

Moray College Annual Audit Report

Year ended 31 July 2018

18 December 2018

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About this report

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

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

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

Complaints

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

1. Executive Summary

Purpose of this report

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

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

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

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the College employs best practice and where processes can be improved. We use these insights to form our audit recommendations to support the College in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. These are highlighted throughout the report together with our judgements and conclusions regarding arrangements.

Scope and responsibilities

The Code sets out the responsibilities of both the College and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the Audit Committee on 22 May 2018. We summarise these responsibilities in Appendix A.

Our Annual Audit Plan set out an overview of our audit scope and approach for the audit of the 2017/18 financial statements. We carried out our audit in accordance with the plan. We applied the materiality levels below to our audit, as outlined in our audit plan and based on our consideration of the key risks and issues facing the College and its financial statements. We reassessed materiality on receipt of the draft financial statements and at the conclusion of our audit work, and concluded the levels identified during our planning work remained appropriate.

• Materiality for our audit – no change to that reported in our Annual Audit Plan	£195,000
• Tolerable Error is our materiality applied at an individual account balance – no change	£145,000
• Reporting threshold, set in line with the requirements of the Code – no change	£9,000

Financial statement audit

We are responsible for conducting an audit of the financial statements of the College. We provide an opinion on the financial statements as to 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 Scottish Funding Council of the state of affairs of the College as at 31 July 2018 and its deficit for the year then ended;
- they have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder issued by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005 and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

We also review and report on other information prepared and published by the College along with its financial statements.

Wider scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the dimensions of wider scope public audit that are relevant for each body. As outlined in our audit plan, the College qualifies as a “smaller body” in line with Audit Scotland guidance, therefore our wider scope work covers the arrangements in respect of financial sustainability and governance and transparency.

Key contacts

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Independence

We confirm that we have undertaken client and engagement continuance procedures, included in which is our assessment of our continuing assessment of our independence to act as your external auditor.

Financial statements audit

We have issued an unqualified audit opinion on the College’s financial statements. We have concluded satisfactorily in respect of each of the significant risks and audit focus areas identified in our Annual Audit Plan. The completed draft financial statements, including the Performance Report, Accountability Report and Remuneration and Staff Report were received at the start of the audit fieldwork; in line with the agreed timetable. A number of iterations of the front end narrative sections of the financial statements were provided in advance of the audit to facilitate timely review. We made a number of suggestions to enhance the presentation and readability, and to ensure compliance with disclosure requirements. Management responded positively to audit comments and addressed all material matters in the finalised version of the financial statements.

Six audit adjustments were made by management as a result of the audit process.

Wider scope audit – key messages

We set out below our key messages in respect of the dimensions we consider for the College based on our scope of work outlined in our Annual Audit Plan, along with our overall assessment of each of these in terms of red / amber / green. Our assessment is built on our consideration of the risks facing the College, the extent to which these are mitigated by the College’s processes and controls, and our assessment of management’s process in implementing recommendations from the 2016/17 audit, where appropriate.

Financial sustainability	<ul style="list-style-type: none"> The financial environment in which the College operates continues to be challenging. There is significant uncertainty going forward around key income and expenditure sources, in particular around externally controlled factors such as future increases to staff costs through national bargaining and future SFC funding. The College has made material progress in recovering and improving its financial position from 2016/17 to 2017/18. There is a clear plan designed to achieve a robust financial position in line with the College’s strategic aims through to 2023. There are significant risks attached to the delivery of this financial position; it is vital that the medium term financial plan is kept under rigorous review and updated as sensitivities and assumptions crystallise. 	Amber
Governance and transparency	<ul style="list-style-type: none"> The College has a number of the key requirements in place for good governance and transparency. However there is an ongoing risk of erosion of the boundaries between governance and management in certain areas through the current working arrangements that need to be addressed. The College has identified two areas of non-compliance with the Scottish Code of Good Governance in its Governance Statement, but has outlined mitigating actions implemented by the end of December 2018. 	Amber

2. **2017/18** financial statements audit

2. Summary of 2017/18 audit opinion



The detailed form and content of our audit report, and the requirements underpinning the report, are set out in guidance issued by Audit Scotland. This covers our reporting requirements in accordance with International Standards on Auditing (UK), plus those matters prescribed by the Code.

Element of Audit opinion	Nature of opinion and basis for that
Opinion on financial statements	Unqualified opinion
<ul style="list-style-type: none"> • Truth and fairness of the state of affairs of the College at 31 July 2018 and of the deficit for the year then ended • Preparation of the financial statements in accordance with the relevant financial reporting framework 	<ul style="list-style-type: none"> • Performance of audit procedures to respond to our assessed risk of misstatement, including significant risks • Accounting policies are appropriate and estimates are reasonable • Completion of financial statement disclosure checklists / consideration of relevant guidance issued by Audit Scotland
Conclusions relating to the going concern basis of accounting	No matters to report
<ul style="list-style-type: none"> • The use of the going concern basis of accounting used in the preparation of the financial statements is not appropriate 	<ul style="list-style-type: none"> • Supported by our core financial statements audit work, supplemented by our wider scope audit procedures in respect of financial sustainability
Other information in the financial statements	No matters to report
<ul style="list-style-type: none"> • We are required to consider whether the other information in the financial statements is materially inconsistent with the annual accounts or our knowledge obtained in the audit 	<ul style="list-style-type: none"> • Review of committee minutes and papers / discussions with management / understanding of the business
Opinions on matters prescribed by Audit Scotland	Unqualified opinions
<ul style="list-style-type: none"> • The audited part of the Remuneration and Staff Report has been properly prepared in accordance with applicable regulations • Information in the Accountability Report / Annual Governance Statement is consistent with the financial statements, and prepared in accordance with the relevant guidance 	<ul style="list-style-type: none"> • We agreed the form of the report to the regulations and agreed the disclosures to underlying accounting records and supporting schedules • We reviewed the content of the narrative statements to the information known to us in the audit, and against the requirements of the guidance
Matters on which we are required to report by exception	No matters to report by exception
<ul style="list-style-type: none"> • Whether adequate accounting records have been kept • Whether financial statements and the audited part of the Remuneration and Staff Report are not in agreement with the accounting records • Whether we have not received the information we require for our audit 	<ul style="list-style-type: none"> • We were provided with all the information we required • We have been able to agree information to the accounting records

