

# North East Scotland College

Annual Audit Report to the  
Regional Board and the Auditor  
General for Scotland - year  
ended 31 July 2019

17 December 2019



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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 North East Scotland College (the College) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and our responsibilities as set out within Audit Scotland's Code of Audit Practice. This report is for the benefit of the College and is made available to the Auditor General for Scotland and Audit Scotland. 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.

# Key Conclusions from our 2018/19 audit

<p><b>Financial statements: Audit Opinion</b></p>	<p>We have concluded our audit of the College's consolidated financial statements for the year ended 31 July 2019. We identified one unadjusted audit differences arising from the audit. Two audit adjustments were processed as part of the audit, along with a number of presentational adjustments.</p> <p>We concluded the other information subject to audit, including parts of the Remuneration Report and the Annual Governance Statement were appropriate.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">GREEN</p>
<p><b>Presentation and disclosures</b></p>	<p>The draft financial statements and supporting working papers were of a good quality and were received at the start of the audit. There would be benefit in management undertaking a comprehensive review of the content and structure of the financial statements. We were satisfied that the Governance Statement materially reflects the requirements of the Scottish Funding Council's 2018/19 Accounts Direction.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">GREEN</p>
<p><b>Wider Scope: Financial Sustainability</b></p>	<p>The College has undertaken a thorough process to develop the Financial Forecast Return including scenario planning review and challenge of key assumptions. In addition, the College has used these forecasts to develop a Financial Plan for the period 2019-2024. This plan was approved by the Regional Board in June 2019.</p> <p>While the College can demonstrate that plans are in place to deliver a financially sustainable future, there are significant external risks that may continue to impact the financial planning and sustainability of the College.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">AMBER</p>
<p><b>Financial Management</b></p>	<p>We were satisfied that financial reporting was clear and consistent throughout the year. The College reported a consolidated surplus for the year of £0.54 million before actuarial losses in respect of pension schemes and unrealised surplus on the revaluation of land and buildings and the asset held for resale. This resulted in a total comprehensive deficit for the year of £13.048 million. The College has an operating surplus after removal of non-cash accounting adjustments of £2.33 million.</p> <p>Financial performance is scrutinised by the senior executive team, the Finance and Resources Committee and the Board. This monitoring includes expenditure against budget and the forecast outturn for the year.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">GREEN</p>
<p><b>Governance and Transparency</b></p>	<p>The key features of good governance are in place and operating effectively. We concluded that the Governance Statement materially complies with the SFC's 2018/19 Accounts Direction.</p> <p>The College's Audit and Risk Committee has an independent chair. Standing Orders regulate how the business of the College is conducted, and detailed terms of reference are in place for the Board's standing committees. The College continues to embed its risk management arrangements, with an established risk management policy updated during the year.</p> <p>We noted that the College should publish Audit &amp; Risk Committee minutes on its website in line with best practice.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">GREEN</p>
<p><b>Value for money</b></p>	<p>A revised strategic plan was introduced from the start of the 2018/19 academic year. Developed by the Board with input from staff, students and stakeholders, the plan identifies the key strategic priorities over the period 2018-21. There is clear and timely reporting against performance indicators. Annual performance reports are published on the website.</p> <p>The College has an appropriate framework in relation to procurement. We noted that the College should develop an overarching policy for voluntary severance schemes in line with best practice.</p>	<p style="writing-mode: vertical-rl; text-orientation: mixed;">GREEN</p>



# Introduction

## Our key contacts:

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Manager  
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Assistant Manager  
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## Purpose of this report

In accordance with the Public Finance and Accountability (Scotland) Act 2000 (“the Act”), the Auditor General for Scotland appointed EY as the external auditor of North East Scotland College (“the College”) for the five year period 2016/17 to 2020/21.

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 Regional Board and the Auditor General for Scotland, and is presented to those charged with governance, identified as being the Board and the College’s Audit and Risk Committee. This report is provided to Audit Scotland and will be 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 Annual 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 practices 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. Such areas we have identified are highlighted throughout this report together with our judgements and conclusions regarding the College’s arrangements.

## Our independence

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as the College’s external auditor.



## Scope and Responsibilities

The Code sets out the responsibilities of both the College and the auditor (summarised in Appendix A). We outlined these in our Annual Audit Plan, which was presented to the Audit and Risk Committee on 10 July 2019.

Our Annual Audit Plan set out an overview of our audit scope and approach for the audit of the 2018/19 financial statements. We can confirm that we carried out our audit in accordance with the plan. Minor changes were made to the level of materiality that we applied during the audit, to reflect the 2018/19 draft financial statements.

Overall Materiality

Tolerable Error

Reporting threshold

£970,000

£727,500

£48,500

2% of the College's gross expenditure

Materiality at an individual account level

Level that we will report to committee

As outlined in our Annual Audit Plan, based on considerations around the expectations of financial statement users and qualitative factors, we apply a lower materiality level of £1,000 to the audited section of the Remuneration Report. We also apply professional judgement to consider the materiality of Related Party Transactions to both parties.

### Financial statement audit

We are responsible for conducting an audit of the College's financial statements. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; relevant Auditing Standards and applicable Practice Notes issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

Our findings are summarised in Section 2 of this report.

### Wider Scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider scope public audit:

- ▶ Financial management;
- ▶ Financial sustainability;
- ▶ Governance and transparency; and
- ▶ Value for money.

Our findings against each dimension are summarised in Section 3 of this report.



# Financial Statements audit

## Introduction

The annual financial statements provide the College with an opportunity to demonstrate accountability for the resources at its disposal, and report on its overall performance in the application of those resources during the year. We are responsible for conducting an audit of the financial statements of the College and provide an opinion on the financial statements as to:

- ▶ whether they give a true and fair view of the state of affairs of the College and its group as at 31 July 2019 and the deficit for the year then ended;
- ▶ whether they have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- ▶ whether they have been prepared in accordance with the requirements of the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005, and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

This section of our report summarises the audit work undertaken to support our audit opinion, including our conclusions in response to the significant and other risks identified in our Annual Audit Plan.

Our Annual Audit Plan was considered by the Audit and Risk Committee on 10 July 2019. The plan highlighted two areas that we identified as a significant risk of material misstatement or fraud risk:

- ▶ the risk of fraud in revenue and expenditure recognition (significant risk); and
- ▶ misstatements due to fraud or error (fraud risk).

The plan also highlighted two areas of higher inherent risk within the 2018/19 financial statements:

- ▶ Valuation of Property, Plant and Equipment; and
- ▶ Valuation of Pension Liabilities.

