pooled costs, £940 contribution to Audit Scotland's costs.

D. Management representations

ISA (UK) 580*: Written representations,* requires the auditor to obtain written representation that management, including those charged with governance, has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant, their fair presentation.

Ernst & Young LLP
Atria One
144 Morrison Street,
Edinburgh, EH3 8EB
[Date]

This letter of representations is provided in connection with your audit of the consolidated financial statements of Lews Castle College ("the College") and its group for the year ended 31 July 2017. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the College and its group consolidated financial statements give a true and fair view of the College and it`s group consolidated financial position as of 31 July 2017 and of its income and expenditure for the year then ended in accordance with applicable law and the Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland, and the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

We understand that the purpose of your audit of our consolidated financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose – all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

A. Financial Statements and Financial Records

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the consolidated financial statements in accordance with applicable law and the Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland, and the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

2. We acknowledge, as members of management of the College and it group, our responsibility for the fair presentation of the consolidated financial statements. We believe the consolidated financial statements referred to above give a true and fair view of the financial position, financial performance (or results of operations) and cash flows of the College and its group in accordance with applicable law and the Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland, and the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

3. The significant accounting policies adopted in the preparation of the consolidated financial statements are appropriately described in the consolidated financial statements.

4. As members of management of the College and its group, we believe that the College has a system of internal controls adequate to enable the preparation of accurate consolidated financial statements in accordance with applicable law and the Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland, and the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.

5. There are no unadjusted audit differences identified during the current audit and pertaining to the latest period presented.

B. Fraud

1. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.

2. We have disclosed to you the results of our assessment of the risk that the consolidated financial statements may be materially misstated as a result of fraud.

3. We have no knowledge of any fraud or suspected fraud involving management or other employees who have a significant role in the College's and its group internal controls over financial reporting. In addition, we have no knowledge of any fraud or suspected fraud involving other employees in which the fraud could have a material effect on the consolidated financial statements. We have no knowledge of any allegations of financial improprieties, including fraud or suspected fraud, (regardless of the source or form and including without limitation, any allegations by "whistleblowers") which could result in a misstatement of the consolidated financial statements or otherwise affect the financial reporting of the College and its group.

C. Compliance with Laws and Regulations

1. We have disclosed to you all identified or suspected non-compliance with laws and regulations whose effects should be considered when preparing the consolidated financial statements.

D. Information Provided and Completeness of Information and Transactions

1. We have provided you with:
   - Access to all information of which we are aware that is relevant to the preparation of the consolidated financial statements such as records, documentation and other matters;
   - Additional information that you have requested from us for the purpose of the audit; and
   - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
2. All material transactions have been recorded in the accounting records and are reflected in the consolidated financial statements.
3. We have made available to you all minutes of the meetings of the Board of Management of the College and its group and its relevant committees (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meetings.
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the College's and its group related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the consolidated financial statements.
5. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
6. We have disclosed to you, and the College and its group have complied with, all aspects of contractual agreements that could have a material effect on the consolidated financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

E. Liabilities and Contingencies

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the consolidated financial statements.
2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in the consolidated financial statements all guarantees that we have given to third parties.
4. No other claims in connection with litigation have been or are expected to be received.

F. Subsequent Events

1. As disclosed in the consolidated financial statements, there have been no events subsequent to period end which require adjustment of or disclosure in the consolidated financial statements or notes thereto.

G. Going concern

1. We have not identified any material uncertainties that may cast significant doubt about the College's and its group ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the consolidated financial statements are authorised for issue.

H. Other information

1. We acknowledge our responsibility for the preparation of the other information. The other information comprises the Management Commentary, the Remuneration Report, the Annual Governance Statement and the Statement of Responsibilities.
2. The disclosures within the Management Commentary reflects our understanding of the financial and non-financial performance of the College and its group over the reporting year, is consistent with the consolidated financial statements and has been prepared in accordance with relevant guidance.
3. The information given in the Annual Governance Statement for the financial year for which the consolidated financial statements are prepared reflects the College's and its group governance framework, is consistent with the consolidated financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016).
4. The information contained in the auditable part of the Remuneration Report has been prepared in accordance with Accounts direction.
5. We confirm that the content contained within the other information is consistent with the consolidated financial statements.

