

Scottish Funding Council

2016/17 Annual Audit Report



 AUDIT SCOTLAND

Prepared for Scottish Funding Council and the Auditor General for Scotland

June 2017

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Key messages

Audit of the 2016/17 financial statements

- 1** The financial statements of the Scottish Funding Council (the Council) give a true and fair view of the financial position and its expenditure and income.
- 2** The expenditure and income in the financial statements was incurred or applied in accordance with applicable enactments and guidance.
- 3** The other information in the annual report and accounts is consistent with the financial statements and prepared in accordance with legal requirements.

Financial management

- 4** The Council effectively managed its finances in 2016/17.
- 5** Systems of internal control operated effectively in 2016/17.
- 6** The Council has satisfactory budget monitoring and control arrangements in place.

Financial sustainability

- 7** The Council has established a sound basis for financial sustainability.
- 8** The Council should work to complete longer term financial plans closely linked to the objectives set out in its 2015-18 strategic plan.
- 9** The Council should consider the implications on its future financial position of non-recovery and clawback of European funding and ensure this risk is reflected in its financial plans.

Governance and transparency

- 10** The Council has effective governance arrangements in place; it may wish to consider whether there are opportunities to further enhance transparency.
- 11** The Council's risk management processes are operating effectively and are fully embedded within its overall governance arrangements.

Value for money

- 12** The Council has implemented a performance management framework and is reviewing this to ensure performance measures remain relevant.
- 13** The Council has acted proactively in self-assessing against the principles of Best Value and developing a Best Value Improvement Plan.

Introduction

1. This report is a summary of our findings arising from the 2016/17 audit of the Scottish Funding Council (the Council).

2. The scope of our audit was set out in our Annual Audit Plan presented to the March 2017 meeting of the Audit and Compliance Committee. This report comprises:

- an audit of the annual report and accounts
- consideration of the wider dimensions set out in the [Code of Audit Practice 2016](#) as illustrated in [Exhibit 1](#).

Exhibit 1

Audit dimensions



Source: Code of Audit Practice 2016

3. The main elements of our audit work in 2016/17 have been:

- an interim audit of the Council's main financial systems resulting in an interim audit report presented to the Audit and Compliance Committee in March 2017
- an audit of the Council's 2016/17 annual report and accounts including the issue of an independent auditor's report setting out our opinions.

4. The Council is responsible for preparing financial statements that give a true and fair view, for the accuracy of the other information in the annual report and

accounts, and for establishing effective arrangements for governance, propriety and regularity that enable the Council to successfully deliver its objectives.

5. Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice 2016](#), supplementary guidance and, guided by the auditing profession's ethical guidance.

6. These responsibilities include giving independent opinions on the financial statements, regularity, the remuneration and staff report, the performance report and the governance statement. We also review and report on the arrangements within the Council to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

7. Further details of the respective responsibilities of management and the auditor can be found in the [Code of Audit Practice 2016](#) and supplementary guidance.

8. The weaknesses or risks identified in this report are only those that have come to our attention during our normal audit work, and may not be all that exist. Also, our annual audit report contains an action plan at Appendix 1 (page 22). It sets out specific recommendations, responsible officers and dates for implementation.

9. Communication in this report of matters arising from the audit of the annual report and accounts or of risks or of weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

10. As part of the requirement to provide fair and full disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2016/17 audit fee for the audit was set out in our Annual Audit Plan and remains unchanged.

11. This report is addressed to both the Council and the Auditor General for Scotland and will be published on Audit Scotland's website www.audit-scotland.gov.uk.

12. We would like to thank all management and staff who have been involved in our work for their cooperation and assistance during the audit.

Part 1

Audit of 2016/17 financial statements



Main judgements

The financial statements of the Council give a true and fair view of the financial position and its expenditure and income.

The expenditure and income in the financial statements was incurred or applied in accordance with applicable enactments and guidance.

The other information in the annual report and accounts is consistent with the financial statements and prepared in accordance with legal requirements.

Unqualified audit opinions

13. The annual report and accounts for the year ended 31 March 2017 will be presented to the Board for approval on 23 June 2017. We reported, within our independent auditor's report:

- an unqualified opinion on the financial statements;
- an unqualified opinion on regularity of expenditure and income; and
- an unqualified audit opinion on the remuneration and staff report, performance report and governance statement.

14. Additionally, we are satisfied that there are no matters which we are required by the Auditor General to report by exception.

