Scott-Moncrieff
business advisers and accountants

Borders College

2017/18 Annual Audit Report to the Board of Management and the Auditor General for Scotland

December 2018

Contents

Key messages

Financial statements

The annual report and accounts for the year ended 31 July 2018 were approved by the Board on 6 December 2018.

We reported within our independent auditor's report an unqualified opinion on the financial statements, the regularity of transactions, and on other prescribed matters. There are no matters which we are required to report by exception.

Wider scope

As outlined in our External Audit Plan, our annual audit work in respect of our wider scope audit responsibilities was restricted to:

- Audit work to allow conclusions to be made on the appropriateness of the disclosures in the Annual Governance Statement; and
- Consideration of the financial sustainability of the organisation and the services that it delivers over the medium and longer term.

Our conclusions and key observations are set out below:

Key facts

- The College continues to receive more than 70% of income through grant funding from the Scottish Funding Council. £9.009million was received in 2017/18.
- The College spent £12.807 million on the delivery of services in 2017/18. Staff costs make up 66% of total expenditure and are a key area of cost pressure for the College.
- The College reported an underlying surplus of £0.823million against an original budgeted deficit position of £0.080million for the year ended 31 July 2018. This represents an improvement on 2016/17 financial performance which showed an underlying deficit of £0.646million.
- The College has approved budget for a small deficit of £46k in 2018/19.

Governance statement

- We reviewed the Annual Governance Statement and identified some minor improvements to help optimise compliance with the requirements of the Government Financial Reporting Manual and the SFC Accounts Direction. These have been updated appropriately in the revised financial statements.
- The College has adequate systems in place to record, process, summarise and report financial and other relevant data. We have not identified any significant issues which would require to be disclosed in the governance statement.

Financial sustainability

- The College has arrangements in place for long term financial planning in line with SFC guidance for compiling Financial Forecast Returns.
- The FFR's show that the College is expected to maintain a small surplus position from 2018/19 onwards with respect of their underlying operating position. We recommend that the College performs robust scenario planning in future financial periods to consider the optimistic, reasonable and pessimistic assumptions.

Conclusion

This report concludes our audit for 2017/18. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK) and Ethical Standards.

Scott-Moncrieff
November 2018

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Introduction

This report is presented to those charged with governance and the Auditor General for Scotland and concludes our audit of the College for 2017/18.

We carry out our audit in accordance with Audit Scotland's Code of Audit Practice (May 2016). This report also fulfils the requirements of International Standards on Auditing (UK) 260: Communication with those charged with governance.

We have designated the College's Regional Board as "those charged with governance".

Introduction

1. This report summarises the findings from our 2017/18 audit of Borders College ("the College").

2. We outlined the scope of our audit in the external audit plan which we presented to the Audit Committee on 16 May 2018. The main elements of our work in 2017/18 have been:

   - an audit of the College's key financial systems and aspects of its corporate governance arrangements;
   - an audit of the draft financial statements, including a review of the annual governance statement,
   - a review of the arrangements as they relate to financial sustainability; and
   - completion of a minimum dataset of information that is submitted to Audit Scotland.

3. The College is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems. The weaknesses and 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. Communication in this report of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

4. This report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding appropriate actions. We give each recommendation a grading to help the College assess their significance and prioritise the actions required.

5. We discussed and agreed the content of this report with the Vice Principal Finance and Corporate Services and the Head of Finance.

Confirmation of Independence

6. We can confirm that we have complied with the Financial Reporting Council's Ethical Standard. In our professional judgement, the audit process has been independent and our objectivity has not been compromised. In particular, there have been no relationships between Scott-Moncrieff and the College that may reasonably be thought to bear on our objectivity and independence.

7. The audit fee reported in our external audit plan was £14,720. We propose to increase the fee to £17,350. This takes into account the additional costs incurred by the audit team due to the extended time required by the College to finalise a full set of accounts and working papers.

8. At the request of the College, Scott-Moncrieff provided VAT services during the year totalling £2,500. This work did not involve management decision making and was undertaken by the Scott-Moncrieff VAT team, entirely separately from the Public Sector External Audit team.

9. In line with Audit Scotland planning guidance, approval was obtained from the Scott-Moncrieff ethics partner and Audit Scotland before commencing non-audit work.

Adding value through the audit

10. All of our clients quite rightly demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the College through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the College promote improved standards of governance, better management and decision-making and more effective use of resources.

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

12. We welcome any comments you may have on the quality of our work and this report via: www.surveymonkey.co.uk/r/S2SPZBX.

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Annual report and financial statements

The College's annual report and financial statements are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

In this section we summarise the findings from our audit of the 2017/18 annual report and financial statements.

Annual report and financial statements

We reported unqualified opinions on the annual report and financial statements for the year ended 31 July 2018 within our independent auditor's report. We did not identify any significant adjustments to the unaudited annual report and financial statements.

