West College Scotland

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

For the year ended 31 July 2017

Contents

This report has been prepared in accordance with our responsibilities as appointed auditors as set out in Audit Scotland's *Code of Audit Practice* ('the Code'). Reports and letters prepared by appointed auditors and addressed to the College are prepared for the sole use of the College and we take no responsibility to any member or officer in their individual capacity or to any third party.

Executive summary

Purpose of this report

Our annual audit report summarises the work we have undertaken as the auditor for West College Scotland ('the College') for the year ended 31 July 2017.

Our responsibilities are defined by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice ('the Code') issued by Audit Scotland in 2016. The detailed sections of this report provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of work	Summary
Financial statements opinion	Our unqualified opinion on the financial statements was issued on 11 December 2017 following the Board of Management's approval of the annual report and accounts on the 4 December 2017.
Opinions on other matters	We also reported an unqualified opinion on the same day for the: • The regularity of income and expenditure; and • The remuneration and staff report, performance report and governance statement.
Wider Scope work	We are required by the Code to form conclusions on four wider scope dimensions. Our conclusions on each dimension are summarised below:
Financial Management	• The College has effective arrangements, including budgetary control, that help Board members scrutinise finances;
Financial Sustainability	• The College has adequate financial planning arrangements in place;
Governance and Transparency	• The College has governance arrangements in place that provide appropriate scrutiny of decisions made by the Board; and
Value for Money	• The College has an effective performance management framework in place that supports progress towards the achievement of value for money.
Independence	We have continued to consider any actual, potential or perceived threats to our independence as part of our ongoing risk assessment. We can confirm that no threats to independence have been identified since the issue of our Audit Strategy Memorandum in June 2017, and therefore we remain independent.

We would like to take this opportunity to thank all management and staff for their assistance and co-operation during our audit.

Financial statements

Financial statements opinion	**Unqualified**
Regularity opinion	**Unqualified**
Opinion on other prescribed matters	**Unqualified**

The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the College and whether they give a true and fair view of the College's financial position as at 31 July 2017 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by Audit Scotland, and International Standards on Auditing for the UK and Ireland (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the College's circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for audit testing (performance materiality), which is also dependent on the level of inherent risk assessed in the area being audited which may be due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Audit Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 July 2017:

Financial statement materiality	£1.2m
Performance materiality	£0.9m
Trivial threshold	£36,000

Our response to significant risks

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the College's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks, the work we carried out on those risks and our conclusions.

Significant risk	How we addressed the risk	Audit conclusion
Management override of control In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such overrides could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.	We addressed this risk through performing audit work over: • Accounting estimates impacting amounts included in the financial statements; • Consideration of identified significant transactions outside the normal course of business; and • Journals recorded in the general ledger and other adjustments made in preparation of the financial statements.	Satisfactory assurance has been gained in respect of the presumed risk of management override. We have no matters to report.
Revenue recognition There is a presumption under International Standards on Auditing that there is a significant risk of fraud and error in the timing of revenue recognition leading to the material misstatement of revenue overall. This is because revenue is an area of particular focus by users of financial statements and can be subject to judgements as to when grant income should be recognised and if clawback conditions apply to the funding.	. We addressed this risk through performing audit work over: • the design and implementation of controls management has in place to ensure income is recognised in the correct period; • cash receipts around the year end to ensure they have been recognised in the right year; and • the judgements made by management in determining when grant income is recognised.	Satisfactory assurance has been gained in respect of the presumed risk of revenue recognition. We have no matters to report.

Areas of audit focus

As part of our continuous planning processes, we carry out work to identify matters that will have a direct impact on the financial statements, but are not likely to represent a risk of material misstatement. The work we carried out in relation to these areas of audit focus is outlined below.