Submission of annual report and accounts for audit

15. We received the unaudited annual report and accounts on 3 May 2017. These were incomplete. We received the performance report and the accountability report and adjustments to figures (including for non current assets, trade and other receivables, and trade and other payables) at later dates.

16. The working papers provided with the unaudited annual report and accounts were of a satisfactory standard and finance staff provided support to the audit team which helped ensure completion of the final accounts audit process.

Risk of material misstatement

17. Appendix 2 (page 24) provides a description of those assessed risks of material misstatement that were identified during the planning process which had the greatest effect on the overall audit strategy, the allocation of resources to the audit and directing the efforts of the audit team.

The annual report and accounts are the principal means of accounting for the stewardship of resources and performance in the use of those resources.

Materiality

18. Materiality defines the maximum error that we are prepared to accept and still conclude that our audit objective has been achieved. The assessment of what is material is a matter of professional judgement. It involves considering both the amounts and nature of any misstatement.

19. Our initial assessment of materiality for the annual report and accounts was undertaken during the planning phase of the audit. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.

20. On receipt of the annual report and accounts we reviewed our original materiality calculations and revised them accordingly. These are summarised in [Exhibit 2](#).

Exhibit 2

Materiality values

Materiality level	Amount
Overall materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It was set at 1% of gross expenditure for the year ended 31 March 2017.	£18.0 million
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 75% of overall materiality.	£13.5 million
Reporting threshold – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at approximately 5.5% of overall materiality.	£100,000

Source: Audit Scotland

Evaluation of misstatements

21. There were no material adjustments to the unaudited financial statements arising from our audit. All individual misstatements which exceeded our reporting threshold have been amended in the audited financial statements.

Significant findings from the audit

22. International Standard on Auditing (UK and Ireland) 260 requires us to communicate significant findings from the audit to you. These are summarised in [Exhibit 3](#).

Exhibit 3

Significant findings from the audit of financial statements

Issue	Resolution
<p>1. European funding</p> <p>The Council is managing two European Social Fund (ESF) projects over the period 2015/16 to 2017/18. The Council provides around £8 million a year for these projects in Lowlands and Uplands Scotland (with some additional funding provided for the Highlands and Islands transitional region) and claims match European funding through the Scottish Government. The Council accounts for this funding on a cash basis. At the end of 2016/17 the Council submitted claims to the Scottish Government for £11.5 million in respect of 2015/16 ESF funding. The Council has not recognised ESF income in its 2016/17 financial statements due to the high level of uncertainty over the level of income it will receive from these claims.</p>	<p>Management have agreed to carry out an annual assessment of the accounting treatment of ESF funding to ensure it is in accordance with the FReM.</p>

Source: Audit Scotland

Other findings

23. The performance report section of the annual report and accounts has been prepared in line with the minimum requirements of the Government financial reporting manual (the FReM). We have, however, identified a number of improvements which could be made to the performance analysis and financial performance report. These include:

- more detailed explanation of delivery targets and analysis of performance against these
- a more comprehensive outline of how the Council supports good governance in colleges and universities
- more detailed analysis and interpretation of financial performance.

These improvements would ensure the performance report provides a complete and meaningful analysis of how the Council performed during the year. Officers have agreed to consider them in preparing the 2017/18 performance report.

Recommendation 1

The Council should review the content of its 2017/18 performance report to ensure it provides users of the annual report and accounts with a sufficiently detailed and understandable analysis of its performance.

24. During our audit testing we noted differences between the asset values recorded in the Council's fixed asset register and the corresponding values recorded in its financial ledger. The individual differences are not material and the net book values for each category of asset have been correctly recorded in the financial statements. However, it is important that the Council maintains an

accurate record of its assets to ensure it correctly accounts for these in future years.

Recommendation 2

The Council should review its fixed asset register and take corrective action to ensure individual asset values are accurately recorded.

25. Our audit identified some presentational and disclosure issues which were discussed with management. These were adjusted and reflected in the audited financial statements.

Part 2

Financial management



Main judgements

The Council effectively managed its finances in 2016/17.

Systems of internal control operated effectively in 2016/17.

The Council has satisfactory budget monitoring and control arrangements in place.

Financial performance in 2016/17

26. The main financial objective for the Council is to ensure that the financial outturn for the year is within the budget allocated by Scottish Ministers.