## **Compliance with financial reporting 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 Trustees Investment (Scotland) Act and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

## **Presentation and quality of financial statements**

Management provided draft financial statements at the start of the audit, in line with the agreed timetable. The financial statements were complete and supported with appropriate working papers. The financial statements had been updated for the new requirements as outlined in the SFC's 2018/19 Accounts Direction for colleges. Management's approach is to update the financial statements on an annual basis for new reporting requirements. There would be benefit in management undertaking a comprehensive review of the content and structure of the financial statements well in advance of the completion of the 2019/20 reporting cycle. This would aid the user friendliness and improve the readability.

## **Group financial statements**

The College prepared group financial statements, consolidating the results of the College and its subsidiary undertakings, Aberdeen Skills and Enterprise Training Limited and Clinterty Estates Limited (dormant company). We are satisfied that the consolidated financial statements have been prepared accordingly. We do not audit the subsidiary entities.

## **Audit outcomes**

We identified one unadjusted audit difference arising from the audit that breached our reporting threshold. Two adjustments were processed as part of the audit. All adjustments are outlined in Appendices F and G.

We noted a number of disclosure adjustments in the narrative section. Material disclosure adjustments were reflected in updated financial statements.

Our overall audit opinion is summarised on the following page.

# Our audit opinion

Element of opinion	Basis of our opinion	Conclusions
<p>Financial statements</p> <p>The financial statements provide a true and fair view of the state of affairs of the College and its group at 31 July 2019 and of the deficit for the year then ended</p> <p>The financial statements are prepared in accordance with the financial reporting framework</p>	<p>We report on the outcomes of our audit procedures to respond to our assessed risk of misstatements, including significant risks within this section of our report. We did not identify any areas of material misstatement.</p> <p>We are satisfied that accounting policies are appropriate and estimates are reasonable.</p> <p>We have considered the financial statements against the financial reporting requirements, and additional guidance issued by the SFC and Audit Scotland.</p>	<p>We issued an unqualified audit opinion on the 2018/19 financial statements for North East Scotland College and its group.</p>
<p>Going concern</p> <p>We are required to conclude and report on the appropriateness of the use of the going concern basis of accounting</p>	<p>We conduct core financial statements audit work, including management’s assessment of the appropriateness of the going concern basis.</p> <p>Wider scope procedures, including financial forecasts are considered as part of our work on financial sustainability.</p>	<p>We have no matters to report.</p>
<p>Other information</p> <p>We consider whether the other information in the financial statements is materially inconsistent with other knowledge obtained during the audit</p>	<p>We conduct a range of substantive procedures on the financial statements. Our conclusion draws upon:</p> <ul style="list-style-type: none"> <li>▶ Review of committee minutes and papers, regular discussions with management, our understanding of the College and the sector.</li> </ul>	<p>We are satisfied that the annual report materially meets the core requirements set out in the Accounts Direction.</p>
<p>Report on regularity of income and expenditure</p> <p>We are required to consider whether in all material respects the income and expenditure in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by Scottish Ministers</p>	<p>Our procedures include:</p> <ul style="list-style-type: none"> <li>▶ Understanding the applicable enactments and guidance issued by the Scottish Ministers</li> <li>▶ Performed detailed testing of income and expenditure testing to ensure transactions are in line with enactments and guidance</li> </ul>	<p>We are satisfied that in all material respects income and expenditure are regular.</p>
<p>Matters prescribed by the Auditor General for Scotland</p> <p>Audited part of Remuneration Report has been properly prepared.</p> <p>The Performance Report and Annual Governance Statement are consistent with the financial statements and have been properly prepared.</p>	<p>We are required to report on whether the sections of the Remuneration and Staff report, and Accountability report have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.</p>	<p>We noted a number of disclosure adjustments in relation to the remuneration report. All disclosure adjustments were reflected in the updated financial statements.</p>
<p>Matters on which we are required to report by exception</p>	<p>We are required to report on whether:</p> <ul style="list-style-type: none"> <li>▶ adequate accounting records have not been kept; or</li> <li>▶ the financial statements and the audited part of the Remuneration and Staff Report are not in agreement with the accounting records; or</li> <li>▶ we have not received all the information and explanations we require for our audit</li> </ul>	<p>We have no matters to report.</p>



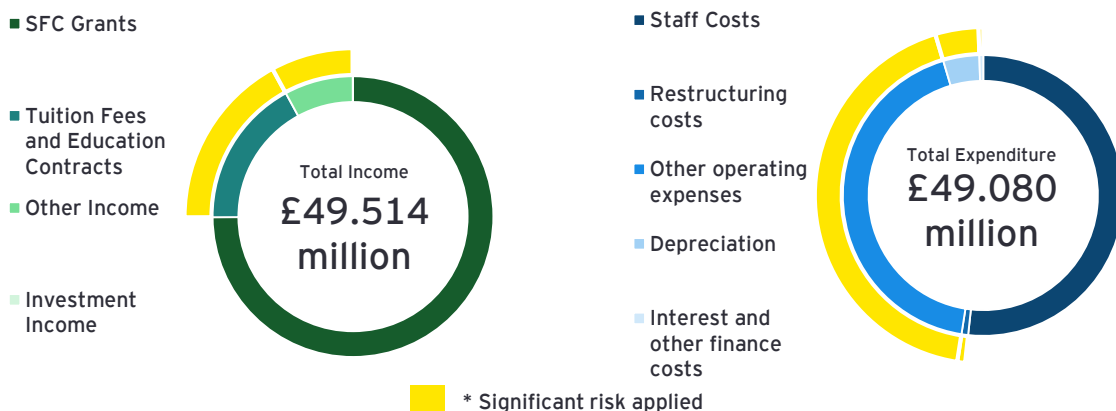
# Significant and fraud audit risks

## 1. Risk of Fraud in Income and Expenditure Recognition

As we outlined in our Annual Audit Plan, ISA (UK) 240 requires us to assume that fraud risk from income recognition is a significant risk. In the public sector, we extend our consideration to the risk of material misstatement by manipulation of expenditure.

In our audit planning, we rebutted the risk of improper recognition of Scottish Funding Council (“SFC”) core grant funding because there is no judgement in respect of this income stream. With regards to expenditure, we rebutted the risk of improper recognition of payroll expenditure (as Practice Note 10 highlights the risk around incorrect recognition of non-pay expenditure). The charts below highlight how our assessment impacts our testing strategy on the College’s financial statements.

Exhibit 1: Key components of the College’s income and expenditure



Source: 2018/19 Financial Statements: Statement of Comprehensive Income and Expenditure

Our testing has not identified any material misstatements relating to revenue and expenditure recognition.