Audit focus	Work undertaken	Conclusion
Valuation of pension liabilities The College makes contributions to two pension schemes – the Scottish Teachers Superannuation Scheme (STSS) and the Strathclyde Pension Fund (SPF). While both are defined benefit schemes, it is not possible to identify the College's share of the underlying assets and liabilities in the STSS and it is therefore accounted for as a defined contribution scheme. The College's share of the SPF's underlying assets and liabilities is identifiable and a net liability is recognised in the accounts. As at 31 July 2017 the College accounts show a liability of £26.5m, a decrease of £0.2m over the previous 12 months. Given the scale of the liability recognised in the accounts, a misstatement in the reported position could be material to the financial statements	We considered the College's arrangements, including the existence of any relevant controls, for making estimates in relation to pension entries within the financial statements. We also considered the reasonableness of the actuary's assumptions used in providing the College with information in the financial statements through the use of our internal experts.	Our audit work has provided satisfactory assurance over pension valuations. We have no matters to report.
Valuation of fixed assets The College holds a significant level of property assets – reporting a net book value of £102m as at 31 July 2017. In line with the requirements of the Government Financial Reporting Manual, the College has adopted a formal revaluation policy of an external valuation every five years, with an interim valuation performed within the third year of the five year period. This meets the requirement of the FE SORP that assets are valued sufficiently regularly so that the carrying value of the asset is not materially different from its fair value. The College is also required to assess on an annual basis whether there are indicators of impairment to assets at the reporting date. Given the significance of the value of fixed assets held, a misstatement in the valuation could be material to the financial statements.	We undertook a range of substantive procedures including: • evaluation of the competencies of the College's valuer; • review and evaluation of the valuer's report; • review of the reconciliation between the College's asset register and general ledger; and • considered the formal impairment review performed by the College as at 31 July 2017.	Our audit work has provided satisfactory assurance over the valuation of fixed assets. We have no matters to report.

Internal control recommendations

As part of our audit we have considered the internal controls in place that are relevant to the preparation of the financial statements. We do this to design audit procedures that allow us to express an opinion on the financial statements; this does not extend to expressing an opinion on the effectiveness of internal control or to identify any significant deficiencies in their design or operation. Our audit work on the financial statements has not identified any recommendations for the improvement of internal controls at the College.

Audit differences

We discussed and agreed a number of disclosure and presentational adjustments that have been reflected in the final annual report and accounts. We identified one material adjustment to the financial statements. The College had accrued £1.4m for expected costs on the Inchinnan-Oakshaw project for which specific Estates Maintenance Funding had been obtained from the Scottish Funding Council. Under the accrual method of recognising grant income, as set out in the HE/FE SORP and FRS 102, grant income should be recognised as the related costs are incurred. At 31 July, the College had not incurred costs related to this grant, but had accrued them. Under HE/FE SORP and FRS102 requirements, we have determined that the SFC Estates Maintenance Funding and the related expenditure and accrual should not be recognised in the financial statements. As this amount is material, we have requested a change to the financial statements. The accounting impact of this change is shown in Appendix 1 to this report.

Qualitative aspects of the College's accounting practices

We are required to communicate to you our views on the significant qualitative aspects of the College's accounting practices, including the accounting policies used and the quality of disclosures.

Qualitative aspect	Our views
Accounting policies and disclosures	We have reviewed the College's accounting policies and disclosures and found these to be in line with the requirements of the 2015 Statement of Recommended Practice: Accounting for Further and Higher Education and the Government Financial Reporting Manual 2016-17. In line with our expectations, there have been no significant changes to accounting policies for the year ended 31 July 2017.
Quality of the draft financial statements	We received draft financial statements from management on 8 September 2017 in advance of our audit fieldwork. A draft annual report followed shortly thereafter. The draft annual report and accounts were of a good quality.
Quality of supporting working papers	Producing high-quality working papers is a crucial part of compiling financial statements that are complete and materially accurate. They also support the delivery of an efficient audit. Working papers were accurate and informative; and staff were responsive to our requests when we were on-site.

Significant matters discussed with management

We have had a number of discussions with management regarding the decision to adjust the draft financial statements to de-recognise SFC Estates Maintenance Funding and the associated expenditure and liability. There were no other significant matters discussed with management.