27. The Council underspent its DEL budget by £18.8 million in 2016/17; however no opportunities were lost to the sectors. The underspend comprises:

- £10.0 million higher education institutions ring-fenced financial transaction budget which has been carried forward to the 2017/18 financial year
- £3.5 million ring-fenced college non-profit distribution budget due to a delay in taking occupation of Ayrshire and Glasgow City College buildings
- £5.3 million from colleges repaying loans entered into before April 2014 which do not score as resource expenditure.

28. The Council's financial performance against DEL is shown in [Exhibit 4](#). Performance against higher education, further education and running costs budgets is separately recorded.

Exhibit 4

Performance against DEL in 2016/17

Performance	Final budget £m	Actual outturn £m	Overspend/ (underspend) £m
Higher Education Resource	1,071.0	1,069.5	(1.5)
Higher Education Capital	73.2	63.2	(10.0)
Further Education Resource and Capital	602.9	595.6	(7.3)
Running costs	7.5	7.5	0
Total DEL	1,754.6	1,735.8	(18.8)

Source: Scottish Funding Council resource return

29. The Council monitors its financial position for higher and further education throughout the year through resource returns to the Scottish Government. The Council manages its budget through an annual re-profiling exercise to re-allocate funds between the higher education, further education and running costs budgets. The Scottish Government approved total re-profiling of £4.6 million, which equates to 0.25% of the total grant-in-aid budget from the Scottish Government.

30. We are satisfied that the Council effectively managed its finances in 2016/17 as illustrated by its performance against DEL and use of re-profiling to manage variations between its higher and further education budgets.

Internal controls

31. As part of our audit we identify and inspect the key internal controls in those accounting systems which we regard as significant for the production of the financial statements. Our objective is to gain assurance that the Council has systems of recording and processing transactions which provide a sound basis for the preparation of the financial statements.

32. Our findings were included in an interim audit report presented to the Audit Committee in March 2017. We concluded that the Council has adequate systems of internal control. We identified a small number of control weaknesses. None of these was significant enough to affect the Council's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

Budgetary processes

33. We also reviewed the Council's budgetary processes and budget monitoring arrangements. From our review of budget monitoring reports and review of committee papers we confirmed that senior management and Council members receive regular, timely and up to date financial information on the financial position.

34. We concluded that the Council has satisfactory budgetary monitoring and control arrangements in place that allow both members and officers to carry out effective scrutiny of its finances.

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

Prevention and detection of fraud and irregularity

35. We assessed the Council's arrangements for the prevention and detection of fraud. Our audit work covered a number of areas such as whistleblowing and a review of the counter fraud processes.

36. We concluded that the Council is proactive in promoting fraud awareness and had appropriate and adequate arrangements in place for fraud detection and prevention during 2016/17.

National Fraud Initiative

37. The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise coordinated by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify 'matches' that might suggest the existence of fraud or error ([Exhibit 5](#)).

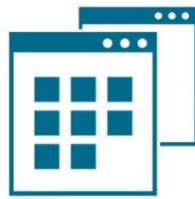
Exhibit 5

Total number of matches



100

Number recommended for investigation



19

Completed/closed investigations



19

Source: Scottish Funding Council

38. The exercise identified 100 matches with 19 recommended for investigation. The numbers involved are small and the Council has been proactive in investigating the matches and will report the outcome of NFI activity to the Audit and Compliance Committee in due course.

Standards of conduct and arrangements for the prevention and detection of bribery and corruption

39. We have reviewed the arrangements in place to maintain standards of conduct. In line with the requirements of 'On Board: A Guide for Board Members of Public Bodies in Scotland', the Council has issued its own Code of Conduct. There is also a Code of Conduct in place for staff. There are established procedures for preventing and detecting any breaches of these standards including any instances of corruption.

40. Based on our review of the evidence we concluded that the Council has appropriate arrangements in place for the prevention and detection of bribery and corruption. We are not aware of any specific issues that we need to bring to your attention.

Part 3

Financial sustainability



Main judgements

The Council has established a sound basis for financial sustainability.

The Council should work to complete longer term financial plans closely linked to the objectives set out in its 2015-18 strategic plan.

The Council should consider the implications on its future financial position of non-recovery and clawback of European funding and ensure this is reflected in its financial plans.

Financial planning

41. The Council received its draft budget allocation from the Scottish Government in April 2017. The total budget allocation is £1,735 million. The budget allocation covers the funding the Council distributes to Higher and Further education institutions and its own running costs.