### Specific procedures relating to significant risks

We undertake specific, additional procedures over income and expenditure streams where we identified a significant risk, including:

- ▶ Review and challenge management’s accounting estimates over revenue or expenditure recognition for evidence of bias.
- ▶ Review transaction listings for individually material balances as well as unusual items to agree to supporting documentation and third party evidence.
- ▶ Perform data analytics procedures over significant risk income and expenditure to ensure testing covered all balances in year. This work included data integrity testing and analysis of trends in the data.
- ▶ Review and test all relevant income and expenditure policies against the relevant accounting standards and SORP.
- ▶ Review and test income and expenditure to ensure it is accounted for in the correct financial period.
- ▶ Perform a search for material payments and receipts received after year end and ensured these had been accounted for in the correct period.

## Our Audit of Other Income and Expenditure

We undertook walkthroughs in respect of the processes management has established to account for material income and expenditure streams. We obtained data downloads from the College's financial ledger to allow us to trace key transactions from initiation to recording in the financial statements.

### Other audit procedures: non-significant risk areas:

Our audit work on other areas, where there were no significant risks, identified no audit misstatements. We did not identify any areas of significant estimation or judgement as part of our audit work in these areas.

**Scottish Funding Council income:** We agreed receipts in the year for SFC grant income to the financial ledger and SFC grant award notification. We have assessed the College's compliance with required grant requirements (such as credits achievement) and did not identify any additional clawback of funding which over and above any clawbacks which the College communicated to us.

**Employee expenses:** We performed a reconciliation of the payroll system to the payroll costs per the ledger, investigating and corroborating any material differences. We tested the integrity of the payroll data by recalculating a sample of employees deductions calculations. In addition, we completed starters and leavers testing to gain assurance that the College has robust processes in place around these higher risk transactions.

We have outlined our consideration of the valuation of pension assets and liabilities held by the College later in this report. In respect of all pension transactions impacting the SOCIE we agreed these journals to the underlying FRS 102 report prepared by the College's actuary.

## 2. Risk of Misstatement due to Fraud or Error

Our Annual Audit Plan recognised that under ISA (UK) 240, management is considered to be in a unique position to perpetrate fraud in 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.

### Our audit procedures

We considered the risk of fraud, inquired with management about their assessment of the risks of fraud and the controls 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.

We tested the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.

We obtained a full list of journals posted to the general ledger during the year, and used our bespoke data analysers to identify any unusual journal types or amounts based on our identified risk areas for the audit.

Management disclose their assessment of the critical accounting judgements and key estimates in the financial statements. We reviewed each significant accounting estimate (pension provision and valuation of PPE) for evidence of management bias, including retrospective consideration of management's prior year estimates.

We identified and considered the appropriateness of key accounting estimates, including provisions, and their susceptibility to bias.

Evaluate the business rationale for any significant unusual transactions.

Review of property, plant and equipment expenditure to ensure it fulfils the accounting requirements to be capitalised.

We consider the consistency and application of accounting policies, and the overall presentation of financial information.

### Our findings

We have not identified any material weaknesses in controls or evidence of management override. We wrote to the chair of the Audit and Risk Committee to inquire about any instances of possible non-compliance identified in year. No issues were brought to our attention.

We identified a number of manual journals requiring further consideration using criteria we established based on our understanding of the College. All journals tested were assessed as appropriate and verified to supporting documentation.

We reviewed each estimate and concluded there was no evidence of material bias.

We are also content that the disclosures that management have made in the relevant section of the financial statements are appropriate.

No unusual transactions were identified outside the normal course of business.

We tested minor works revenue expenditure and reconciled this expenditure to the backlog maintenance schedule agreed with SFC. No issues were identified.

There are no accounting practices that materially depart from what is acceptable under the accounting framework.

We have not identified any material weaknesses in controls or evidence of material management override.

We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the College's normal course of business.

# Other Inherent Risk Areas

**Recommendation 1:**  
College should ensure that there is a robust process for the finance team to be aware of all fixed asset additions and disposals at year end.

Our Annual Audit Plan highlighted additional areas of inherent risk. We identified no further areas of risk as part of our audit procedures. The results of our procedures on inherent risk areas are summarised below.

## Valuation of Property Plant and Equipment

The College's property portfolio totals £97.6 million as at 31 July 2019 (2017/18 £97 million), with the major elements of this being in respect of land and buildings. Land and buildings are revalued to fair value with a full revaluation taking place at least every five years with an interim valuation at year 3.

An interim valuation of existing land and buildings was undertaken as at 31 July 2018. The College is required to consider annually the valuation of the College estate remains appropriate outside of formal revaluation cycles.

In addition, the College has recently revised its Capital strategy

### Our audit procedures

- ▶ Analysed the source data and made inquiries as to the procedures used by management's specialist to establish the source data as complete.
- ▶ Reviewed the reasonableness of the assumptions and methods used, including the College's compliance with the SORP.
- ▶ Considered the appropriateness of the timing of when the specialist carried out the valuation work.
- ▶ Reviewed the substance of the specialist's findings to ensure they were properly reflected in the financial statements.
- ▶ Considered the potential for impairment across the College estate that had not been reflected in the financial statements or most recent formal valuation.
- ▶ Verified that the specialist's findings for assets held for resale have been correctly processed in the financial statements through testing of accounting entries.
- ▶ Reviewed the College's backlog maintenance estates plans, including consideration of whether backlog maintenance expenditure in the year had been correctly accounted for as capital or revenue expenditure.

### Our findings

We reviewed the valuation report provided by the specialist for the asset held for sale, challenging the accuracy and appropriateness of this property being held for sale. We agreed the workings to underlying asset information.

We physically verified all material land and buildings, reviewing all assets for signs of impairment.

We assessed management's desktop exercise which considered whether there had been a material change in the valuation of land and buildings since the 2018 interim valuation. The College engaged their valuers to provide a desk top review of land and buildings valuations as at 31 July 2019. This resulted in an audit adjustment of £2.5 million to increase the valuation of land and buildings as at 31 July 2019 to bring the value in line with the valuation report.

We tested minor works revenue expenditure and reconciled this expenditure to the backlog maintenance schedule agreed with SFC. No issues were identified from this work undertaken.

We noted that the College should ensure that there is a robust process for the finance team to be aware of all fixed asset additions and disposals at year end.



## Our audit procedures

### Valuation of Pension Liabilities

The College participates in two pension schemes; the North East Scotland Pension Fund (NESPF), and the Scottish Teachers Superannuation Scheme (STSS).