Significant difficulties during the audit

During the course of the audit we did not encounter any significant difficulties and we have had the full co-operation of management and staff.

Financial management

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

West College Scotland has effective arrangements, including budgetary control, that help Board members scrutinise finances

Financial performance

FE/HE SORP Accounting	2016/17 £'000	2015/16 £'000
Operating Income	55,236	55,149
Staff Costs	(39,531)	(37,911)
Operating Expenditure	(18,216)	(18,270)
Operating Deficit for the year (FE/HE SORP basis)	**(2,511)**	**(1,032)**

The above table shows the financial performance of the College for the last two academic years, as reported under the FE/HE SORP. Although a deficit was shown over both years:

- The College achieved its financial targets and spending was in line with the plan;
- There were no significant changes to the reported position during the year; and
- The student credit target was met confirming the level of funding in the financial statements.

The Statement of Comprehensive Income is prepared under the FE/HE SORP. Colleges are also subject to Central Government accounting rules but the FE/HE SORP does not permit Colleges to include government non-cash allocations for depreciation in the statement of Comprehensive Income. As can be identified below, the College reported an operating surplus, under Central Government accounting rules and is therefore operating within its funding.

Central Government Accounting	2016/17 £'000	2015/16 £'000
Operating Deficit for the year (FE/HE SORP basis)	(2,511)	(1,032)
Add:		
Non-cash allocation for depreciation	2,987	1,626
Non-cash adjustment for salary and interest	1,416	1,130
Less:		
Exceptional income release of prior provision	(1,216)	(500)
Revenue Funding allocated to loans	(658)	(1,176)
Operating Surplus on Central Government accounting basis	**18**	**48**

Budgetary process

We have reviewed and considered the budgetary processes and controls and budget monitoring arrangements in place at the College. Our work consisted of a review of budget monitoring reports and committee papers and attendance at committees. Overall, we consider that the Board of Management obtains regular and timely financial information that reflects the actual financial position.

We noted that budget reports accurately predicted the financial position and were produced on a timely basis and considered by the appropriate committee. The Finance and General Purposes Committee considers the management accounting pack regularly, reporting to the Board of Management. Minutes of the meeting document the level of challenge to the financial performance.

Internal controls

As part of our audit we have considered the internal controls in place that are relevant to the preparation of the financial statements. We do this to design audit procedures that allow us to express an opinion on the financial statements; this does not extend to expressing an opinion on the effectiveness of internal control or to identify any significant deficiencies in their design or operation.

We have also considered the work of internal audit, from individual reviews of financial systems and their annual audit opinion on the control framework in place at the College. Internal audit concluded, in their 2016-17 annual report, that the College has an *"adequate and effective framework of governance, risk management and internal control, and proper arrangements are in place to promote value for money and deliver best value in the achievement of organisational objectives".*

We conclude that the processes and controls in place at the College are operating effectively. The College has all the expected control, risk, performance and financial arrangements in place. There are a series of regularity documents including standing orders, articles of governance, code of conduct, and financial regulations intended to ensure regularity of transactions. These are all up to date and relevant.

Prevention and detection of fraud and irregularity

Management and the Audit Committee, as those charged with governance also have responsibilities in respect of fraud. They are responsible for safeguarding assets and for the prevention and detection of fraud, error and non-compliance with laws and regulations.

We have a responsibility to review the College's arrangements for the prevention and detection of fraud. Our audit work was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. We found the arrangements in place to be satisfactory and identified no material misstatements resulting from fraud or irregularity.

National Fraud Initiative

The College took part in the National Fraud Initiative (NFI) for the first time in 2016/17. NFI is a counter-fraud exercise co-ordinated by Audit Scotland that analyses data held by public sector bodies to identify 'matches' that may indicate the existence of fraud or error.

National Fraud Initiative 2016/17	
Total number of matches	414
Number recommended for investigation	0
Completed	414

No matches identified have led to discovery of fraud. We reviewed the processes in place for the College's participation in NFI and identified no issues.