The annual financial statements enables the College to demonstrate its accountability for the resources at its disposal, and its overall performance in the application of those resources during the year. They also enable the College to demonstrate openness and transparency in its governance and remuneration arrangements.

Financial Statement preparation 2017/18

Compliance with requirements

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

The financial statements were prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder issued by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005 and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

Presentation and quality of financial statements

Management provided completed draft financial statements, including the Performance Report, Accountability Report and Remuneration and Staff Report at the start of the audit fieldwork; in line with the agreed timetable. A number of iterations of the front end narrative sections of the financial statements were provided in advance of the audit to facilitate timely review.

Draft financial statements provided by management represented a notable improvement compared to 2016/17; reflecting the timeliness of preparation and investment made by management before the yearend. We made a number of suggestions to enhance the presentation and readability, and to ensure compliance with disclosure requirements. In particular, the financial statements had not been updated for the new requirements of the SFC's 2017/18 Accounts Direction due to the timing of the direction being later than when the initial draft was completed. Management responded positively to audit comments and addressed all material comments in the final version of the financial statements.

While the financial statements are materially compliant with the requirements outlined in the SFC 2017/18 Accounts Direction, FE SORP and FRS 102, the readability and usefulness to the reader should be an ongoing area of focus and improvement.

Audit differences

We identified six audit differences arising from our audit work, all of which have been adjusted by management. The impact of the adjusted differences was to increase the deficit by £25,000. All audit adjustments are outlined in Appendix E.

The annual financial statements enables the College to demonstrate its accountability for the resources at its disposal, and its overall performance in the application of those resources during the year. They also enable the College to demonstrate openness and transparency in its governance and remuneration arrangements.

Financial Statement preparation 2017/18: Other areas

Arms Length Foundation (ALF)

As a result of the reclassification of Scotland's Colleges from 1 April 2014, Arm's Length Foundations (ALF) were set up in order that any reserves were not required to be returned to the Scottish Government. Moray College transferred assets to the Scottish Colleges Foundation. At 31 July 2018 approximately £65,000 remained in the ALF. This is to be awarded by the ALF to applicants in line with the ALF's charitable objectives. The governance arrangements between colleges and ALFs across the sector is an area of increased focus in 2017/18, in particular around the independence of the ALF and influence college's can extend over their operations.

We have re-assessed the independence of the ALF for the year ended 31 July 2018 to consider the requirement for consolidation of the ALF into the College financial statements. We have concluded that the ALF is independent of the College based on a number of factors:

- There is a board of trustees which is independent of the College; no trustees are appointed by the College
- All applications for funding from the ALF are reviewed thoroughly against the ALF's charitable objectives
- Day to day management of the ALF is not delegated to, and does not involve, management from the College

We have also considered that should the College be deemed to have exercised significant influence or control over the ALF, based on the financial position at 31 July 2018 and the 2017/18 financial transactions, the ALF would not be considered material to the College's financial statements.

The annual financial statements enables the College to demonstrate its accountability for the resources at its disposal, and its overall performance in the application of those resources during the year. They also enable the College to demonstrate openness and transparency in its governance and remuneration arrangements.

Opinions on matters prescribed by the Audit Scotland

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

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

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

We have reviewed the governance statement and provided commentary to management around enhancing the layout and structure of the information, including the requirement to include committee attendance. See further commentary within governance and transparency section of wider-scope. We are satisfied that the information with the Accountability Report is consistent with the financial statements and has been prepared in accordance with applicable requirements.

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

We are satisfied that the auditable part of the Remuneration and Staff Report has been properly prepared in accordance with regulations.

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

In 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.

2. Significant audit risks



Significant risk - risk of fraud in income and expenditure recognition: ISA (UK) 240 requires us to make a rebuttable presumption that the fraud risk from income recognition is a significant risk. In the public sector, we extend that to consider the risk of material misstatements by manipulation of expenditure.

Our overall approach

As set out in our Annual Audit Plan, given the nature of funding to the College from the Scottish Funding Council (SFC), we rebutted the assumed fraud risk in respect of this income stream. However we recognised a revenue recognition risk for tuition income and other material income in respect of possible manipulation of cut-off around the financial year end.

We also recognised the same risk around incorrect recognition of non-pay expenditure in line with Practice Note 10.

What did we do in response to the significant risk?