In 2017/18 there was turnover of the finance team, this was a significant factor leading to delays in the delivery of the financial statements and working papers which resulted in additional pressures on the audit timescales.

Arrangements are in place to enable the annual report and financial statements to be submitted to the Scottish Funding Council and Auditor General for Scotland by the 31 December deadline.

Our assessment of risks of material misstatement

13. The assessed risks of material misstatement described in Exhibit 1 below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the audit team. Our audit procedures relating to these matters were designed in the context of our audit of the financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described in Exhibit 1 below.

Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

1. Management override

In any organisation, there exists a risk that management have the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the annual accounts. This is treated as a presumed risk area in accordance with ISA 240(UK) – *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Excerpt from the 2017/18 External Audit Plan

14. We have not identified any indications of management override in the year. We have reviewed the College's accounting records and obtained evidence to ensure that transactions outside the normal course of business were valid and accounted for correctly. In 2017/18, it was identified that controls in place for authorisation and review of journals were not operating fully in line with the financial procedures manual. While we did not identify any errors as a result, controls should be reviewed in this area.

Action plan point 1

15. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.

Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

2. Revenue recognition

Under ISA 240 (UK) – *The auditor's responsibilities relating to fraud in an audit of financial statements* there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the College could adopt accounting policies or recognise revenue transactions in such a way as to lead to a material misstatement in the reported financial position.

Excerpt from the 2017/18 External Audit Plan

16. As part of our planning process we considered the nature of the revenue streams at the College against the risk factors set out in ISA 240. We considered that for Scottish Funding Council (SFC) grant funding the risk of revenue recognition can be rebutted due to a lack of incentive and opportunity to manipulate revenue of this nature. However, we considered the risk of fraud in relation to revenue recognition remained present in all other income streams.

17. In response, we evaluated each material revenue stream, considered the College's revenue recognition policy and carried out testing to ensure this is appropriate and has been applied consistently. We performed detailed testing of each material income stream. We did not identify any evidence of fraud in relation to revenue recognition.

3. Risk of fraud in the recognition of expenditure

The FRC has published a revised Practice Note 10 which applies to the audit of financial statements of public sector bodies in the UK, for periods commencing after June 2016. The practice note recognises that most public sector bodies are net spending bodies and notes that there is an increased risk of material misstatement due to improper recognition of expenditure.

In line with the practice note, our presumption is that the College could adopt accounting policies or recognise expenditure in a way that materially misstates the College's financial performance.

Excerpt from the 2017/18 External Audit Plan

18. While we did not suspect incidences of material fraud and error, we evaluated each type of expenditure transaction and documented our conclusions. We have gained reasonable assurance on the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the annual accounts. To inform our conclusion, we carried out testing to confirm that the College's policy for recognising expenditure is appropriate and has been applied consistently throughout the year.

Our application of materiality

19. Materiality is an expression of the relative significance of a matter in the context of the financial statements as a whole. A matter is material if its omission or misstatement would reasonably influence the decisions of an addressee of the auditor's report. The assessment of what is material is a matter of professional judgement over both the amount and the nature of the misstatement.

20. Our initial assessment of materiality for the financial statements was £0.225 million and it remained at this level throughout our audit. Our assessment of materiality equates to

approximately 1.8% of the College's expenditure. We consider this to be a principal consideration for the users of the accounts when assessing the performance of the College.

Performance materiality

21. Performance materiality is the amount set by the auditor at less than overall materiality for the annual accounts as a whole to reduce to an appropriately low level the probability that the aggregate of the uncorrected and undetected misstatements exceed materiality for the annual accounts as a whole.

22. We set a performance materiality for each area of work based on a risk assessment for the area and percentage application of overall materiality. We then perform audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we are performing a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are set out in the table below:

Area risk assessment	Weighting	Performance materiality
High	45%	£101,000
Medium	55%	£124,000
Low	75%	£169,000

23. We agreed to report any misstatements identified through our audit that fall into one of the following categories:

- All material corrected misstatements;
- Uncorrected misstatements over £11,250; and
- Misstatements below £11, 250 that we believe warrant reporting on qualitative grounds.

Audit differences

24. We are pleased to report that there were no material adjustments to the draft financial statements. We identified some minor disclosure and presentational adjustments during our audit, which have been reflected in the final set of accounts.

25. We also identified three adjustments, one which was below our performance materiality and two which were above our performance materiality. Management has considered the adjustment and elected to revise the accounts. We will verify the adjustments have been processed correctly on receipt of the revised financial statements. These adjustments did not impact the financial position of the College, with no change in the reported deficit between the draft and final accounts.

26. We can confirm that there were no unadjusted differences to the accounts.

27. We have requested that a signed representation letter be presented to us at the date of signing the financial statements.