NESPF is accounted for as a defined benefit scheme. The net pension liabilities on the balance sheet arising from participation in the scheme at 31 July 2019 were £24.2 million (2017/18 £8.2 million).

In addition the College recognises a provision for future early retirement liabilities - £6.8 million as of 31 July 2019 (2017/19 £7.2 million).

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

We have focused on the following areas, which are consistent with those of management:

- ▶ The reasonableness of the underlying assumptions used by the College's actuary, including those associated with recent judgements on McCloud and Guaranteed Minimum Pensions (GMP).
- ▶ Ensuring the information supplied to the actuary in relation to the College was complete and accurate.
- ▶ Ensuring the accounting entries and disclosures made in the financial statements were consistent with the actuary's report.

We have liaised with the appointed auditor of the North East Scotland Pension Fund to obtain assurances over the information supplied to the actuary in relation to the College.

We have assessed the work of the Pension Fund actuary including the assumptions they have used by utilising our in-house experts. We have assessed both the robustness of the methodology used to derive the key actuarial assumptions and the reasonableness and consistency of the assumptions underpinning such reports, using guidance available.

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 assessed the approach taken by the actuary to account for the estimated impact of the recent rulings made around the McCloud judgement and various rulings around GMP.

We reviewed the calculation of the College's early retirement liabilities at 31 July 2019.

## Our findings

We confirmed that the actuarial report had taken into account the McCloud ruling. The actuary disclosed an impact from the McCloud ruling of £0.51 million which was assessed to be within the expected range for the College.

The actuary did not allow for the impact of GMP. Our analysis of the potential impact of this ruling on the College concluded that any impact would not be material to the financial statements.

In calculating the scheme assets as at 31 July 2019 the actuary performs a roll forward technique using investment returns and cash flow data since the last triennial valuation. We have considered the reasonableness of the reported asset position and note that the actuary's estimated investment returns were consistent with actual investment returns for North East Scotland Pension Fund.

Assumptions used by the actuary and adopted by the College are considered to be generally acceptable. The sensitivities surrounding these assumptions have been correctly disclosed in the notes to the financial statements.

No material misstatements were identified relating to the valuation of pension liabilities for the work outlined above.

# Looking ahead


## **Updated Statement of Recommended practice: accounting for further and higher education 2019 edition**

The Statement of Recommended Practice (SORP): accounting for further and higher education has been updated to reflect the amendments made to FRS 102 following its triennial review in 2017. The revised SORP will be effective for financial periods beginning on or after 1 January 2019 and therefore will be applied by the College within their 2019/20 financial statements.

The triennial review was published by the Financial Reporting Council in December 2017. The majority of amendments were editorial in nature and clarified rather than changed accounting treatment. The amendments to the SORP follow a similar basis and it is not therefore anticipated that the College will be required to adopt substantive changes to accounting treatments. We do, however, anticipate that the College will be required to adopt a number of changes to disclosure requirements.

We will work with management during 2019/20 to ensure the correct application of the new requirements.

**Recommendation 2:**  
The College should conduct an impact assessment on the implementation of the revised SORP.



# Wider Scope Dimensions

## **Introduction**

Under Audit Scotland's Code of Audit Practice (May 2016), we are required to reach conclusions in relation to the effectiveness and appropriateness of the College's arrangements for each of the wider scope audit dimensions. We apply our professional judgement to risk assess and focus our work on each of the dimensions.

## **The Wider Scope dimensions**

Financial Sustainability:

- ▶ considers the medium and longer term outlook to determine if planning is effective to support service delivery. This will focus on the arrangements to develop viable and sustainable financial plans.

Financial Management:

- ▶ considers the effectiveness of financial management arrangements, including the adequacy of financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Governance and Transparency:

- ▶ considers the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

Value for Money:

- ▶ considers whether best value can be demonstrated in the use of resources, including the extent to which there is an alignment between spend, outputs and outcomes delivered and that there is a clear focus on improvement.

# Financial Sustainability

The College has undertaken a thorough process to develop the Financial Forecast Return including scenario planning review and challenge of key assumptions. In addition, the College has used these forecasts to develop a Financial Plan for the period 2019-2024. This plan was approved by the Regional Board in June 2019.

While the College can demonstrate that plans are in place to deliver a financially sustainable future, there are significant external risks that may continue to impact the financial planning and sustainability of the College.

A  
M  
B  
E  
R

## **The context for financial sustainability in the FE sector**

In June 2019, Audit Scotland published their annual report on the further education sector, *Scotland's Colleges 2019*. The report provides an overview of college finances based on the latest annual financial statements and financial forecast returns. The sector reported an improved, but marginal underlying surplus in 2017/18 but the report notes a widening gap between college's income and expenditure. Twelve incorporated colleges currently forecast recurring financial deficits by 2022/23.

Scottish Government revenue funding to the sector has increased year on year since 2016/17 in real terms, but this increase has solely related to funding the costs of harmonising staff terms and conditions. This means that there has been no additional funding for cost pressures such as cost of living increases and increases in employer pension contributions.

The Scottish Funding Council's 2017 estates condition survey indicates that college buildings require urgent and significant investment. Reduced capital funding poses a risk to some colleges' ability to continue to deliver their core services in a safe environment and to invest in new technologies to generate efficiencies and enhance the student experience.

## **Medium term financial strategy and plan**

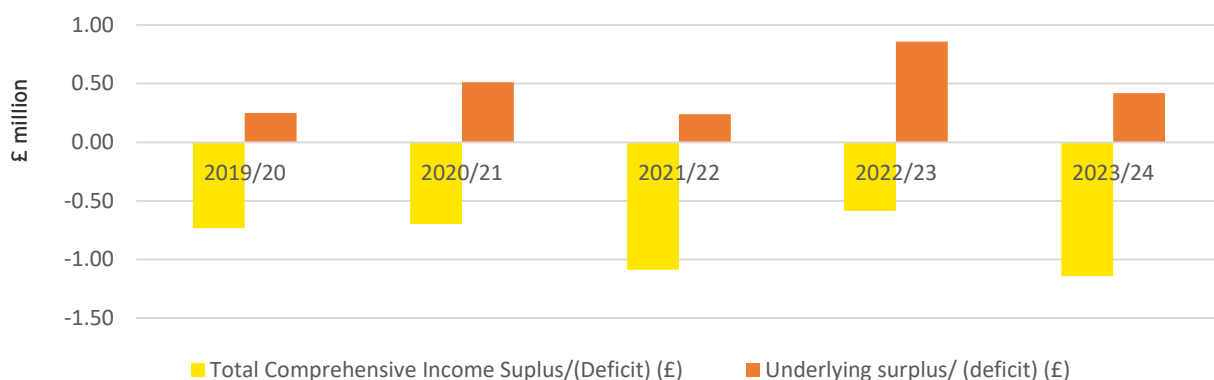
A Financial Plan covering the period 2019-2024 was presented and approved by the Regional Board in June 2019. The basis of this financial plan was the underlying work and consideration of the five-year financial forecasts prepared in the form of the template Financial Forecast Return (FFR) required by the SFC.