We undertook the following procedures as part of our audit:

- Reviewed and tested revenue and expenditure recognition policies against the relevant accounting standards and the SORP
- Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias
- Developed a testing strategy in respect of material revenue and expenditure streams:
 - For tuition fees and education contracts, we performed an analytical review of the key movements in the year and substantive testing across a sample of contracts to ensure appropriate recognition
 - For SFC and other funding body grant income we reviewed all material grant funding recognised in the year for any indicators of either claw-back or that the terms and conditions of the financial memorandum have not been complied with in all material respects
 - For other income and expenditure, we performed an analytical review of movements and selected key item and representative samples for testing, and obtained the third party evidence along with confirmation of the balance received / receivable by the College
- We performed focused additional testing around income and expenditure transactions posted nearer to the year end to gain comfort that any material items are recorded in the correct accounting period. In particular we focused on material income transactions incurred after 31 July, but included in the 2017/18 financial ledger, and material expenditure transaction incurred before 31 July but deferred into 2018/19
- We reviewed and tested a sample of debtor balances at the year end, including any material balances. We undertook an assessment of aged balances held on the balance sheet at year end including investigation of unusual items, such as those past payment due date
- We tested an extended sample of year end income and expenditure accruals held on the balance sheet at 31 July. We obtained evidence to support management's conclusion that balances related to transactions in respect of the financial year in question

What are our conclusions?

Our testing has not identified any material misstatements relating to revenue and expenditure recognition. We identified one misstatement in respect of the valuation of historic aged debtors for tuition fee income which was adjusted by management. We did not identify any areas of significant estimation or judgement as part of our audit work in these areas.

2. Significant audit risks (cont.)



Significant risk – management override: As identified in ISA 240, management is in a unique position to perpetrate fraud in its financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively.

We respond to this risk on every engagement

Audit procedures performed	What did we find?
<p>We gave consideration to the risk of fraud, inquiring of management about their assessment of the risks of fraud and the controls put in place to address those risks. We also updated and developed our understanding of the oversight of those charged with governance over management’s processes over fraud.</p>	<p>We have not identified any material weaknesses in controls or evidence of material management override.</p> <p>As part of the audit process we wrote to the chair of the Audit Committee to make inquiries around both the governance arrangements at the College and any instances or possible non-compliance identified in the year. Those charged with governance identified through their response no instances of non-compliance. They also did not draw to our attention to any significant matters or material weaknesses or concerns in respect of the College’s governance arrangements.</p>
<p>Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements</p>	<p>We obtained a full list of journals posted to the general ledger during the year, and used our bespoke data analysers to identify any unusual journal types or amounts based on our identified risk areas for the audit. We then tested a sample of these journals, understood their purpose and agreed and corroborated them to supporting documentation.</p>
<p>Review accounting estimates for evidence of management bias, including management’s retrospective consideration of prior year estimates.</p>	<p>We identified and considered the appropriateness of key accounting estimates, including provisions, and their susceptibility to bias. Management has disclosed their consideration of the critical accounting judgements and key estimates in the financial statements. We have reviewed these and agree with the detail of the assessment performed.</p>
<p>Evaluate the business rationale for any significant unusual transactions</p>	<p>We did not identify any significant unusual transactions outside the normal course of business.</p>
<p>Consistency and application of accounting policies / overall presentation of financial information</p>	<p>We consider the accounting policies adopted by the College to be appropriate. There are no significant accounting practices which materially depart from what is acceptable under FRS 102 or the SORP.</p>
<p>What are our conclusions?</p>	
<p>We have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls.</p> <p>There was no disagreement during the course of the audit over any accounting treatment or disclosure. We encountered no significant difficulties in the audit through our interaction with management.</p>	

Valuation of property, plant and equipment: Our overall approach

The value of property, plant and equipment ("PPE") represents a significant balance on the College's balance sheet and is subject to valuation changes, depreciation charges and possible impairment. The total value of the College estate at 31 July 2018 was £24.1 million, and was last subject to an interim valuation in 2017, with a full revaluation due again in 2019.

As set out in our Annual Audit Plan, given that a number of assumptions are used in valuing property, plant and equipment, we assigned a higher inherent risk to the valuation of PPE at 31 July 2018.

What did we do in response to the risk?

We undertook the following procedures as part of our audit:

- We reviewed management's own assessment of impairment of the estate at the financial yearend and challenged the key assumptions within this assessment
- We reviewed the College's backlog maintenance plans, including consideration of possible indicators of impairment of the existing estate, and whether backlog maintenance expenditure in the year had been correctly accounted for as capital or revenue expenditure
- We agreed the PPE balances disclosed in the financial statements to underlying accounting records, in particular the College's fixed asset register
- We tested a sample of additions and disposals in the year, considering the appropriateness of capitalisation in line with the College's accounting policies and to ensure the correspondingly replaced assets had been appropriately disposed
- We considered any material capital grant income to supporting documentation and consideration of the appropriateness of recognition against the terms of any grant conditions, the College's own accounting policies and the applicable accounting standards

What are our conclusions?

Management provided an impairment consideration paper on 13 November 2018, considering the valuation of the estate at the balance sheet date and concluding there was no adjustment necessary to the valuation of the estate. We challenged this view and considered against the current plans for backlog maintenance expenditure on the estate, being £1.3 million planned in 2018/19 and an identification of £13 million in total.

Our testing has not identified any material misstatements relating to property, plant and equipment. At the start of our audit work management made us aware of a number of fully depreciated assets on the fixed asset register that it could not verify the College still held. Based on the age of the assets and their nature (being low value items unlikely to still be in use) it was agreed that management remove these from the fixed asset register and the financial statements. There was no impact on the net book value of assets. Management has agreed to review the fixed asset register on an annual basis in advance of the audit to remove any assets that cannot be physically verified by the College.

Recommendation one

2. Other inherent risks (cont.)



Accounting for retirement benefits: Our overall approach

In line with accounting standards, the College recognises the cost of retirement benefits provided to its staff in the reported cost of service when they are earned by the employee and not when the pension benefits are actually paid.