42. The Council announced indicative funding allocations to Universities and Colleges in February 2017. It announced final outcome agreement funding allocations in May 2017 based on the budget allocation from the Scottish Government. The final allocations were broadly unchanged from the indicative allocations.

43. The running costs grant-in-aid budget for 2017/18 is £7.2 million which is the same as in 2016/17. The Council has budgeted for additional costs in 2017/18 from a planned office move. The full cost of the move is estimated to be £1.1 million. It plans to meet these costs from funds brought forward and in year savings, principally from a reduction in the facilities budget. The Council anticipates that the office move will in time significantly reduce its fixed accommodation costs.

2016/17 financial position

44. The Statement of Financial Position summarises what is owned and owed by the Council. This shows taxpayers' equity – an accounting measurement of the amount invested that has continuing public benefit. It shows how much of this has arisen from the application of revenues and that which has resulted through changes over time in the value of assets.

45. The Council's net expenditure in 2016/17 was £1,764.5 million. The Council is funded from Scottish Government grant-in-aid and other Scottish and UK Government grants. This funding totalled £1,763.8 million in 2016/17 which resulted in an accounting deficit of £0.7 million. This deficit has been met from reserves, which have reduced to £9.1 million as at 31 March 2017. The year end position is largely attributable to movements in working capital.

46. The council is funded in line with the financial year but distributes funds to higher and further education institutions based on their academic year. The

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they are delivered.

academic year runs from the beginning of August to the end of July. The Council holds reserves to manage fluctuations in the distribution of funding between the financial and academic years.

47. We have concluded that the Council has established a sound basis for financial sustainability.

Medium to long term financial planning

48. We reviewed the financial planning processes and assessed how effective they are in identifying and addressing risks to financial sustainability across the medium and long term. We have taken into account that the Council is mainly funded through grant-in-aid (99% of 2016/17 funding) and this is set on a year-on-year basis by the Scottish Government.

49. The Council's strategic plan for 2015-18 contains high level objectives on the use of resources but it has yet to establish detailed financial plans underpinning the strategic plan. The Council is developing longer term financial plans for its running costs, higher education and further education budgets. The Council is using sensitivity analysis and scenario planning to ensure its financial plans account for the impact of significant developments affecting the higher and further education sector such as:

- the implications of Brexit
- the outcome of national bargaining for teaching staff pay
- the implications of a full conditions survey of the College estate.

The Council is also working on a three year running costs budget position.

50. The Council recognises that further work is required before longer term financial plans are in place. It is part of a Strategic Futures Group which includes representation from higher education institutions and the Scottish Government. This group is considering the financial implications of policy change resulting from Brexit and widening access.

Recommendation 3

The Council should work to complete medium to longer term financial plans which measure the likely financial impact of major developments affecting the higher and further education sector. These plans should be linked closely to the objectives set out in its 2015-18 strategic plan.

European funding

51. The Council is managing two European Social Fund (ESF) projects over the period 2015/16 to 2017/18. The Council provides around £8.0 million a year for these projects in Lowlands and Uplands Scotland (with some additional funding provided for the Highlands and Islands transitional region) and claims match European funding through the Scottish Government. The Council accounts for this funding on a cash basis. At the end of 2016/17 the Council submitted claims to the Scottish Government for £11.5 million in respect of 2015/16 ESF funding. The Council has not recognised ESF income in its 2016/17 financial statements due to the high level of uncertainty over the level of income it will receive from these claims.

52. The Scottish Government carried out an audit of the 2013-15 ESF 'Skills for a Competitive Workforce' programme in 2016/17. The Council received the final verification and compliance report from the Scottish Government in March 2017.

The Scottish Government found there was ineligible expenditure of approximately £37,000 due to a small amount of college expenditure that lacked some evidence and did not fully comply with regulations. It also found that the Council was not fully complying with its enrolment procedures and conditions for ESF funded courses. This has resulted in clawback of approximately £16,000 in funding. The Council has changed its guidance in response to some of the Scottish Government's findings. The Council has identified a risk of a further, more significant clawback from its 2015-18 ESF programmes as the previous enrolment procedures were in place for activity currently being funded through these programmes.

Recommendation 4

The Council should consider the implications on its future financial position of non-recovery and clawback of European funding and ensure this is reflected in its financial plans.

Part 4

Governance and transparency



Main judgements

The Council has effective governance arrangements in place; it may wish to consider whether there are opportunities to further enhance transparency.