28. Full details of the audit differences are outlined in Appendix 2.

Group Consideration

29. The College has one group body: BC Business Consultants Ltd. The company has been dormant since 2010 and has had no transactions during the year.

30. The College does not present Group financial statements as the subsidiary is dormant and the only balance held in the subsidiary is the College's £10,000 investment.

31. Given the immaterial nature of the subsidiary we consider the College's approach to group accounts to be reasonable. Our audit approach has equally considered the position of the College and the Group.

An overview of the scope of our audit

32. The scope of our audit was detailed in our External Audit Plan, which was presented to the College in May 2018. The plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the College. This ensures that our audit focuses on the areas of highest risk. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.

33. At the planning stage we identified the significant risks that had the greatest effect on

our audit. Audit procedures were then designed to mitigate these risks.

34. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical review. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit management team. In performing our work, we have applied the concept of materiality, which is explained earlier in this report.

Other matters identified during our audit

35. During the course of our audit we noted the following:

Pension Liability

36. As at 31 July 2018 the net LGPS pension liability was £5.337million, a decrease of £3.308milion in comparison to the net pension liability as at 31 July 2017 (£8.645million).

37. The movement is primarily as a result of the triennial valuation of the Scottish Borders Pension Fund (carried out as at 31 March 2018). The actuarial valuation for the 31 July 2018 is the first year that the results of the triennial valuation are taken into account. In the interim years between triennial valuations, actuarial valuations are based on rolled forward data rather than a full valuation.

Performance and Accountability Report

38. We were provided with the Performance and Accountability report on the 1 November after the fieldwork for the audit was completed. We identified a number of disclosure adjustments which have been discussed with management and will be corrected in the revised accounts.

39. Our opinion on other prescribed matters includes a requirement to provide an opinion on whether the performance report is consistent with the financial statements and whether it has been properly prepared in accordance with applicable legal requirements.

Governance statement

40. The College's Governance Statement explains that the College was compliant with the principles of the 2016 Code of Good Governance for Scotland's Colleges. This is deemed to be in accordance with the requirements outlined in the 2017/18 Accounts Direction, released by the SFC.

41. While we are satisfied the content of the Governance Statement is not inconsistent with information gathered during the course of our normal audit work, we identified some disclosure improvements to help improve the level of compliance with the SFC guidance.

42. The College has taken on board our comments and has updated the Governance Statement in the revised annual report and financial statements.

Remuneration report

43. Our independent auditor's report confirms that the part of the Remuneration Report to be audited has been properly prepared.

44. We identified misstatements with regards to four employees' disclosed real increases in pension, lump sum and CETV within the remuneration report. We also noted misstatements with regards to the disclosed pension benefits. This will be adjusted in the revised financial statements and we intend to conclude that the disclosures are in line with underlying records and disclosure requirements.

Accounting and internal control systems

45. The College has adequate systems in place to record, process, summarise and report financial and other relevant data. While we have not identified any significant weaknesses or governance issues in the accounting and internal control systems, we did identify a number of moderate-to-low risk areas for improvement during our final audit. We outline the issues identified and our recommendations at Appendix 1.

Action plan points 2-7

Regularity

46. We have planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual report and accounts. We did not identify any instances of irregular activity.

Cyber security

47. In May 2017, a number of public sector bodies across Scotland were impacted by the Wannacry global ransomware attack. In response to this the Scottish Government launched ‘A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017/18’.

48. The action plan outlines a number of requirements that public sector bodies should be taking forward. This includes an action for public sector bodies to achieve Cyber Essentials or Cyber Essentials Plus certification by the end of October 2018.

49. In April 2018, the College completed the Cyber Essentials Plus pre-assessment and are awaiting a date for an assessment to achieve the Cyber Essentials Plus assessment.

General Data Protection Regulations

50. The General Data Protection Regulations (the Regulations) came into force in the UK on 25 May 2018. The Regulations replace the Data Protection Act 1998 and as well as strengthening existing Regulations, the Act has brought in new legislative duties for the Partnership. The Regulations bring significant potential penalties for non-compliance.

51. College staff received GDPR awareness training delivered through an online training module during 2017/18 and the role of data protection officer is being fulfilled by through the APUC DPO Shared Service. This means that the College will share a Data Protection Officer with other colleges and the DPO role is part-time.

52. The College followed the 12-step action plan recommended by the Information Commissioners Office. Updates on these actions were presented to the Board.

53. The College has published a number of revised privacy policies their website.

54. Compliance with the Regulations is an ongoing process, which we will monitor as part of our annual audit procedures. We have not identified any significant issues at this stage.