The College's employees belong to two principal pension schemes, the Scottish Teachers Superannuation Scheme (STSS) and the Northeast Scotland Pension Scheme (LGPS). The present value of Unfunded Obligations in relation to early retirements agreed in previous years is £2.6 million (2016/17: £2.9 million). As at 31 July 2018, the College's share of the pension scheme net liability is £2.2 million (2016/17: £7.4 million).

The information disclosed is based on the FRS 102 report issued to the College by the actuary appointed by the Northeast Scotland Council Pension Fund. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

What did we do in response to the risk?

As a result of the thematic review performed by the Financial Reporting Council, there has been an increase in focus in accounting for retirement benefits and, as such, auditors have additional requirements to address in completing and concluding on the valuation of these balances. We undertook the following procedures as part of our audit:

- Obtained the actuarial report at the year end date for the scheme and utilised our in-house experts to assess both the robustness of the methodology used to derive the key actuarial assumptions, and the reasonableness and consistency of the assumptions underpinning such reports
- We wrote to the actuaries of the pension scheme to confirm their independence and expertise to ensure this was appropriate and sufficient for the purposes of preparing their FRS 102 report
- We wrote to the auditor of the Pension Fund to gain assurance over the completeness, existence and valuation of the assets at 31 March 2018, as well as the processes and controls to ensure accurate information is obtained in respect of the College's share of fund assets
- We performed additional testing on the College's share of the fund pension assets at 31 July, performing roll forward procedures on its share of assets from 31 March to the College balance sheet date
- We reviewed the calculation of the College's valuation of future early retirement liabilities at 31 July and completed integrity testing over the inputs into the calculation

What are our conclusions?

We concluded that we were able to rely on the work of management's specialists - the pension fund actuaries - and were satisfied that the actuarial assumptions used in the preparation of the FRS 102 report were appropriate. These include the assumptions directed to be used by management (such as assumptions over future salary cost increases).

We obtained relevant assurances from the pension fund auditor to support our conclusions.

Our testing has not identified any material misstatements relating to future early retirement liabilities.

3. Wider scope audit

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 should be delivered.

Amber

- The financial environment in which the College operates continues to be challenging. There is significant uncertainty going forward around key income and expenditure sources, in particular around externally controlled factors such as future increases to staff costs through national bargaining and future SFC funding.
- The College has made material progress in recovering and improving its financial position from 2016/17 to 2017/18. There is a clear plan designed to achieve a robust financial position in line with the College's strategic aims through to 2023. There are significant risks attached to the delivery of this financial position; it is vital that the medium term financial plan is kept under rigorous review and updated as sensitivities and assumptions crystallise.

Elements of financial sustainability, and our assessment of the College's arrangements

We consider whether:

- The College's revenue and capital outturn for 2017/18 was in line with the approved budgets, with material changes to budgets identified and reported?
- The College has a medium term financial strategy and plan which takes into account risks and uncertainties?
- The College has arrangements to address any identified funding gaps?

The context for financial sustainability

In June 2018, Audit Scotland published their report Scotland's colleges 2018. This report provided an overview of the college sector in Scotland and provided an update on college finances across the sector. The report highlighted that while the college sector's underlying financial position improved in 2016/17, several colleges face significant financial challenges. Scotland's 20 incorporated colleges reported an overall underlying financial surplus for 2016/17 of £0.3 million. This compares to an underlying deficit of £8 million in 2015/16. Across the sector, the cash held by colleges increased by 13 per cent in 2016/17 and the net value of their assets – such as land and property, compared against financial liabilities such as pension costs – grew by 10%. However, these sector-wide increases mask significant variations between colleges.

The report noted that several factors pose a risk to colleges' financial sustainability, including: the future impact of national bargaining for support staff; uncertainties around long-term funding of improved employment terms; the cost of maintaining buildings and land; and the potential impact of leaving the European Union.

The SFC's 2017 estates condition survey indicates that college buildings require urgent and significant investment. The survey estimates a backlog of repairs and maintenance over the next five years of up to £360 million. The SFC is providing £27 million of capital funding to colleges in 2018/19 to cover the very high priority needs identified in the condition survey. We have commented on the College estate and backlog maintenance earlier in this report.

For the College, 2017/18 represents year two of the College's three year financial recovery plan, agreed following the College's section 22 report as a result of acute financial pressures in 2015/16. In previous years the College was required to draw down in advance on its UHI funding to meet its day to day operational costs.

2017/18 College financial position

The College has reported an actual accounting deficit of £461,000 for the year (2016/17: £463,000). Following actuarial gains of £5.7 million, the College reported total comprehensive income of £5.3 million (2016/17: £1.3 million surplus). The 2017/18 College budget was approved in June 2017 for a deficit of £240,000 (being exclusive of SFC net depreciation adjustment and any pension adjustments), resulting in a forecast underlying operating surplus of £87,000 after removing net depreciation. The budget recognised significant uncertainties around the Scottish Government's funding of national pay bargaining and the potential impact this could have on the College's cost base.

Elements of financial sustainability, and our assessment of the College's arrangements (cont.)

2017/18 College financial position (continued)

As part of the submission of its financial forecast return ("FFR") for 2018/19, management outlined the key movements in the year between the College's 2017/18 budget and actual position. It noted a number of movements in both income and expenditure, with both being lower than initially budgeted. We have reviewed the movements against our understanding from our yearend audit work, and our review of the budget from the prior year audit. We consider the movements to be reasonable given the timing of variances crystallising and not indicative of underlying inaccuracies in the College's budget process.