The forecast is based on assumptions provided by the SFC in addition to College specific assumptions for areas such as other income and staff numbers. The assumptions have been subject to scrutiny by the College's senior management, Finance & Resources Committee and the Board. The College performed scenario planning for six different scenarios as part of the development of the financial forecasts.

The forecasts have been prepared on the basis of the Board's strategic plans and supporting aims and objectives. This includes direct linkages to how the financial forecasts will support the College in achieving targets outlined within the College's strategies and plans.



**Exhibit 2: The College's FFR highlights that the College is forecasting an accounting deficit for the next 5 years, with a modest underlying surplus for all years. The difference between the comprehensive income position and the underlying position is attributed to net depreciation and planned donations to the North East Scotland Further Education Foundation.**



Source: North East Scotland College Financial Forecast Return, October 2019

### Key Assumptions

The Scottish Funding Council issued guidance on the assumptions and information required from Colleges in June 2019. The guidance is developed in conjunction with sector representatives to provide guidance on key assumptions to be applied in the Financial Forecast Return to ensure that the SFC can understand the financial health of the sector as a whole.

Key FFR assumptions provided by the SFC include:

- ▶ SFC recurrent grant is based on indicative funding allocations provided by the SFC alongside the College's assessment of the additional costs associated with the increase in STSS pension contributions. Additionally, the SFC has assumed that there are no plans to revise activity targets prior to 2022/23 when there will be a 3.1% activity reduction for the College.
- ▶ Capital maintenance funding should be based on the final 2019/20 allocations.
- ▶ The impact of national bargaining harmonisation/job evaluation costs should be included based on data from Colleges Scotland and cost of living pay award increases should be included. The Public Sector Pay Policy should be applied.

The College's local analysis is based on internal assumptions including:

- ▶ Student numbers have been forecast to remain stable throughout.
- ▶ The College continuing to deliver commercial courses to employers responding to the need across the Region, however, no expectation of an increase of this commercial income built into the plans due to the extended downturn in the oil and gas industry.
- ▶ Staff numbers are expected to remain relatively stable within the requirements of the curriculum plan.
- ▶ For non-staff costs, the College has assumed they will make small efficiencies through procurement and control of utilities.

While we have concluded that the College's approach to financial planning is robust, a number of the most significant variables are outwith the College's control and therefore continue to present a risk that the College may be unable to deliver their FFR.

### Key risks and uncertainties

The College has identified the 6 most significant risks that may impact the delivery of the FFR (Exhibit 3 below). Other risks are likely to include future potential pay increases, and the management of significant sources of other income.

### Exhibit 3: The College has identified 6 key risks that pose a risk to the College's ability to achieve their financial forecast return and thus impacting their ability to be sustainable in the medium term

Description	Risk mitigating actions
The increased costs of pay as a result of national bargaining and pay harmonisation present a significant risk to the College, as negotiated settlements are largely outwith its control.	The College will include all known costs and funding as and when they are advised and will seek to implement efficient delivery models across all its functions.
The College has a demonstrable need to address significant deficits in its estate but has not been able to agree a funding package to meet this. The result is that the estate will become increasingly unfit for purpose.	The College has approved a new Estates Strategy for the period 2019-2029, and will continue to address high priority areas and maintain estates to the best of its ability. It will continue to discuss options for funding with SFC.
Full utilisation of the Flexible Workforce Development Fund (FWDF) has proved a challenge for the College, although it has met its target overall.	The College continues to work with the business community to utilise the funding available. The increase to the upper limit is expected to be beneficial.
Commercial trading remains difficult in the North East and the College does not expect opportunities for this to improve greatly in the near future.	The College continues to promote commercial opportunities and use the FWDF as a means to initiate discussions with business.
Delivery of Foundation Apprenticeships remain challenging with a risk that the College may not meet SDS targets.	Engagement with stakeholders, effective marketing and promotion of benefits will assist in meeting targets.
The College negotiated a 3000 credit reduction in its allocation for 2018/19 and this continues to be an area of concern.	The College is closely monitoring its recruitment and retention and is preparing a longer term plan for the size and shape of its curriculum offer.

Source: North East Scotland College FFR October 2019

# Financial Management

We were satisfied that financial reporting was clear and consistent throughout the year. The College reported a consolidated surplus for the year of £0.54 million before actuarial losses in respect of pension schemes and unrealised surplus on the revaluation of land and buildings and the asset held for resale. This resulted in a total comprehensive deficit for the year of £13.048 million. The College has an operating surplus after removal of non-cash accounting adjustments of £2.33 million.

Financial performance is scrutinised by the senior executive team, the Finance and Resources Committee and the Board. This monitoring includes expenditure against budget and the forecast outturn for the year.

## Financial Monitoring

The College's 2018/19 budget was approved in June 2018 with the College budgeting for a deficit for the year of £0.5 million. Despite a challenging financial operating environment, the College's financial performance was slightly better than expected, with the College reporting a consolidated surplus for the year of £0.5 million.

Financial updates are presented regularly at meetings of the Finance and Resources Committee with periodic updates also presented to the Board. We reviewed financial updates presented during the year and evaluated the quality and quantity of content provided. Members are provided with the following key information which we consider to support members in appropriately scrutinising financial performance:

- annual and year to date budget figures;
- period forecast and actual performance;
- budget variances as both a number and percentage; and
- explanations to support significant budget movements.

## Financial Performance

The College reported a consolidated surplus of £0.5 million for the year (2017/18: £4 million deficit). Following an actuarial loss of £15.7 million and an unrealised gain on revaluation of land and buildings and assets held for resale of £2.08 million, the College reported total comprehensive deficit of £13 million (2017/18: £15 million income). The College had an operating surplus after removal of non-cash accounting adjustments (relating to pension and depreciation adjustments) of £2.3 million (2017/18: £1.3m deficit).

An activity target of 132,530 credits was allocated to the College from the SFC which the College fell short of this by 0.23% (306 credits). The College has accrued for a clawback of £65,000 as a result of this shortfall in credits.