Qualitative aspects of accounting practices and financial reporting

55. We have considered the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the financial statements. Our findings are summarised in the following table:

Qualitative aspect considered	Audit conclusion
The appropriateness of the accounting policies used.	We are satisfied with the appropriateness of the significant accounting policies applied by the College.
The timing of the transactions and the period in which they are recorded.	We did not identify any concerns over the timing of transactions or the period in which they were recognised.
The appropriateness of the accounting estimates and judgements used.	We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the financial statements. Estimates have been made in relation to the valuation and depreciation of property, plant and equipment and pension provisions. Where available, the College has utilised the work of independent experts or industry practice to support the estimate applied. Pension estimates have been informed by advice from qualified, independent experts. We evaluated the competence, objectivity and capability of managements' experts in line with the requirements of ISA (UK) 500. We also evaluated the reasonableness of the estimates applied by the actuary and sought further clarification across our further education clients as to how the estimated investment returns had been derived.
The potential effect on the financial statements of any uncertainties, including significant risks and related disclosures that are required.	We have not identified any uncertainties, including any significant risk or required disclosures, which should be included in the financial statements.
The extent to which the financial statements have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed.	From the testing performed, we identified no significant unusual transactions in the period.
Apparent misstatements in the annual report or material inconsistencies with the financial statements.	The annual report contains no material misstatements or inconsistencies with the financial statements.
Any significant financial statements disclosures to bring to your attention.	There are no significant financial statements disclosures that we consider should be brought to your attention. All the disclosures required by relevant legislation and applicable accounting standards have been made appropriately.
Disagreement over any accounting treatment or financial statements disclosure.	While disclosure and presentational adjustments were made during the audit process there was no material disagreement during the course of the audit over any accounting treatment or disclosure.

Qualitative aspect considered	Audit conclusion
Difficulties encountered in the audit.	It was agreed that financial statements would be provided on 22 October 2018, however, the full draft annual report and financial statements was not received until 1 November 2018. In 2017/18 there was a change to key individuals within the finance team which resulted in a loss of local and sector knowledge. Compared to previous experience with the College, there was a higher level discussion and negotiation over disclosure and accounting adjustments in the financial statements and additional support required from the audit team to ensure compliance with the SFC accounts direction and the Government Financial Reporting Manual (the FReM).

3

Financial sustainability

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

Financial sustainability

The College reported a significant reduction in their accounting deficit for 2017/18 compared with 2016/17. The underlying deficit has moved from a deficit of £0.646million in 2016/17 to a deficit of £0.076million in 2017/18. This is a reflection of the College's management of cost pressure areas in year and additional grant income received in year.

The College has arrangements in place for long term financial planning in line with SFC guidance for compiling Financial Forecast Returns. The FFR's show that the College is expected to maintain a small surplus position with respect of their underlying operating position. We recommend that the College performs robust scenario planning in future financial periods to consider the optimistic, reasonable and pessimistic assumptions.

Significant audit risk

56. As outlined in our audit plan, we considered there to be a significant risk to the wider scope of our audit in relation to financial sustainability:

Exhibit 2: Key audit risk: financial sustainability

Financial sustainability

The College's 2017/18 revenue budget, as reported to the Regional Board in June 2017, forecasted an underlying operating deficit. The initial budget was prepared before the full impact of national pay bargaining could be considered. The updated 2017/18 budget projected an operating deficit of £0.106million. The College are now hopeful of achieving a breakeven position for 2017/18.

The Scottish Funding Council ('SFC') issued guidance on Financial Forecast Returns required for the period to 2021/22 in June 2017. The returns required standard information from all colleges and contribute to the SFC financial health monitoring framework. The College's return showed an increasing deficit position reaching £950,000 by 2021/22. Colleges are working with the SFC with regard to the assumptions used in future FFRs.

The indicative funding allocations for 2018/19 were announced in February 2018. The College are expected to receive an increase of 12.7% compared to 2017/18 with respect of their core teaching funding allocation. This allocation includes additional funding for the full expected costs of national bargaining and additional rural and remoteness funding. While the indicative allocations are likely to provide some short term financial stability for the College, the longer term financial sustainability remains challenging.

Excerpt from the 2017/18 External Audit Plan

57. The Scottish Funding Council issued guidance on Financial Forecast Returns required for the period to 2022/23 in June 2018. The returns require standard information from all colleges and contribute to the SFC financial health monitoring framework. Colleges are provided with sector wide assumptions although they are advised to review the appropriateness of these to ensure they reflect individual College circumstances.

58. The return shows that the College will move to a small surplus position from 2018/19. The

Exhibit 2: Key audit risk: financial sustainability

College has noted that there are risks to the delivery of the budget. Confirmation of SFC grant funding for 2019/20 is expected in December 2018 and following this the College will engage in curriculum planning. It is recognised that depending on the outcome of the grant funding there may be challenging decisions regarding service delivery which are required.