The College's underlying financial position continues to improve year on year, with an underlying operating surplus disclosed in the financial statements of £142,000 after removal of non-cash accounting adjustments (relating to net depreciation). This is against a budgeted underlying operating surplus of £87,000. Both throughout the financial year and at the 31 July yearend the College had positive cash and is no longer reliant on cash advances from UHI to support operational expenditure, and is not forecast to be so again through to 2022.

Medium-term financial strategy and plan

The College has prepared its five-year financial forecasts from 2018 to 2023 and submitted these to the SFC through its FFR. The forecasts have been prepared on the basis of the College's core strategy, which was updated during the year. We have outlined the forecast position through to 2023, along with the possible impact of key sensitivities.

Year	18/19 / £000's	19/20 / £000's	20/21 / £000's	21/22 / £000's	22/23 / £000's	Total
Accounting surplus / (deficit)	(100)	(120)	(220)	(350)	(400)	(1,190)
Underlying surplus / (deficit)	227	304	204	74	24	833
College assumptions around future SFC funding of national bargaining costs	-	-	986	986	986	2,958
Sensitivity around commercial income growth - variance between 10% and 2%*	26	55	89	126	167	462
Sensitivity around commercial income growth - variance between 10% and 5%*	16	35	57	82	110	300

* Shows the impact on future forecast between the 10% commercial income growth forecast by management and other scenarios - 2% increase in commercial income year on year and 5% increase year on year.

The forecast prepared by management shows recurring surpluses and as a result a continually improved yearend position for the College in respect of its underlying operating position through the five year period. This builds on the improved financial performance of the College in 2016/17 and 2017/18. Management has noted in its preparation of these forecasts a number of assumptions that could have a significant impact on the future financial position:

- Assumption that increased costs associated with the recently completed (for support staff) and ongoing (for teaching staff) national bargaining negotiations will be fully funded by the SFC throughout the period forecast
- Assumption of a 10% increase in commercial income for the College in line with the objectives outlined in its revised strategy throughout the period forecast, with other operating expenditure increases contained to 2% increases annually
- Assumption that cost of living increases through the period remain at approximately 2%
- The College has correctly assumed capital funding for backlog maintenance for 2018/19 only, in line with SFC guidance, however has not forecast any additional funding from its own resources from 2019/20 onwards

Elements of financial sustainability, and our assessment of the College's arrangements (cont.)

Assessment of the College's Financial Forecast Return

We have reviewed the College's FFR submitted to the SFC for 2018/19 through 2022/23, as well as the underlying assumptions underpinning the return. The forecast submitted is based on robust management workings for the five year period and represent management's best estimate of the future position. In our view while the assumptions are based on sound underlying supporting information, there remains a material risk around the realisation of this forecast position given the sensitivities attached to some of the key assumptions. In particular:

- Management's assumption that additional costs resulting from national bargaining agreements for staff will be fully funded throughout the five year period is subject to the SFC confirmation of funding on an annual basis for the forecast period. There are variations in assumptions around this across the sector
- While the College has developed a plan as part of its strategy going forward to achieve a 10% year on year increase in commercial income, this is an ambitious objective when combined with controlling non-payroll expenditure to 2% year on year increases. In our experience a forecast increase in commercial income of this scale is rare across the further education sector. We have outlined the sensitivity to the future financial position around the scale to which this is achieved on the proceeding page
- The SFC identified, through its condition survey completed in 2017 £13 million in backlog maintenance, with which management concurs on the requirement for subsequent investment. The College has confirmed with the SFC funding of £1.3 million to be provided by 31 March 2019, however management cannot be certain of funding after this date, therefore has not included future funding from the SFC beyond 2019. While this is the appropriate approach given the uncertainty around future SFC funding, should further funding not be available the College will have to consider how to finance any remaining estate maintenance

Overall, our view is that the College has made material progress in recovering and improving its financial position from 2016 to the financial yearend 31 July 2018. It has a clear plan designed to achieve a robust financial position in line with the College's strategic aims through to 2023. This plan is ambitious, and as such there are material risks attached to the delivery of this plan and the achievement of this financial position. In addition there are a number of assumptions included which remain outside of management's control, and as such could be subject to significant variance. It is vital that the medium term financial plan is kept under rigorous review and updated as sensitivities and assumptions crystallise. Management should ensure that UHI, as the College's regional strategic body, is aware of any significant changes to assumptions or new information as it becomes available, and not just on the annual return deadline.

Recommendation two

Focus on EU withdrawal

Withdrawing from the European Union will have implications for the college sector. In October 2018 Audit Scotland published a paper setting out the key issues for the public sector. The issues were identified around the three themes of people, finances and rules and regulations. The risks and opportunities presented by EU withdrawal will vary markedly between organisations. Some parts of the public sector are already experiencing an impact. Audit Scotland expects all public bodies to be assessing the potential impact of EU withdrawal on their organisation, and identifying any specific risks and how they will respond to them.

Discussions with management and review of Board papers has confirmed that the College is sighted on Brexit as likely to have an impact on both the further education and wider College sector, while recognising uncertainty as to the detail behind those risks. We have confirmed as part of our review of the College's medium term financial plans that it does not assume any future income through EU grant funding from 2018/19. This has had minimal impact on the College's forecast financial position in 2018/19 as it received no ESF funding in 2017/18, and Erasmus funding received has been offset by related expenditure.

Outcomes from the Audit Scotland Overview Report

The overview report notes that in 2016/17 colleges overall exceeded the SFC's activity target and delivered more credits than in 2015/16. In 2017/18, the College slightly over delivered its credit target of 18,907. The report noted the College to have attainment levels towards the bottom of the sector in 2016/17, however the 2017/18 performance noted in the financial statements shows a significant improvement in this area (60.1% in 2016/17 to 69% in 2017/18). In respect of its financial position, the report noted the challenging position the College had been in in 2015/16 and the improved position in 2016/17, in particular in respect of increased cash and an underlying surplus.