### **Prior Year recommendation Follow up**

We have reviewed the College's actions in response to prior year recommendations in Appendix E. In 2017/18, we noted that the College was yet to develop a multi-year plan to address its backlog maintenance, following the condition survey conducted by the SFC. An Estates Strategy has been agreed and approved by the Board in June 2019, with the final version of the strategy available on the College's website. Addressing the backlog maintenance for all campuses is a key deliverable in the Estates Strategy. In addition, we obtained and reviewed the backlog maintenance funding return submitted to the SFC.

In 2017/18, we also noted that the College should assess the potential impact of EU Withdrawal on their organisation, identifying any specific risks and how they plan to respond to them in line with Audit Scotland guidance. The College has created a Brexit action plan, based on a checklist created by the SFC which covers a range of potential issues related to Brexit. This action log is regularly reviewed by the Regional Board.

See Appendix E for further detail on prior year recommendation follow up.

### **Systems of internal control**

Within the annual governance statement, the College has concluded that they have obtained reasonable assurance that the system of internal control was operating effectively during the year with no exceptions or issues identified.

Through our audit of the financial statements, we have tested the design and implementation of key controls related to areas of significant risk to the financial statements. This work has included documenting the key internal financial controls and performing walkthroughs to ensure controls are operating as designed. Based on the work undertaken, our work has not identified any significant weaknesses in the College's systems of internal control.

### **National Fraud Initiative (NFI)**

NFI is a counter-fraud exercise co-ordinated by Audit Scotland and overseen by the Cabinet Office to identify fraud and error. The NFI exercise produces data matches by comparing a range of information held on public bodies' systems to identify potential fraud or error.

We submitted an assessment of the College's participation in the exercise to Audit Scotland in June 2019. We concluded that the College has actively participated in the NFI exercise and that it is well embedded within the College's Policy and Response Plan.



# Governance and Transparency

The key features of good governance are in place and operating effectively. We concluded that the Governance Statement materially complies with the SFC's 2018/19 Accounts Direction.

The College's Audit and Risk Committee has an independent chair. Standing Orders regulate how the business of the College is conducted, and detailed terms of reference are in place for the Board's standing committees. The College continues to embed its risk management arrangements, with an established risk management policy updated during the year.

We noted that the College should publish Audit and Risk Committee minutes on the website in line with best practice.

## Recommendation 3:

The College should ensure Audit and Risk Committee agendas and minutes are published on their website.

We concluded that the Annual Governance Statement meets the requirements of the Accounts Direction and is consistent with our knowledge of the College.

The College has not identified any areas of non-compliance with the Code of Good Governance.

## Governance arrangements

The College has in place the key requirements for good governance. We consider the following to be examples of good governance:

- ▶ The Board and committee minutes and set out clearly the matters considered and discussed.
- ▶ The Board has approved detailed terms of reference for its standing committees which are subject to regular review.
- ▶ The College publishes Board and the majority of its standing committee agendas, minutes and papers on their website in a timely manner and information, including financial performance, is generally clear and concise.
- ▶ However, we noted that the Audit and Risk Committee agendas, minutes and papers are not currently published on the College's website.

## Annual Governance Statement

We reviewed the Governance Statement within the financial statements against the requirements outlined in the SFC's 2018/19 Accounts Direction. This includes the requirements to conclude on the College's compliance with the 2016 Code of Good Governance for Scotland's Colleges, or to explain any areas of non-compliance. Our consideration of the governance statement has included:

- ▶ Ensuring that the College has met all requirements of the SFC's 2018/19 Accounts Direction.
- ▶ Ensuring that the content of the statement is consistent with our understanding of the College's governance arrangements and any issues identified during the year.
- ▶ Ensuring that the College has performed a self-assessment of compliance with the Code of Good Governance for Scotland's Colleges and that this assessment is reflected in the Statement.
- ▶ While the final financial statements are materially compliant with the requirements, there are areas where the Governance Statement, and other disclosures, can be further enhanced to improve the readability to users.

## **Risk management**

The College's approach to risk management is set out within the risk management policy. This was formally approved in September 2019. Once a month the Senior Executive Team meets and assess the strategic risk register, to ascertain the completeness of the risks to ensure it is reflecting the current situation in the College. Matters are referred to standing committees, as appropriate. The Audit and Risk Committee reviews the risk register on a quarterly basis. The Board are also advised of new risks or changes to risks assigned to them in the Strategic Risk Register and reviews this at least annually.

## **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. Internal audit's opinion for the year was based on its agreed audit plan for the year, as approved by the Audit and Risk Committee. For 2018/19 the Internal Auditor's annual statement of assurance notes "In our opinion North East Scotland College did have adequate and effective risk management, control and governance processes to manage its achievement of the College's objectives at the time of our audit work. In our opinion, the College has proper arrangements to promote and secure value for money. We have however raised a weak level of assurance around the Fixed Asset Management arrangements in place which should be followed up during the follow up review for 2019/20."

## **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. At present, national reports are reviewed by management and the impact on the College is considered. These will be presented to the Board or relevant committee where necessary.

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.

## **Enquiries of those charged with governance**

During 2018/19, we formally wrote to the Chair of the Audit and Risk 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. No matters were brought to our attention.

## **Register of Interests**

It is a College requirement that all Board members and the senior executive team complete a register of interests declaration at least annually (or when circumstances change). We confirmed that Board members are asked to review and update their declarations of interest at least twice a year. Registers of interests are then updated and published on the College's website. In addition, declarations of potential conflicts of interest are a standing item on meeting agendas.

## EU withdrawal

While risks remain for all public sector bodies, we are satisfied that the College's arrangements to prepare for EU withdrawal are appropriate and informed by wider sector involvement.

As in 2017/18, Audit Scotland has maintained an interest in public bodies' preparedness for EU withdrawal. We assessed the College's preparedness and consideration of Brexit as part of the audit.

The College has created a Brexit action plan, based on a checklist created by the SFC which covers a range of potential issues related to Brexit. The College has assessed that key impact areas include:

- ▶ Supply chain;
- ▶ Staff members from the EU;
- ▶ Students from the EU;
- ▶ EU funding

This action log is regularly reviewed by the Regional Board.

# Value for Money

A revised strategic plan was introduced from the start of the 2018/19 academic year. Developed by the Board with input from staff, students and stakeholders. The plan identifies the key strategic priorities over the period 2018-21.

There is clear and timely reporting against performance indicators. Annual performance reports are published on the College's website.

The College has an appropriate framework in relation to procurement. We noted that the College should develop an overarching policy for voluntary severance schemes in line with best practice.