59. Further analysis of the College's financial sustainability is included from paragraph 66.

Budget Monitoring

60. The College's Finance and General Purpose Committee received quarterly budget monitoring reports throughout the financial year. The reports include details of any revisions to the budget, variances against the budget and year end forecast figures. Appropriate narrative is provided to Committee members to allow for scrutiny of the financial position.

The College's financial performance in 2017/18

61. The Statement of Comprehensive Income for 2017/18 recorded a deficit before other gains and losses of £0.076 million, equating to 0.6% of the College's total income.

62. The College's 2017/18 budget was set with an initial deficit of £0.080million although this was revised throughout the year to £0.069million. The College has demonstrated strong financial management throughout the year to achieve this position.

63. Savings were made during the year in relation to payroll costs as a result of lower than expected temporary lecturing posts.

64. The College's financial outturn in 2017/18 is a significant improvement on 2016/17. In 2016/17 a £0.646 million deficit before other gains and losses was achieved in comparison to the £0.076million deficit in 2017/18.

65. The College's reserves position has also improved as a result of the lower deficit and change in actuarial assumptions resulting in lower pension liability.

Financial Planning

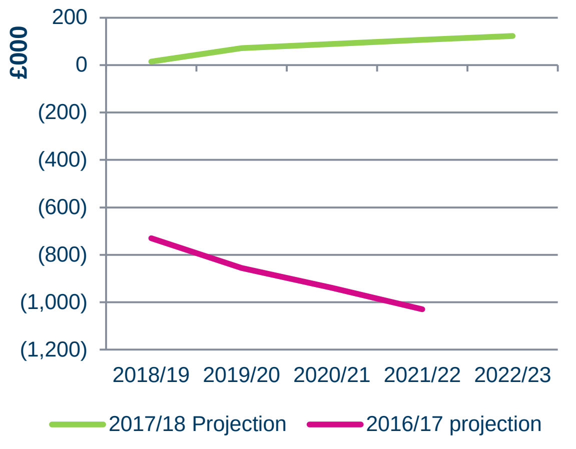
66. As noted above, the Scottish Funding Council issued guidance on Financial Forecast Returns required for the period to 2022/23 in June 2018. The returns require standard information from all colleges and contribute to the SFC financial health monitoring framework.

67. As part of this guidance the SFC worked with sector representatives to provide guidance on key assumptions to be applied in the Financial Forecast Return as follows:

- Financial projections for 2018/19 should be based on the funding allocation announced in May 2018. Colleges should plan for 2019/20 to include pay harmonisation with the SFC providing estimated income for this year. In the years following, Colleges are to assume that activity levels remain the same until 2022/23.
- Funding has not been assumed to cover inflationary pressures and therefore Colleges are expected to continue delivering efficiency savings of at least 3% per annum.
- Capital maintenance will be held at 2017/18 levels
- Non- SFC income and non-staff expenditure should be informed by local circumstance.
- Staff costs should take account of national bargaining harmonisation/job evaluations costs for all staff. Cost of living pay award increases for lecturing staff and for support staff should also be included. An annual increase of 2% for each remaining year should also be included.

68. Using the above assumptions the College has prepared a Financial Forecast Return which forecasts a surplus in each year from 2020/21 to 2021/22 as follows:

Exhibit 3: Projected underlying surplus/ (deficit)



69. The Financial Forecast Returns were presented to the Chair's Committee in August 2018 and the assumptions were subject to challenge and scrutiny. However, we noted that the College's projected underlying operating position has changed dramatically from that presented in the 2016/17 FFR as shown in exhibit 3.

70. There have been some key changes in the assumptions and information included in the FFR's, however it is not clear from the information provided to the Board the full reason for the significant improvement in the expected underlying position. In future presentations of these FFRs, it is recommended that the College clearly document the changes made year on year.

Action plan point 8

71. We have considered the assumptions used by the College in year and confirmed that they are in line with the SFC guidance. We noted that there is a requirement for colleges to tailor certain assumptions to local circumstance.

72. We have considered the assumptions used by the College and we have noted that they have used prior year financial information to underpin the assumptions. For example income from tuition fees and other education contracts is assumed to increase by 2% per annum based on the movement between 2016/17 and 2017/18.

73. Our review of previous financial performance shows that this trend has not occurred consistently over the previous five financial years. We recommend that the College performs greater scenario planning in future financial periods to consider the optimistic, reasonable and pessimistic assumptions.

Action plan point 8

Future Developments

74. Borders College, in partnership with Dumfries and Galloway College, is to benefit from an investment of just over £6.6 million as part of plans approved by the South of Scotland Economic Partnership (SoSEP). The investment aims to enable the creation of a digital learning platform and infrastructure that aims to provide access to learning opportunities for individuals of all ages, irrespective of location.