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.

Amber

- The College has a number of the key requirements in place for good governance and transparency. However there is an ongoing risk of erosion of the boundaries between governance and management in certain areas through the current working arrangements that need to be addressed.
- The College has identified two areas of non-compliance with the Scottish Code of Good Governance in its Governance Statement, but has outlined mitigating actions implemented by the end of December 2018.

Elements of governance and transparency, and our assessment of the College's arrangements

We consider whether:

- Is the governance framework sound and arrangements operating effectively?
- Is there effective scrutiny, challenge and transparency on decision making?
- Is the Governance Statement complete and does it reflect key findings from audit, scrutiny and inspection?

Governance and transparency

While we have not identified any significant risks in relation to the College's governance arrangements through our audit planning, we consider the adequacy and effectiveness of the College's governance arrangements as part of our audit work, and the appropriateness of the related disclosures made in the financial statements around governance and transparency.

The Board is responsible for establishing robust governance arrangements. This includes ensuring effective systems of internal control, including arrangements to safeguard public money, and compliance with applicable laws and regulations.

The College has in place a number of the key requirements for good governance and transparency. We have reviewed Board minutes and papers and found these to set out clearly the matters considered and discussed. Standing Orders regulate how the business of the College is conducted. The Board has approved detailed terms of reference for its standing committees. The College publicises Board and standing committee agendas, minutes and papers on their website on a timely basis and information, including financial performance is generally clear and concise.

Audit and Risk Committee arrangements

As part of our consideration of governance and transparency arrangements through the year we have attended all meetings of the Audit Committee. We have noted extensive interaction between management and the non-executive members of the committee, and robust challenge by the committee through the year. We have discussed with both management and those charged with governance the risk of the committee assuming a management role through its scrutiny and challenge, becoming involved in day to day operational management matters. This is also evidenced by a significant number of draft reports being reviewed and commented on by the committee, rather than only final reports being presented for consideration.

These practices can increase the risk of eroding the segregation between management and those charged with governance, and is not considered best practice. It also adds further to the committee's workload, impacting its effectiveness. As noted above, the College publishing Audit Committee papers on its website to support transparency has also resulted in incomplete reports with possible factual errors or subsequently amended conclusions being made public.

Recommendation three

Elements of governance and transparency, and our assessment of the College's arrangements (cont.)

Internal audit

The College's internal audit service provides an important source of assurance to inform management and the Board's assessment of the College's governance arrangements. We have reviewed the internal audit annual report for 2017/18. Internal audit's opinion for the year was based on its agreed audit plan for 2017/18, as approved by the Audit Committee. For 2017/18 the Internal Auditor's annual statement of assurance notes "the College has adequate and effective arrangements for risk management, control and governance. Proper arrangements are in place to promote and secure Value for Money. This opinion has been arrived at taking into consideration the work we have undertaken during 2017/18".

A key part of internal audit's work in the year was the review of implementation of outstanding recommendations. As part of the annual audit reporting, internal audit has confirmed that all 67 historic outstanding recommendations have been agreed as either implemented by management (61), or considered by management and not implemented (6), and all recommendations due at 31 October 2018 have also been implemented on time. This represents a material continued improvement in the College's arrangements for addressing internal audit recommendations.

Governance Statement

We reviewed the College's Governance Statement against the requirements outlined in the SFC's 2017/18 Accounts Direction. This includes the requirement to conclude on the College's compliance with the Scottish Code of Good Governance, or to explain any areas of non-compliance. We also considered management's arrangements for its own self-assessment over compliance with the Code through the governance checklist provided to all incorporated Colleges by UHI during the year.

Management's initial assessment of compliance with the Code of Good Governance noted full compliance. Through our review of the checklist and discussions with management this was amended to identify two areas of non-compliance with actions undertaken to ensure full compliance by 31 December 2018.

We made a number of recommendations to enhance the presentation and disclosures in the Governance Statement complied with the core requirements. These were addressed by management.

Elements of governance and transparency, and our assessment of the College's arrangements (cont.)

Risk management

The College's approach to risk management is set out within the risk management procedure document. This was formally approved by the Board in December 2017. There is routine reporting of the College's risk register to the senior management team. The Audit Committee reviews the risk register on a routine basis and the Board considers the risk register as part of its agenda.

Enquiries of those charged with governance

During 2017/18 we formally wrote to the chair of the Audit Committee to make inquiries around the College's governance arrangements, including consideration by those charged with governance in respect of compliance with laws and regulations; identification of fraud, error and breaches of internal control; and material litigation and claims. We considered the response received from the chair of the Audit Committee on 30 October against our wider understanding of the College and other inquiries made through the year. No significant matters were noted.

Severance payments

During 2017/18 the College made payments of £90,000 to three employees who left the College under voluntary severance agreements, as approved by the Regional Strategic Body and the SFC. These payments were approved by the College's Remuneration Committee. We confirmed a sample of payments to evidence of approval from the committee, and agreed that they were consistent with SFC guidance around severance payments.

Audit Scotland national reports

It is important that the College has embedded arrangements to ensure that consideration is appropriately given to national reports published by Audit Scotland. This should include ensuring that management has evaluated the implications for the College and that the reports and assessment are shared with the Board.

Discussions with management highlighted that national reports are reviewed by management and the impact on the College is considered. These are taken to the Board as and when deemed necessary.