## Strategic Plan 2018-21

A revised strategic plan was introduced from the start of the 2018/19 academic year. Developed by the Board with input from staff, students and stakeholders, the plan identifies the key strategic priorities for the College over the period 2018-21. It sets a clear direction for the College in responding to the needs of the region and in delivering on national policy.

The strategic plan notes five strategic themes:

- ▶ Being Responsive
- ▶ Developing People
- ▶ Working in Partnership
- ▶ Delivering Quality
- ▶ Building Sustainability

Each strategic theme has accompanying objectives and strategies to support achievement. The College will monitor their progress using the key strategic indicators identified and a table of progress against these indicators will be published annually.

## Performance reporting

The College publishes its performance information annually on its website as well as including key measures within the financial statements and Board and committee papers published on the website. The Evaluative Report and Enhancement Plan and a performance report showing key financial information and performance indicators are also presented to the Board.

## Voluntary Severance Policy

We noted through discussions with management and through prior year audit work that the College has a governance process in place for the approval of exit packages. This includes approval of the severance scheme by the Board. Once a scheme is approved, a policy would be developed for that specific severance scheme.

However, we noted that there is not currently an overarching voluntary severance policy at the College, which outlines the process any severance scheme should follow.

### Recommendation 4:

The College should document an overarching severance scheme policy which outlines the governance process for the approval of exit arrangements. This should outline the process to be followed for any severance scheme considered by the College.



### **Procurement processes**

The College has a procurement strategy, developed for the period 2016-2020. The strategy has been designed to ensure legislative compliance with the Procurement Reform (Scotland) Act 2014 and other relevant legislation. It is aligned with both the College's and the SFC's key strategic outcomes. A copy of the strategy is available on the College website.

The College utilises the procurement software PECOS. All purchases must be approved, with tiered levels of approval, depending on value. The Finance and Resources Committee review procurements for contracts above £50,000, as well as any retentions for contracts above this threshold. Based on the scope of our work, we have concluded that there is appropriate framework in relation to procurement.



# Appendices

A - Code of Audit Practice: responsibilities

B - Independence and audit quality

C - Required communications with the Audit and Risk Committee

D - Action plan

E - Follow up of prior year recommendations

F - Adjusted errors identified during the audit

G - Unadjusted errors identified during the audit

H - Timing and deliverables of the audit

# Appendix A: Code of Audit Practice Responsibilities

## Audited Body's Responsibilities

### Corporate Governance

Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.

### Financial Statements and related reports

Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:

- ▶ preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation.
- ▶ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.
- ▶ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.
- ▶ maintaining proper accounting records.
- ▶ preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body.

Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.

Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.

### Standards of conduct / prevention and detection of fraud and error

Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.

### Standards of conduct / prevention and detection of fraud and error

Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- ▶ such financial monitoring and reporting arrangements as may be specified
- ▶ compliance with any statutory financial requirements and achievement of financial targets
- ▶ balances and reserves, including strategies about levels and their future use
- ▶ how they plan to deal with uncertainty in the medium and longer term
- ▶ the impact of planned future policies and foreseeable developments on their financial position.

### Best Value

The Scottish Public Finance Manual sets out that accountable officers appointed by the Principal Accountable Officer for the Scottish Administration have a specific responsibility to ensure that arrangements have been made to secure best value.

# Appendix 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.

## Matters that 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 2018 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 10 July 2019.

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

	2018/19	2017/18
<b>Component of fee:</b>		
<b>Total agreed auditor remuneration</b>	<b>£32,030</b>	£31,300
Fee variation in respect of wider scope focus areas	-	-
<b>Audit Scotland fixed charges:</b>		
Pooled costs	<b>£1,840</b>	£2,010
Audit support costs	<b>£1,940</b>	£1,740
<b>Total fee</b>	<b>£35,810</b>	£35,050

As outlined in our Annual Audit Plan we anticipated additional audit work required around the implications of a High Court ruling on Guaranteed Minimum Pensions and the McCloud judgement. We have also undertaken additional procedures to gain assurance over the valuation of the College's PPE. We are in the process of quantifying the additional work required in these areas and agreeing the fee variation with management based on the agreed Audit Scotland day rates for fees. We will report the finalised fee as part of our 2019/20 Audit Planning Report.

Matters that we are required to communicate

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 2019 UK Transparency Report, can be accessed on our website at [https://www.ey.com/Publication/vwLUAssets/ey-uk-2019-transparency-report/\\$FILE/ey-uk-2019-transparency-report.pdf](https://www.ey.com/Publication/vwLUAssets/ey-uk-2019-transparency-report/$FILE/ey-uk-2019-transparency-report.pdf). The report explains 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 (AQB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AQB meets monthly and also holds an annual strategy session. The AQB reports to the EY UK Board. The AQB 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 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 since appointment can be found at: [www.audit-scotland.gov.uk/uploads/docs/report/2018/as\\_audit\\_quality\\_1718.pdf](http://www.audit-scotland.gov.uk/uploads/docs/report/2018/as_audit_quality_1718.pdf).



# Appendix C: Required Communications

Required communication	Our reporting to you
<p><b>Terms of engagement / Our responsibilities</b></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><b>Planning and audit approach</b></p> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>	<p>Annual Audit Plan</p>
<p><b>Significant findings from the audit</b></p> <ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	<p>Annual Audit Plan</p> <p>Annual Audit Report</p>
<p><b>Going concern</b></p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	<p>Annual Audit Report</p>
<p><b>Misstatements</b></p> <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ Corrected misstatements that are significant</li> <li>▶ Material misstatements corrected by management</li> </ul>	<p>Annual Audit Report - See appendices F and G</p>
<p><b>Fraud</b></p> <ul style="list-style-type: none"> <li>▶ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	<p>Annual Audit Report or as occurring if material.</p>
<p><b>Consideration of laws and regulations</b></p> <ul style="list-style-type: none"> <li>▶ 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</li> <li>▶ Enquiry of the Audit 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 Committee may be aware of</li> </ul>	<p>Annual Audit Report or as occurring if material.</p>

## Required communication

## Our reporting to you

### Related parties

Significant matters arising during the audit in connection with the entity's related parties including, when applicable:

- ▶ 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 entity

No significant matters have been identified.

### Independence

Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence

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

- ▶ The principal threats
- ▶ Safeguards adopted and their effectiveness
- ▶ An overall assessment of threats and safeguards
- ▶ Information about the general policies and process within the firm to maintain objectivity and independence

Annual Audit Plan

This Annual Audit Report - Appendix B

### Internal controls

Significant deficiencies in internal controls identified during the audit

This Annual Audit Report - no significant deficiencies reported

### Group audits

- ▶ An overview of the type of work to be performed on the financial information of the components
- ▶ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components
- ▶ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work
- ▶ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted
- ▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements

Annual Audit Plan

This Annual Audit Report

### Subsequent events

Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.