The Council's risk management processes are operating effectively and are fully embedded within its overall governance arrangements.

Governance arrangements

53. The corporate governance framework within the Council is centred around the Council Board, supported in its role by six committees including the Audit and Compliance Committee and the Finance Committee. The Board is responsible for establishing the strategic processes within the Council and arrangements for ensuring the proper conduct of the affairs of the Council.

54. The Board delegates responsibility for scrutiny to the Audit and Compliance Committee which meets quarterly. Each year the Audit and Compliance Committee undertakes a self-assessment exercise. The Audit and Compliance Committee members demonstrate a clear understanding of their responsibilities, and of the respective roles of management, internal audit and external audit. Members participate in development opportunities on an ongoing basis to ensure their skills adapt to changing demands. A recent training session jointly delivered by internal and external audit helped support members' understanding of the current context for public finances in Scotland.

55. We concluded that the Council has effective governance, decision making and scrutiny arrangements in place which provide an appropriate framework for organisational decision making.

The Annual Governance Statement

56. Under the FReM, the Council must prepare an annual governance statement within the Annual Report and Accounts. Guidance is set out within the Scottish Public Finance Manual (SPFM) for the content of the statement and provides assurances around the achievement of the organisation's strategic objectives.

57. The SPFM does not prescribe a format for the annual governance statement, but sets out minimum requirements for central government bodies. The process undertaken by the senior management team included conducting an assurance mapping process which underpinned the preparation of the governance statement.

58. We concluded that the 2016/17 annual governance statement complies with the guidance issued by the Scottish Ministers and based on our knowledge and work performed presents an accurate picture of governance arrangements and matters.

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.

Internal audit

59. Internal audit provides the Council and the Accountable Officer with independent assurance on the Council's overall risk management, internal control and corporate governance processes.

60. The internal audit function is carried out by Scott Moncrieff. We carried out a review of the adequacy of the internal audit function and concluded that it operates in accordance with the Public Sector Internal Audit Standards and has sound documentation standards and reporting procedures in place.

61. To avoid duplication of effort we place reliance on the work of internal audit wherever possible. In 2016/17 we reviewed and considered the findings of the following internal audit reports:

- Financial Controls Self Assessment
- Grant Funding Distribution
- Further Education Reporting/Accounting Arrangements
- Internal Communications
- Review of Edinburgh College's Business Transformation Plan.

Risk management

62. We reviewed the risk management processes within the Council. The Council's risk strategy is implemented through a risk management framework which helps identify, assess and manage risk effectively. The Council maintains a corporate risk register which is regularly reviewed by the senior management team. There are also periodic reviews of the risk register by the Audit and Compliance Committee which has responsibility for providing assurances to the Council that the risk management strategy and framework are effective. The Council has further developed its approach to risk management during 2016/17 by developing individual risk registers for key functions or projects and by providing briefing and training material to staff on risk management.

63. We concluded that risk management processes are operating effectively and are fully embedded within the Council's governance arrangements.

Transparency

64. Transparency means that stakeholders, including the public, have access to understandable, relevant and timely information about how the Council is taking decisions and how it is using resources.

65. Agendas, minutes and papers of Board and committee meetings are published on the Scottish Funding Council website. The Council uses the Freedom of Information Act to withhold publication of a wide range of papers. This is used for areas which are considered to be of a confidential or sensitive nature. Examples of areas where papers have been withheld include:

- funding allocations
- analysis of College and University financial positions
- follow up of internal audit recommendations.

66. With increasing expectations for enhanced openness in the conduct of public business the Council may wish to consider whether there are opportunities to

further enhance transparency. For example, the Council could review how it applies Freedom of Information guidance in making available information contained in Board and committee papers.

Part 5

Value for money



Main judgements

The Council has implemented a performance management framework and is reviewing this to ensure performance measures remain relevant.

The Council has acted proactively in self-assessing against the principles of Best Value and developing a Best Value Improvement Plan.

Performance management

67. Accountable officers have a specific responsibility to ensure that arrangements have been made to secure Best Value. The Auditor General may require that we consider whether accountable officers have put in place appropriate arrangements to satisfy their corresponding duty of Best Value. Where such requirements are not specified we may, in conjunction with our client agree to undertake local work in this area.