Appendices

- A – Code of Audit Practice: responsibilities
- B – Independence and audit quality
- C – Required communications
- D – Action plan
- E – Summary of audit differences

In our Annual Audit Plan, we provided a summary of the responsibilities on audited bodies falling within the public sector audit framework, as set out in the Code of Audit Practice (the Code).

Responsibilities of audited bodies

Corporate governance	Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.
Financial statements and related reports	<p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> • preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. • maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures. • ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority. • maintaining proper accounting records. • preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body. <p>Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.</p> <p>Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate Internal Audit and risk-management functions.</p>
Standards of conduct / prevention and detection of fraud and error	Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	<p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> • such financial monitoring and reporting arrangements as may be specified • compliance with any statutory financial requirements and achievement of financial targets • balances and reserves, including strategies about levels and their future use • how they plan to deal with uncertainty in the medium and longer term • the impact of planned future policies and foreseeable developments on their financial position.
Best Value	The Scottish Public Finance Manual sets out that accountable officers appointed by the Principal Accountable Officer for the Scottish Administration have a specific responsibility to ensure that arrangements have been made to secure best value.

B. Independence and audit quality



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

What we are required to communicate

The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY), its directors and senior management and affiliates, and you, including all services provided by us and our network to you, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 August 2017 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan, dated May 2018.

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

We consider that our independence in this context is a matter which you should review, as well as us. It is important that management and members of the Board consider the facts known collectively to you and come to a view.

Audit fees – payable in the respect of the year ended 31 July 2018

Component of fee:	2017/18	2016/17
Auditor Remuneration – expected fee	£13,260	£13,130
Fee variations*	£2,710	£7,800
Pooled Costs	£850	£820
Contribution to Audit Scotland costs	£740	£750
Total fee	£17,560	£22,500

*Fee variation in 2017/18 is in respect of additional work around wider scope risk work, agreed with management at planning stage and communicated to the Audit Committee in our Annual Audit Plan in May 2018.

Audit Quality

International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

The EY 2018 UK Transparency Report can be accessed on our website at www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018. This material is published to provide a timely and relevant source of information about EY in general, and our audit business in particular.

The disclosures are extensive. For example, they explain our outlook and how we are structured and governed, including the role of our Independent Non-Executives and how we apply the requirements of the UK's Audit Firm Governance Code. We refer to the quality of our audits and our commitment to recruiting, developing and diversifying our people and talent pool. We also explain how we manage our risks and remain innovative and technologically advanced in what we do and how we do it.

Maintaining high audit quality across all of our engagements is of paramount importance to us. Our transformational Audit Quality Programme continues and is a part of the global EY Sustainable Audit Quality Programme (SAQ).

Our Audit Quality Board (AOB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AOB meets monthly and also holds an annual strategy session. The AOB reports to the EY UK Board. The AOB receives regular updates on regulatory matters, results of internal and external reviews, results of root cause analysis, resourcing, the SAQ programme and pursuit approvals, as well as a comprehensive dashboard on quality measures.

Our Audit Quality Support Team (AQST), which started within the SAQ programme, reviews 40 to 50 audits each audit cycle providing challenge and guidance to the engagement teams. These are in-depth reviews carried out by experienced auditors independent of the audit team. AQST reviews enhance the quality of both the audit under review and other audits on which team members apply the lessons learned. The AQST has now become a business-as-usual function.

Audit Scotland – Audit Quality Framework / Annual Audit Quality Report

Audit Scotland's Appointments and Assurance Team are responsible for applying the new Audit Quality Framework across all financial audits and performance and Best Value audits. This covers the quality of audit work undertaken by Audit Scotland staff and appointed firms. The team are independent of audit delivery and provide assurance on audit quality to the Auditor General and the Accounts Commission.

We support Audit Scotland in their commitment to reporting on audit quality through responding to requests for information and providing the results of internal quality reviews undertaken in respect of relevant public sector audits in Scotland.

The most recent audit quality report which covers our work at the College since appointment can be found at: www.audit-scotland.gov.uk/uploads/docs/report/2018/as_audit_quality_1718.pdf.

Required communication	Our reporting to you
<p>Terms of engagement / Our responsibilities</p> <p>Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.</p> <p>Our responsibilities are as set out in our engagement letter.</p>	<p>Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice</p>
<p>Planning and audit approach</p> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>	<p>Annual Audit Plan – May 2018</p>
<p>Significant findings from the audit</p> <ul style="list-style-type: none"> • Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures • Significant difficulties, if any, encountered during the audit • Significant matters, if any, arising from the audit that were discussed with management • Written representations that we are seeking • Expected modifications to the audit report • Other matters if any, significant to the oversight of the financial reporting process 	<p>This Annual Audit Report</p> <p>We request written representation from you in respect of key matters arising during the course of our audit, and in accordance with auditing standards. A copy of this letter is provided for your consideration and signature at the time of approval of the financial statements.</p>
<p>Going concern</p> <p>Events or conditions identified that may cast significant doubt on the College's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> • Whether the events or conditions constitute a material uncertainty • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements • The adequacy of related disclosures in the financial statements 	<p>No conditions or events were identified, either individually or together to raise any doubt about the College's ability to continue for the 12 months from the date of our report.</p>
<p>Misstatements</p> <ul style="list-style-type: none"> • Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Corrected misstatements that are significant • Material misstatements corrected by management 	<p>This Annual Audit Report</p>
<p>Fraud</p> <ul style="list-style-type: none"> • Enquiries of the Audit & Risk Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the College • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist • A discussion of any other matters related to fraud, relevant to the Audit & Risk Committee 	<p>This Annual Audit Report</p>
<p>Consideration of laws and regulations</p> <ul style="list-style-type: none"> ▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▶ Enquiry of the Audit & Risk Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit & Risk Committee may be aware of 	<p>This Annual Audit Report</p> <p>We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.</p>