Yours faithfully,

____

Principal

____

Chair of the Board of Management of the College

E. Action Plan

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Board or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and risk**	**Our recommendation and grading**	**Management response**
1	**Actuarial assumptions** In respect of the key assumptions around discount rates and inflation used in the calculation of pension liabilities at year end, our actuaries noted that the assumptions were within a range we consider acceptable for the year end date. However, they noted the underlying methodology used to obtain these assumptions was not as robust as they could be, in particular around the estimates of future cash flows for pension costs by the College. While we are comfortable with the assumptions used for the 2017 financial statements there is a risk that future assumptions are not considered appropriate.	Management should ensure our audit findings are fed back to the actuaries in advance of the 2017/18 preparation of the FRS102 pensions report and assumptions calculation. *Grade 3*	Agreed. Management will share a detailed explanation of the auditor's findings with the actuaries and share any actuary response with the auditors to agree in advance of the 17/18 financial statement audit.
2	**Board effectiveness review** An external effectiveness review of governance arrangements was conducted by the College, later than initially required to reflect the fact that the Board members were not in place at the start of the financial and academic year. We have not obtained a copy of the final report for review at the time of completion of this report, and so have not been able to make an assessment of the findings.	Management should ensure the review of effectiveness is finalised and considered as soon as possible, with actions to make the required improvements considered immediately. *Grade 1*	Agreed. The review is now finalised and will be shared along with actions imminently.

E. Action Plan

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Board or management to action.

No.	Findings and risk	Our recommendation and grading	Management response
3	**Register of Interest and other policies** We have noted through the course of our audit inquiries that the register of interest of members of the Board and key management personnel has not been updated since 2015. We have completed mitigating procedures to gain assurance over the disclosure of transactions in the year in the financial statements, however there remains a risk that without full disclosure of interests conflicts of interest may arise that should be considered by the College before making key decisions. We have also noted a number of other policies and procedures have not been formally updated in 2016/17.	Management should ensure that the Board of Management and senior management at the College complete updated registers of interest and consider any possible conflicts arising going forward. Management should also ensure all policies and procedures at the College are reviewed to ensure they remain up to date and appropriate. *Grade 2*	Agreed. The registers of interest will be updated at the December board meeting and then on an annual basis thereafter. All other policies and procedures will be reviewed to ensure they are up to date and subject to sufficiently routine review.
4	**Arrangement of standing committees** During the year management made the decision to restructure its standing committees, resulting in the Board of Management taking on greater responsibilities, with only the audit committee being retained as a standing committee. While this decision is a matter for the Board, we note this was made before the review of effectiveness was completed, and would consider it good practice to fully consider the structure of standing committees in light of the findings of the report.	Management should ensure the review of effectiveness results are considered in the assessment of the structure of committees going forward. *Grade 2*	Agreed. Management will consider in conjunction with the findings of the effectiveness review.

F. Summary of audit differences

There were a number of adjustments processed to the unaudited financial statements as a result of our audit work. The impact of these is summarised below.

Summary of audit differences – adjusted differences

No.	Account	Comprehensive income and expenditure statement (Increase) / Decrease £000	Balance sheet (Decrease) / Increase £000
1	***Being an accrual of previously unrecorded income at yearend***		
	Balance Sheet – Accrued Income		12.8
	CIES – Other Income	(12.8)	
2	***Being a correction of year-end cash from review of the bank reconciliation***		
	Balance Sheet - Cash		18
	Balance Sheet – Prepayments and Accrued Income		(18)

EY | Assurance | Tax | Transactions | Advisory

About EY
EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

Ernst & Young LLP

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

© 2017 Ernst & Young LLP. Published in the UK.
All Rights Reserved.

ey.com