68. The Council introduced a performance report following the approval of its 2015-18 strategic plan in November 2015. The most recent performance report was reported to the October 2016 meeting of the Council's Board. The performance report includes a range of measures of inputs, activity, outputs, and outcomes linked to the strategic plan. The indicators and targets used in the performance report are discussed with stakeholders, including the Scottish Government, to ensure they remain relevant.

69. The Council recognises that it can further develop performance reporting and management. At the April 2017 Finance Committee members discussed how performance measures could be further strengthened. This included consideration of whether:

- the performance report measured the right things
- further measures should be developed
- appropriate evidence is available to support the measures.

Following this discussion, members agreed that performance objectives and measures should be updated to reflect the outcome of the Scottish Government's Review of Enterprise and Skills.

Self assessment

70. The Council carried out a self assessment against the principles of Best Value in 2016/17. The results of this exercise were considered by the Audit and Compliance Committee in March 2017. This is the fourth such exercise, following previous self assessments in 2005/06, 2008/09 and 2012/13. The 2016/17 self assessment measures the Council against the Best Value characteristics an organisation should be able demonstrate, as identified by the Scottish

Value for money is concerned with using resources effectively and continually improving services.

Government. The exercise was undertaken through questionnaires which asked senior officers to provide a qualitative assessment against the Best Value characteristics.

71. The Council has concluded from its self assessment that it is able demonstrate its characteristics are either “well-developed” or “under-development”. The Council has identified nine actions for improvement. These will be brought together to form a Best Value Improvement Plan which will be included in the Council’s 2017/18 operational plan.

72. We are encouraged that the Council has been proactive in taking action to ensure it has appropriate arrangements for securing Best Value in place.

National performance audit reports

73. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2015/16, we published a number of reports which are of direct interest to the board. These are outlined in Appendix 3 accompanying this report.

74. The Council is actively involved in the consideration and review of the Scotland’s colleges overview reports.

Appendix 1

Action plan 2016/17

2016/17 recommendations for improvement



Page
no.

Issue/risk

Recommendation

Agreed management
action/timing

9	<p>1. Performance report</p> <p>We have identified a number of improvements which could be made to the performance analysis and financial performance report. These improvements would ensure the performance report provides a complete and meaningful analysis of how the Council performed during the year. Officers have agreed to consider them in preparing the 2017/18 performance report.</p> <p>Risk</p> <p>The performance report does not provide users of the accounts with a meaningful analysis of the Council's performance.</p>	<p>The Council should review the content of its 2017/18 performance report to ensure it provides users of the annual report and accounts with a sufficiently detailed and understandable analysis of its performance.</p>	<p>Agreed. This work will be taken forward during 2017/18.</p>
9-10	<p>2. Accuracy of asset register</p> <p>During our audit testing we noted differences between the asset values recorded in the Council's fixed asset register and the corresponding values in its financial ledger. The individual differences are not material and the net book values for each category of asset have been correctly recorded in the financial statements. However, it is important that the Council maintains an accurate record of its assets to ensure it correctly accounts for these in future years.</p> <p>Risk</p> <p>Capital is incorrectly accounted for in future financial statements.</p>	<p>The Council should review its fixed asset register and take corrective action to ensure individual asset values are accurately recorded.</p>	<p>Agreed. The fixed asset register will be updated during 2017/18.</p>
15	<p>3. Medium to long term financial</p>	<p>The Council should work to complete medium to longer</p>	<p>Agreed. This work will be taken forward during</p>



Page no.	Issue/risk	Recommendation	Agreed management action/timing
	<p>planning</p> <p>The Council's Strategic Plan for 2015-18 contains high level objectives on the use of resources but it has yet to establish detailed financial plans underpinning the strategic plan. The Council is developing longer term financial plans for its running costs, higher education and further education budgets.</p> <p>Risk</p> <p>The Council cannot accurately forecast the financial impact of ongoing developments and take action to manage the future impact on its financial position.</p>	<p>term financial plans which measure the likely financial impact of major developments affecting the higher and further education sector. These plans should be linked closely to the objectives set out in its 2015-18 strategic plan.</p>	<p>2017/18.</p>
<p>15-16</p>	<p>4. European funding</p> <p>At the end of 2016/17 the Council submitted claims to the Scottish Government for £11.5 million in respect of 2015/16 European Social Fund (ESF) activity. The Council has not recognised ESF income in its 2016/17 financial statements due to the high level of uncertainty over the level of income it will receive from these claims. In addition, the Scottish Government has advised the Council that it will clawback around £16,000 in 2013-15 ESF funding. The Council has identified a risk of a further, more significant clawback from its 2015-18 ESF programmes.</p> <p>Risk</p> <p>The council does not receive the expected level of ESF funding from the Scottish Government and is subject to a further clawback of funding.</p>	<p>The Council should consider the implications on its future financial position of non-recovery and clawback of European funding and ensure this is reflected in its financial plans.</p>	<p>Agreed. ESF funding is already a standing item on the Finance Committee agenda.</p>