Financial sustainability

Financial sustainability extends the going concern assumption from the financial statements, looking forward two to five years, reviewing and assessing arrangements for financial planning and affordable and sustainable service delivery in this timescale.

West College Scotland has adequate financial planning arrangements in place

Financial planning

In its annual review of the FE sector, Audit Scotland's 'Scotland's Colleges 2017' recommended that Colleges should:

- *prepare longer-term financial plans, as we recommended last year, in order to support financial decision-making that takes account of both immediate and future cost pressures; and*
- *calculate the cost of harmonising staff pay, terms and conditions and include these in their financial plans.*

The College prepared a 5-year budget in June 2017 that was scrutinised by the Finance and General Purposes Committee and then approved by the Board. The plan includes assumptions about inflation in the short and medium term and also highlights other financial stability risks. The College is very clear on the risks to financial sustainability it faces and the uncertainty of funding over the medium and long term for example national pay bargaining, the ending of ESF funding, the lack of clarity on future Scottish Funding Council (SFC) funding and national support staff job evaluation.

The 5-year plan includes adjustments for SFC income and pay costs associated with National Bargaining and the level of saving required to be made to deliver a small operating surplus. On the assumption of 'flat funding' from the SFC, West College Scotland estimates that this will result in a financial deficit of £952,000 in 2017-18 rising to a deficit of £3,118,000 in 2021-22. There are significant financial pressures facing the College that will continue to be monitored and reported upon.

There is more certainty over the 2017/18 budget and the College is on track to achieve its financial targets. In October 2017 the College completed a Financial Forecast Return (FFR) for the SFC. This includes a 5 year plan for which the SFC have set assumptions. We note that the College did not use all the assumptions advised by the SFC in its completion. For example, it did not apply inflationary increases of 1.5% to income and expenditure because the College considered them to be unrealistic. This local approach was approved by the Board of Management and has been highlighted to the SFC.

Asset management and Estates Strategy 2016-2026

The College has a significant estate with a replacement value of £273m as at 31 July 2017 and currently manages 17 buildings with an area of 80,903 square metres. These buildings are spread across eight principle locations within the local authority areas of Renfrewshire, West Dunbartonshire and Inverclyde. Three of these buildings are non-operational residential properties, with the remaining 14 being core to College activities. The College Estate Strategy identifies a need to invest £33m in order to bring our operational buildings up to a suitable condition and required standard over the next 10 years. Challenges exist in relation to fitness for purpose of the College estate, with only 4 of 14 operational buildings being graded at Level 1 (excellent) for functional suitability, and half of the operational buildings requiring major repair or replacement.

In response the College is prioritising the expenditure of the £1.9m (2015-16: £2.4m) Scottish Funding Council (SFC) Estate Maintenance funding towards areas of most need. The College submitted an Outline Business

Case (OBC) for the development of the Greenock campus to the SFC in October 2016 and in October 2017 submitted an OBC for development of the Paisley campus. The College is continuing to engage with the SFC to progress the authorisation of these documents to full business cases. Acceptable building conditions are key to the College being able to attract students and achieve performance targets going forward.

Governance and transparency

Governance and transparency covers the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information

West College Scotland has governance arrangements in place that provide appropriate scrutiny of decisions made by the Board

Governance arrangements

Our work in this area has considered the overall governance arrangements in place at the College, reviewed the financial and performance reporting to the Board, and reviewed the minutes of committees to inform our assessment of the appropriateness of the governance structure. We have also attended Audit Committees during the year.

Financial papers submitted to committees are relevant and timely. Each paper has a summary setting out the purpose of the paper and the action required by the members. Minutes are understandable and contain detail of discussions and rationale for decision making.

The Board consists of 18 members, 8 female (including the Principal) and 10 male. The Board continues to work towards a gender balance that meets with the objective of the Gender Representation on Public Boards (Scotland) Bill which was introduced by the Scottish Parliament in June 2017 with an implementation date of 2022.