Required communication	Reference
<p>Related parties</p> <p>Significant matters arising during the audit in connection with the College's related parties including, when applicable:</p> <ul style="list-style-type: none"> • Non-disclosure by management • Inappropriate authorisation and approval of transactions • Disagreement over disclosures • Non-compliance with laws and regulations • Difficulty in identifying the party that ultimately controls the College 	<p>No significant matters have been identified.</p>
<p>Independence</p> <p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> • The principal threats • Safeguards adopted and their effectiveness • An overall assessment of threats and safeguards • Information about the general policies and process within the firm to maintain objectivity and independence 	<p>Annual Audit Plan</p> <p>This Annual Audit Report – Appendix B</p>
<p>Internal controls</p> <p>Significant deficiencies in internal controls identified during the audit</p>	<p>This Annual Audit Report – no significant deficiencies reported</p>
<p>Subsequent events</p> <ul style="list-style-type: none"> • Where appropriate, asking the Audit & Risk Committee whether any subsequent events have occurred that might affect the financial statements. 	<p>We have asked management and those charged with governance. We have no matters to report.</p>
<p>Material inconsistencies</p> <p>Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</p>	<p>This Annual Audit Report</p>

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

Classification of recommendations

Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.

Grade 2: Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.

Grade 3: Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
1	<p>Fixed asset register review</p> <p>At the yearend audit a significant number of fixed assets with nil value which could not be verified by management remained on the fixed asset register.</p>	<p>Management should ensure the fixed asset register is reviewed annually in advance of the financial statement audit to remove any assets which are no longer in use or whose existence cannot be verified.</p> <p style="text-align: right;">Grade 3</p>	<p>Agreed.</p> <p>This has been actioned for 2017/18, and will form part of annual review of fixed assets register going forward.</p>
2	<p>Future financial forecasts</p> <p>The College has a clear plan designed to achieve a robust financial position in line with the College's strategic aims through to 2023. However, there are significant risks attached to the delivery of this financial plan, and it is vital that the medium term financial plan is kept under rigorous review and updated as sensitivities and assumptions crystallise going forward.</p>	<p>Management should ensure that UHI, as the College's regional strategic body, and the SFC, is aware of any significant changes to assumptions for new information as it becomes available, and not just on the annual return deadline, in particular as new information materially impacts any key assumptions in future forecasts.</p> <p style="text-align: right;">Grade 1</p>	<p>Agreed.</p> <p>Reforecasting financial plans at the six and nine month period of the year was carried out during 17/18, and is normal practice. Recent communication from the SFC has requested a reforecast FFR after six months of 2018/19, which will be submitted via the Regional Strategic Body. In addition to the internal reforecasting process, as part of the SFC requirements of the recovery plan management has monthly meetings with the RSB to update them on the current financial position at the College, and any changes in anticipated outturn for the year. Changes are then updated on a monthly basis to the SFC.</p>

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

Classification of recommendations

Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.

Grade 2: Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.

Grade 3: Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
3	<p>Audit Committee working arrangements</p> <p>We have discussed with both management and those charged with governance the risk of the Audit Committee assuming a management role through its scrutiny and challenge, and involvement in day to day operational management matters. This is also evidenced by a significant number of draft reports being reviewed and commented on by the committee, rather than only final reports being presented for consideration.</p>	<p>A point of improvement in the ongoing governance arrangements at the College should be to ensure the Board and committees are able to fulfil their governance and oversight roles without being drawn into involvement in management functions, potentially blurring the distinction between the executive and non-executive responsibilities at the College. This should be achieved through discussion and agreement with management.</p> <p>In the first instance we would recommend ensuring no draft reports are submitted to committee and Board agendas unless critical and time sensitive.</p>	<p>Agreed.</p> <p>To address the issue of draft reports, management will prepare a timeline for approval at the next Audit Committee meeting, which will factor in suitable times for completion of Internal Audit reports with consideration of Audit Committee meeting dates.</p> <p>In respect of the wider governance arrangements, in particular through involvement with management as noted in the recommendation, management will arrange an informal debrief with the chair of the Board to consider the 2017/18 committee arrangements and areas where working arrangements can be enhanced going forward into 2018/19 and beyond. Any actions will be shared with the College's auditors and progress will be specifically considered as part of the Board and committee's self effectiveness review that takes place annually.</p>

Grade 1

E – Summary of audit adjustments



This appendix sets out the significant adjustments processed in the financial statements prior to their finalisation. No unadjusted audit differences were identified.

	Income and Expenditure impact / £	Balance sheet impact / £
1. Adjustment to Working bank account following reconciliation error		
Dr Other Creditors		83,174
Cr Bank		(83,174)
2. Adjustment to Euro bank account to reflect unreconciled items		
Dr Cash and Bank		£25,202
Cr Income / gains and losses on valuation	(9,268)	
Cr Deferred Income		(15,934)
3. Adjustments to Fixed Assets		
Dr Accumulated Depreciation		2,812,603
Cr Fixed Assets		(2,812,603)
4. Adjustment to Loan Balance Outstanding		
Dr Accruals		18,721
Cr Loan > 1 Year		(11,721)
Cr Loan Interest	(7,000)	
5. Write-off of Historical SAAS Debtor		
Dr Bad Debt Written Off	41,831	
Cr Debtors		(41,831)
6. Adjustment to remove the Discretionary Fee Waiver		
Dr Other Creditors		£99,396
Cr Debtors		(£99,396)
Total impact	25,563	(25,563)

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