75. The Colleges will develop a network of Science, Technology, Engineering and Maths (STEM) Hubs across the South of Scotland to address the immediate skills gaps in areas such as Energy and Engineering, Construction and Care.

76. This is a significant project for the College, with over £1.1million disclosed within capital commitments in the financial statements. At the time of our audit the project is at an early stage and we will consider the ongoing implications for financial sustainability as part of our 2018/19 audit work.

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Appendices

Appendix 1: Management action plan

Our action plan details the control weaknesses and opportunities for improvement that we have identified during our audit.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist. The weaknesses or risks identified are only those which have come to our attention during our normal audit work, and may not be all that exist.

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

Action plan grading structure

To assist the College in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated. The rating structure is summarised as follows:

Grade 5	Very high risk exposure – major concerns requiring Partnership attention
Grade 4	High risk exposure – material observations requiring senior management attention
Grade 3	Moderate risk exposure – significant observations requiring management attention
Grade 2	Limited risk exposure – minor observations requiring management attention
Grade 1	Efficiency / housekeeping point

Action plan point	Issue, Risk & Recommendation	Management Comments
1. Journal review	**Issue** Per the financial procedures manual, all journals should be passed to the Head of Finance and Procurement for review and authorisation in advance of posting. A secondary check would be performed by the Head of Finance and Procurement at month end whereby a sample of postings on the ledger would be traced back to hard copy journal vouchers and supporting documentation. Neither control has been fully operating during the year. Instead journals were posted to the ledger and then passed to the Head of Finance and Procurement. While all journals were signed as authorised, not all journal vouchers were reviewed and traced to the ledger to confirm the accuracy of journal posting. **Risk** There is a risk that incorrect or fraudulent postings could be made without detection by the College's finance team. **Recommendation** While our audit review in respect of the 2017/18 financial year did not identify any indications of incorrect or fraudulent journal postings, we recommend that the College reviews approval processes to ensure all manual journals are appropriately reviewed and authorised. Additionally, the College should ensure processes are consistent with the Financial procedures manual.	In conversations with the auditors it has been agreed that the some of the current procedures in place are not practical and are outdated. Hence we will be updating our procedures in the near future. Last time the procedures were updated was in 2014. **Responsible officer: Head of Finance & Procurement.** **Implementation date:** Jan 2019 (amend Financial Procedure Manual)
Rating		
Grade 3		
Paragraph ref **14**		

Action plan point	Issue, Risk & Recommendation	Management Comments
2. System access removal **Rating** **Grade 2** **Paragraph ref** **45**	**Issue** Two members of the College's senior finance team have left in the last 12 months. We reviewed a list of users for the College's finance system and noted that both former staff members were still listed as users. Through review of bank statements, we also noted that these continued to be addressed to the former Head of Finance and Procurement. We further noted that one staff member is still listed as a company director for the College's subsidiary. Following discussion of the issue with the Head of Finance and Procurement, both users were removed from the finance system. Additionally, the College was able to provide evidence that they had requested that the bank removed users from the bank accounts. **Risk** There is a risk that unauthorised users can access both the finance system and bank accounts due to a lack of controls around user access reviews. **Recommendation** The College should ensure in future that leavers are promptly removed as users for all IT systems in the College, bank accounts and directorships. Where suppliers do not address requests promptly, the College should ensure these are actively chased to reduce the risk of fraudulent activity.	Action will be taken immediately to remove the staff member who has left the college from directorship of the College's subsidiary. However, please note that the subsidiary has been dormant for many years and will remain dormant into the future. The bank has yet again been recently informed of the change in College's senior finance team. **Responsible officer:** Head of Finance & Procurement. **Implementation date:** Immediate

Action plan point	Issue, Risk & Recommendation	Management Comments
3. Declaration of interests **Rating** **Grade 3** **Paragraph ref** **45**	**Issue** Board members are encouraged to declare their interests on a regular basis through a standing item on Board and Committee agendas. Where interests are disclosed at meetings or the Board Secretary is notified of a change, these will be reflected in the member's register of interests which is published on the College's website. However, we noted that there is not an effective formal process to ensure members update their written register of interests on an annual basis. Our review of declared interests identified that one member had two undisclosed interests. We also found that one member's interest declaration was out of date. **Risk** There is a risk that the College does not identify all related parties resulting in failure to accurately disclose all related party transactions in the College's financial statements. There is a further risk that potential conflicts of interests are not identified and therefore not appropriately managed. **Recommendation** The College should ensure that all members are asked to review their registers of interest on at least an annual basis and reminded of the importance of ensuring that up-to-date registers of interest are maintained.	Members are asked to provide updates to the register of interests at every Board and committee meeting. Members will be reminded of the need to comply with laid down procedures. **Responsible officer:** Board Secretary **Implementation date:** December 2018