The key committees comprise of lay members, with each also containing the Principal and the Chair of the Board, with the exception of the Audit Committee where the Principal cannot be a member. In addition, the Chair of the Board is also not permitted to be a member of the Audit Committee. A lay member of the Board chairs all Committees. Appropriate College officers attend committees and present reports as required.

Governance Statement

As part of our audit we have read the governance statement included in the annual report. The governance statement sets out the corporate governance framework in place throughout the reporting year, the internal controls in operation, the work of internal audit and the overall efficiency and effectiveness of the governance framework.

For the first time in 2016/17, we are required to read and provide an opinion on the governance statement. In our opinion, the information contained within is consistent with the financial statements. We also consider that the governance statement has been prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and further directions made by the Scottish Funding Council.

Internal audit

An effective internal audit service is an important element of any organisation's governance arrangements. Internal audit provide the College with independent assurance on internal control and corporate governance processes. The internal audit function at the College is provided by Scott-Moncrieff. In its review on the Board's effectiveness Scott-Moncrieff concluded that there were '*many areas of good governance and also a strong self-awareness amongst board members of the Board's strengths and opportunities for improvement'*.

Transparency

Transparency means that service users and the public have access to understandable information about how the College is making decisions and using its resources. There is a commitment to transparency, with the minutes of the Board of Management being available on the web-site.

Value for money

Value for money concerns using resources effectively and continually improving services

West College Scotland has an effective performance management framework in place that supports progress towards the achievement of value for money

Performance management

The College delivered its target credits, achieved a break even in performance with improvements in student access and feedback although staff turnover and sickness levels both worsened during the year.

The College can point to achievement of financial targets, management of costs and income and a number of improvements in performance in 2016/17. The College has arrangements to analyse cost and performance and has improved performance reporting during 2016/17 with the introduction of a dashboard reporting system. Through delivery of the 2016/17 budget there is clear evidence that the College understands cost drivers and is in control of costs.

Regularity

As part of our audit of the College's financial statements, we are required by the Public Finance and Accountability (Scotland) Act 2000 to give an opinion on the regularity of expenditure and receipts shown in the financial statements. Regular expenditure and income is that which has been incurred / obtained in line with guidance issued by the Scottish Ministers and the terms and conditions of funding of the Scottish Funding Council.

The College has arrangements to monitor the requirements of the Scottish Funding Council, Audit Scotland and other regulatory or advisory bodies to ensure it complies with the terms and conditions of funding including regular reporting of financial and operational performance to the Board and its committees.

Our review found an effective control environment exists over regularity of expenditure and receipts. No instances of non-compliance with Scottish Funding Council terms and conditions were noted.

Our fees

Fees for work as the College's appointed auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to the June 2017 Audit Committee. Having completed our work for the 2016/17 financial year, we can confirm that our final fees are as follows:

Area of work	2016/17 proposed fee £	2016/17 final fee £
Auditor remuneration	25,900	25,900
Pooled costs	1,620	1,620
Contribution to Audit Scotland costs	1,470	1,470
Total fee	28,990	28,990

We confirm that these fees are in line with the scale fee set by Audit Scotland.

We also confirm that we have not undertaken any non-audit services for the College in the year.

Appendix 1 – Summary of misstatements

The misstatements identified for adjustment during the course of the audit that are above the trivial level of £36,000, are set out below. All have been amended.

Adjusted misstatements 2016/17				
	Statement of Comprehensive Income and Expenditure		**Balance Sheet**	
	Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
Dr: Accruals and deferred income			1,445	
Cr: Amounts owed to SFC – Estate Maintenance				1,445
Dr: Funding Body Grants - (Estates Maintenance Funding)	1,445			
Cr: Other Operating Expenses		1,445		
Reversal of recognition of SFC Estates Maintenance Funding and associated accrual				

There are no misstatements, identified during our audit work that have not been adjusted for.