Appendix 2

Significant audit risks identified during planning

The table below sets out the audit risks we identified during our planning of the audit and how we addressed each risk in arriving at our conclusion. The risks are categorised between those where there is a risk of material misstatement in the annual report and accounts and those relating to our wider responsibility under the [Code of Audit Practice 2016](#).

Audit Risk	Assurance procedure	Results and conclusions
Risks of material misstatement in the financial statements		
<p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit.</p> <p>This includes consideration of the risk of management override of controls to change the position disclosed in the financial statements.</p>	<p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Focused testing of accruals and prepayments.</p> <p>Testing transactions to confirm that they are accounted for in the correct period.</p> <p>Evaluation of any significant transactions that are outside the normal course of business.</p>	<p>We concluded from our audit testing that all 2016/17 journal entries, accounting estimates and judgements, and significant transactions we reviewed were appropriate.</p> <p>No issues were highlighted from our controls and year end testing that would indicate management override of controls.</p>
<p>2 Risk of fraud over income</p> <p>The Scottish Funding Council receives income in addition to Scottish Government funding. The extent and complexity of income means that, in accordance with ISA 240, there is an inherent risk of fraud.</p>	<p>Analytical procedures on income streams.</p> <p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p>	<p>We did not identify any significant issues from our detailed testing of grant income.</p> <p>We confirmed through audit testing that revenue had been recognised appropriately in the financial statements.</p>
<p>3 Risk of fraud over expenditure</p> <p>The Code of Audit Practice requires consideration of risk of fraud over expenditure (excluding payroll costs which are already a core part of all annual audits).</p>	<p>Analytical procedures on expenditure streams.</p> <p>Detailed testing of expenditure transactions focusing on the areas of greatest risk.</p>	<p>We found no significant issues from our detailed testing of running costs expenditure.</p>
<p>4 Grants paid to colleges and universities</p> <p>The main activity of the Scottish Funding Council is the award and payment of grants</p>	<p>Review of the processes and controls in place for payment of grants.</p> <p>Focused substantive testing of formula based grant awards to</p>	<p>We reviewed the controls in place for the payment of grants as part of our interim audit and did not identify any significant issues.</p> <p>We found no misstatements of</p>





