Action plan point	Issue, Risk & Recommendation	Management Comments
4. Year-end preparedness **Rating** **Grade 3** **Paragraph ref** **45**	**Issue** There were delays in obtaining the annual report and the financial statements and working papers in 2017/18. In addition we found the financial ledger for 2017/18 remained open until 18 October 2018, almost three months after year end. We also noted that there were areas where the College did not adhere to the model disclosures recommended by the Scottish Funding Council's Accounts Direction 2017/18. **Risk** There is a risk that transactions are incorrectly or fraudulently posted to the wrong financial period. There is a risk that the College are not adhering to the expectations of the Scottish Funding Council. **Recommendation** The College should ensure that a timetable is in place for year-end close down of the ledger and preparation of the financial statements. This should ensure that all audit and committee deadlines are met. This should also aid in sufficient time being allocated to ensure all key disclosures are in line with best practice.	A high level timetable was communicated to the audit team. This took account of the change in finance leadership and the prioritisation of workload in relation to budget setting. The ledger was held open for longer than normal to ensure that an accurate trial balance was compiled for audit review. It was agreed with auditors that onsite work would commence based on the trial balance. It is agreed that completion of the full report and financial statements took longer than anticipated and this added extra complexity to the process. The finance leadership team sought assistance from the auditors on some disclosures. A detailed timetable will be developed for 2018/19 covering compilation of the annual report and financial statements, the audit and committee process. **Responsible officer: Head of Finance & Procurement.** **Implementation date:** June 2019.

Action plan point	Issue, Risk & Recommendation	Management Comments
5. Impairment review **Rating** **Grade 3** **Paragraph ref** **45**	**Issue** Land and buildings are subject to at least a 5 yearly formal valuation with the College's next valuation due to take place on 31 July 2019. In the interim years between property valuations, the College should ensure that a review of their property portfolio is performed at year end to ensure that the valuation remains appropriate. Discussion with the Head of Finance and Procurement found that this had not taken place. **Risk** There is a risk that the College holds land and buildings at an incorrect value resulting in the financial statements being misstated. **Recommendation** While additional audit work was performed and did not identify any issues which would indicate that the College's land and buildings are valued incorrectly, the College should ensure that a review is conducted in the interim years between valuations. This review should be documented with clear consideration of the factors likely to impact the property and land value.	The auditors were provided with a narrative on in relation to the valuation basis in 2017/18. There are no indications that any impairment is required. Our accounting policies do not state the requirement for a review of the property portfolio each year. We will review this for 2018/19. A full valuation will be conducted in 2018/19 in line with our accounting policies. **Responsible officer:** Vice Principal Finance and Corporate Services **Implementation date:** July 2019

Action plan point	Issue, Risk & Recommendation	Management Comments
6. Asset Held for Sale **Rating** **Grade 2** **Paragraph ref** **45**	**Issue** The College acquired the Netherdale campus in 2006/07 and subsequently moved into the campus in April 2009. The College's old Melrose Road campus was subsequently to be sold. However, despite several offers over the last 10 years, no sale has been finalised. The property is currently marked as an asset held for sale within the financial statements. **Risk** There is a risk that the College holds land and buildings at an incorrect value resulting in the financial statements being misstated. There is the further risk that SFC is not achieving value for money. **Recommendation** We obtained confirmation from external sources regarding the property value. However, in future, the property should ensure that a documented review of the property and associated value is performed. The College does not have any direct financial risk associated with the property as any sales proceeds would be passed to the Scottish Funding Council, however, the College does have a responsibility to ensure that the site is actively sold and steps are taken to ensure this is processed in the near future.	The auditors were provided with a narrative on the position relating to the Melrose Road site. The site remains for sale at £700k but valued at £585k which in the view of our advisors is closer to the likely value to be realized. We will be engaging with the Council regarding the planning brief and will review the position again for the 2018/19 accounts. **Responsible officer:** Vice Principal Finance and Corporate Services **Implementation date:** July 2019

<table>
<tr><th>Action plan point</th><th>Issue, Risk & Recommendation</th><th>Management Comments</th></tr>
<tr><td>7. Payroll reconciliations</td><td rowspan="5">Issue
A year-end reconciliation between the ledger and the payroll system was not prepared.
Risk
There is a risk that material differences between the ledger and payroll system were not identified in a timely manner resulting in potential financial loss for the College.
Recommendation
While audit performed the reconciliation with no material differences observed, the College should ensure that payroll reconciliations are performed on a monthly basis and in a timely manner to ensure differences can be promptly addressed and investigated.</td><td rowspan="5">Responsible: Finance Team
Implementation date: On a monthly basis going forward.</td></tr>
<tr><td>Rating</td></tr>
<tr><td>Grade 3</td></tr>
<tr><td>Paragraph ref</td></tr>
<tr><td>45</td></tr>
</table>

Action plan point	Issue, Risk & Recommendation	Management Comments
8. Financial Forecasting Return	**Issue** The Financial Forecasting Return shows a significant difference from previous FFRs. However, we noted that no additional commentary has been provided on why such significant movements have been observed. We also noted that the College has not presented appropriate scenario planning to the Board in order to inform their understanding of assumptions. **Risk** There is a risk that the FFR and assumptions used within the return have not been subject to appropriately robust scrutiny due to a lack of detail provided by management. **Recommendation** Future FFRs should show the movement between previous iterations of the FFR and include management's justification for changing figures. Management should also prepare greater scenario planning and include optimistic, likely and pessimistic assumptions for review by the Board.	We used SFC guidance on planning assumptions, to ensure a consistent approach across the sector. Scenario planning is discussed at Board level. We will consider extending this into the FFR process for 2019/20. We will implement tracking of the movement in the FFR. **Responsible officer:** VP Finance and Corporate Services **Implementation date:** Tracking will be implemented December 2018 Scenario planning will be considered as part of 2019/20 planning
Rating		
Grade 3		
Paragraph ref		
70 and 74		

Follow up of prior year audit recommendations

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
1. Campus Lifecyle Trust Fund **Rating** **Grade 2**	The contract terms state that the campus lifecycle trust fund shall be lodged in a joint name bank deposit. The practical arrangements in place, where the College is the only signatory on the account, are not currently wholly consistent with the contract terms. No issues have been identified with the approach taken to date for administering the bank account. However, the College should consider updating the contracted terms or getting formal confirmation that the approach being taken is accepted by all parties.	**Action owner:** Vice Principal – Finance and Resources **Due Date:** 31 December 2017 Agreed. Confirmation will be sought from Heriot-watt University that current arrangements are accepted.	**Action Incomplete**

Action plan point	Issue & Recommendation	Management Comments	External audit update 2017/18
2. Estimation basis for the Netherdale Provision **Rating** **Grade 3**	Over the term of the agreement to date the College has recognised a provision on the balance sheet in relation to its obligations under the contracted terms. The value of the estimated provision has been informed by an initial assessment from an independent Quantity Surveyor at the outset of the agreement and periodic reviews by the College and University facilities management teams in the subsequent periods. As time progresses, there is a risk that the estimates being made become a less accurate reflection of the College's obligation at each year end. While the adequacy of the provision has been subject to internal review, we consider the College should ensure reassessment by an independent Quantity Survey periodically throughout the life of the agreement.	**Action owner:** Vice Principal – Finance and Resources **Due Date:** 31 July 2019 Agreed. Assessment has been scheduled to take place in 2018-19, in accordance with Campus Management Committee direction.	**Action incomplete** Per management responses, the Assessment has been scheduled to take place in 2018-19. This matter is not yet due – rather than incomplete.

Appendix 2: Audit differences

Adjusted differences

We identified the following adjustment during the audit. We have discussed this adjustment with management and have agreed that it should be incorporated into the financial statements:

Adjusted differences		SOCI		Balance Sheet	
		DR £000	CR £000	DR £000	CR £000
1.	SFC Recurrent grants	70			
	Other SFC grants		70		
	Being the reallocation of other SFC grants				
2.	Other creditors and accruals			121	
	Provisions				121
	Being the reallocation of College contribution to the Campus Lifecyle costs fund				
3.	Short term creditors			812	
	Long term creditors				812
	Being the reallocation of deferred income between long and short term creditors				

Appendix 3: Respective responsibilities of the College and the Auditor

Management responsibilities

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

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

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

Auditor responsibilities

Public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance not only on the financial statements and associated documents such as the governance statement, but also providing a view, where appropriate, on matters such as propriety, performance and the use of resources.

Our responsibilities, as independent auditors, are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland, and guided by the auditing profession's ethical guidance.

Specifically in relation to the financial statements, we are required to audit them in accordance with ISAs and to give: an opinion on the financial statements, an opinion on regularity and an opinion on other prescribed matters. We are also required to report certain matters by exception. Each of these responsibilities is described below

Opinion on financial statement

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

- give a true and fair view in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the SFC of the state of the body's affairs as at 31 July 2018 and of its surplus for the period then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Further and Higher Education (Scotland) Act 1992 and directions made thereunder, the Charities and Trustee Investment (Scotland) Act 2005, and regulation 14 of The Charities Accounts (Scotland) Regulations 2006.

Opinion on regularity

We confirm whether, in our opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Opinion on other prescribed matters

We express an opinion on whether:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Ministers; and
- the information given in the Performance Report for the financial period for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

- We are also required to report if, in our opinion: proper accounting records have not been kept; or
- the financial statements and the part of the Remuneration and Staff Report to be audited are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit; or
- the governance statement does not comply with Scottish Funding Council requirements.

Scott-Moncrieff
business advisers and accountants