Audit Risk	Assurance procedure	Results and conclusions
<p>to colleges and universities. There is a risk that grants paid to institutions are incorrectly recorded in the financial statements.</p>	<p>individual bodies. Sample testing of grant commitments at the year end. Review Internal Audit's Grant Funding Distribution report.</p>	<p>grant payments to institutions from our sample testing of in year grant payments, commitments relating to the remainder of the academic year 2015/16, and funding clawbacks.</p>
<p>Risks identified from the auditor's wider responsibility under the Code of Audit Practice</p>		
<p>5 Financial management and sustainability</p> <p>The Scottish Funding Council's Strategic Plan for 2015-18 contains high level objectives on the use of resources. There are currently no detailed financial plans underpinning the Strategic Plan.</p> <p>To support effective distribution of capital resources, the Council is currently developing a long term infrastructure strategy</p> <p>Without longer term planning, there are risks to ongoing financial management and financial sustainability.</p>	<p>Follow up and review progress in the development of longer term plans and the infrastructure strategy.</p> <p>Review progress of the development of reconciliations between the financial year and academic year budget allocations.</p> <p>Review internal audit's work in this area.</p>	<p>The Council is still developing longer term financial plans for its running costs, higher education and further education budgets. See action plan point 3.</p>
<p>6 Workforce and capacity</p> <p>The Scottish Funding Council's responsibilities have increased in recent years, including, for example, the college merger programme and increased support for the governance of colleges and universities.</p> <p>This presents a capacity risk that may also impact on the Council meeting its performance targets.</p> <p>There is a risk that the Council does not have sufficient capacity to deliver its responsibilities.</p>	<p>Review the development of workforce planning processes.</p> <p>Review the performance management processes and reports.</p>	<p>We confirmed that the staffing budget is closely monitored throughout the year by the Senior Management Team (SMT). The SMT meets monthly to review organisational changes and make decisions about how its resources should be deployed in response to changing needs.</p> <p>A more in-depth review of staffing in light of current and future needs is undertaken at least once a year. This is currently focussed on developing the knowledge and skills of existing employees and building agility into the design of the organisation. A key aim is to enable the Council to more easily respond to a changing environment and priorities. From 2017/18 this process will be documented, managed and communicated using an internal workforce planning tool.</p>
<p>7 Monitoring the financial health of all colleges and universities</p> <p>The Scottish Funding Council is responsible for monitoring</p>	<p>Consider the Council's arrangements for monitoring and reporting on the financial health of institutions.</p>	<p>We are a satisfied that the assurance framework for the further education sector provides an appropriate framework for monitoring the financial health of</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>the financial health of all colleges and universities.</p> <p>There is a reputational risk in the event of an institution failing and a financial risk if the Council has to intervene to ensure continuity of services.</p>		<p>Colleges.</p> <p>The risk associated with a higher education institution failing is lower as they are less reliant on funding from the Scottish Funding Council as a source of income.</p>
<p>8 Governance and accountability</p> <p>In September 2010 the Auditor General published a report on the role of boards. The report highlighted the need for boards to demonstrate strong leadership and strategic direction.</p> <p>There is a risk that any changes flowing from the Scottish Government's Review of Enterprise and Skills may affect the effectiveness of the Council's governance arrangements.</p>	<p>Follow-up on our 2010 Role of Boards report.</p> <p>Monitor the Scottish Government's Review of Enterprise and Skills.</p>	<p>We have concluded from our review of governance and accountability that the Council has effective governance arrangements in place.</p> <p>In March 2017, the Scottish Government confirmed that the Council would retain its current decision making powers.</p>
<p>9 ICT arrangements</p> <p>The Scottish Funding Council is currently developing its ICT strategy. The risk of cyber attacks will be considered as part of that process.</p> <p>There is a risk that cyber attacks may lead to data loss and financial and/or reputational loss.</p>	<p>Consider the Council's progress in developing its ICT strategy and its references to cyber security.</p> <p>Review the Council's risk register.</p>	<p>We confirmed through discussions with officers that the Council's ICT strategy is still in development and a draft will be circulated internally shortly.</p> <p>Officers confirmed that the risk associated with a successful cyber attack will feature in the latest iteration of the Council's risk register.</p>
<p>10 National Fraud Initiative</p> <p>The NFI data matching exercise, led by Audit Scotland, allows public bodies to investigate data matches, and if fraud or errors have taken place, stop payments and attempt to recover the amounts involved. The current data matching exercise collected data in October 2016 and match investigation work has started earlier this year.</p> <p>Without appropriate processes to review the matches identified by NFI there is a risk that fraudulent payments are undetected.</p>	<p>Monitor the Council's participation and progress with the NFI process.</p> <p>Complete an NFI questionnaire which will reflect the Council's NFI activity.</p>	<p>We concluded from our review of the NFI exercise that the Council has been proactive in investigating matches and will report the outcome of NFI activity.</p>

Appendix 3

Summary of national performance reports 2016/17



Apr			
May		Common Agricultural Policy Futures programme: an update	
Jun		South Ayrshire Council: Best Value audit report	 The National Fraud Initiative in Scotland
Jul		Audit of higher education in Scottish universities	 Supporting Scotland's economic growth
Aug		Maintaining Scotland's roads: a follow-up report	 Superfast broadband for Scotland: a progress update
			 Scotland's colleges 2016
Sept		Social work in Scotland	 Scotland's new financial powers
Oct		Angus Council: Best Value audit report	 NHS in Scotland 2016
Nov		How councils work – Roles and working relationships in councils	 Local government in Scotland: Financial overview 2015/16
Dec		Falkirk Council: Best Value audit report	 East Dunbartonshire Council: Best Value audit report
Jan			
Feb		Scotland's NHS workforce	
Mar		Local government in Scotland: Performance and challenges 2017	 i6: a review
			 Managing new financial powers: an update

Central Government relevant reports

[Audit of higher education in Scottish universities](#) – July 2016

[Scotland's colleges 2016](#) – August 2016

[Scotland's new financial powers](#) – September 2016

[Managing new financial powers: an update](#) – March 2017

Scottish Funding Council

2016/17 Annual Audit Report

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