We have asked management and those charged with governance. We have no matters to report.

### Material inconsistencies

Material inconsistencies or misstatements of fact identified in other information which management has refused to revise

This Annual Audit Report

# Appendix D: Action Plan

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the 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><b>Fixed Assets - Additions and Disposals Process</b></p> <p>We noted through our work over fixed assets that there is an element of reliance on the budget holders to inform the finance team of any disposals that have taken place or are due to take place throughout the year.</p> <p>We noted that the process to identify additions throughout the year and at year end is not documented in a way that audit can review in a robust way.</p>	<p>The College should ensure that there is a robust process for the finance team to be aware of all fixed asset additions and disposals at year end.</p> <p>This could include developing formal process (e.g. form) for all area managers to complete at year end so that the finance team is aware of all disposals processed in different locations.</p> <p>In addition, any work that the finance team completes for consideration of additions should be documented so that audit can complete a review of this process.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed.</p> <p>This was already identified by internal audit in 2018-19 and an updated procedure has been drafted.</p> <p><b>Responsible officer:</b> Head of Facilities and Estates</p> <p><b>Implementation date:</b> January 2020</p>
2	<p><b>New SORP</b></p> <p>The SORP will be revised with effect from 2019/20.</p>	<p>The College should perform a formal impact assessment on the application of the revised SORP in 2019/20.</p> <p style="text-align: right;"><i>Grade 3</i></p>	<p>Agreed.</p> <p>An impact assessment will be undertaken in conjunction with guidance from SFC and Colleges Scotland.</p> <p><b>Responsible officer:</b> Financial Controller - External Affairs</p> <p><b>Implementation date:</b> July 2020</p>
3	<p><b>Availability of Minutes</b></p> <p>Audit and Risk Committee agendas and minutes should be available online in line with best practice for governance and transparency, however, this is not currently in place at the College. Discussions with management noted that this gap had previously been identified but had not yet been actioned.</p>	<p>The College should ensure that all Audit and Risk Committee agendas and minutes are available online in line with best practice for governance and transparency arrangements.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed.</p> <p>Agendas and minutes will be published on the website.</p> <p><b>Responsible officer:</b> Director of Strategy and Planning</p> <p><b>Implementation date:</b> December 2019</p>

# Appendix D: Action Plan (cont.)

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
4	<p><b>Overarching VSER Policy</b></p> <p>We noted through discussions with management and through prior year audit work that the College has a governance process in place for the approval of exit packages. This includes approval of the severance scheme by the Board. A policy will be developed for a specific severance scheme identified.</p> <p>However, we noted that there is not currently an overarching voluntary severance policy in place at the College, which outlines the process any severance scheme should follow.</p>	<p>The College should document an overarching severance scheme policy which outlines the governance process for the approval of exit arrangements. This should outline the process to be followed for any severance scheme considered by the College.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed.</p> <p>Director of HR and OD was aware of this and it was included as part of the Policy Review schedule with a new policy to be considered by the HR Committee in April 2020.</p> <p><b>Responsible officer:</b> Director of HR and OD</p> <p><b>Implementation date:</b> April 2020</p>

# Appendix E: Follow up of prior year recommendations

This section of our report summarises our assessment of the College's progress against the recommendations that we identified during our 2017/18 audit.

Prior year recommendations			
No.	Recommendation / grading	Management response/ Implementation timeframe	Our assessment of progress
1	<p>Management should review its financial statement preparation arrangements. Particular focus should be given to:</p> <ul style="list-style-type: none"> <li>▶ Ensuring preparation of the financial statements is assigned to appropriate individuals.</li> <li>▶ Ensuring sufficient time is built into the financial statement process to allow multiple levels of detailed review and subsequent updated versions of financial statements</li> <li>▶ Ensuring preparation is completed in line with applicable guidance, ensuring changes in requirements are addressed on a timely basis.</li> <li>▶ Revising the performance report to provide enhanced clarity and greater insight into the performance of the College, linking to the new strategic plan.</li> <li>▶ Enhancing the presentation and structure of the financial statements to improve the readability to users.</li> </ul> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed. The College's new Strategic Plan, which clearly links to national and regional priorities provides a clear basis for performance reporting.</p> <p>While the College has utilised a consistent format of report over recent years, we will ensure that further changes as required by the SFC Accounts Direction are incorporated in future years.</p>	<p>As part of the audit process, we identified a number of disclosure and presentation changes requiring attention by management.</p> <p>While the final financial statements are materially compliant with the requirements, there are areas where the Governance Statement, and other disclosures, can be further enhanced to improve the readability to users.</p> <p><b>Audit Assessment: we recognise that progress has been made by management in a number of areas. However, this recommendation remains open due to the similar points being raised in 2018/19 specifically in relation to the improvement in the readability to the users.</b></p> <p><b>2018/19 Management Response:</b></p> <p>The College will undertake a further review of the content and format of the Performance Report and Governance Statement to consider whether changes should be made to improve readability.</p> <p><b>Responsible officer:</b> Vice Principal - Finance and Resources</p> <p><b>Implementation date:</b> March 2020</p>

# Appendix E: Follow up of prior year recommendations (cont.)

This section of our report summarises our assessment of the College's progress against the recommendations that we identified during our 2017/18 audit.

Prior year recommendations			
No.	Recommendation / grading	Management response/ Implementation timeframe	Our assessment of progress
2	<p>In line with Audit Scotland guidance, the College should assess the potential impact of EU Withdrawal on their organisation, identifying any specific risks and how they plan to respond to them.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed. This has already been considered by the Senior Management Team and will be added to the Corporate Risk Register, with mitigating actions included.</p>	<p>The College has created a Brexit action plan, based on a checklist created by the SFC. This checklist covers a range of potential issues related to Brexit.</p> <p>The College has assessed that key impact areas include:</p> <ul style="list-style-type: none"> <li>• Supply chain</li> <li>• Staff members from the EU</li> <li>• Students from the Eu</li> <li>• Funding</li> </ul> <p>This action log is regularly reviewed and considered by the Regional Board.</p> <p><b>Audit Assessment: closed</b></p>
3	<p>The College requires to develop and approve a backlog maintenance plan.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed. This will be included as part of the development of the new Estates Strategy, to be completed by summer 2019.</p>	<p>The Estates Strategy was approved by the Regional Board in June 2019 with the caveat of specific figures being finalised. This has now been actioned and a finalised Estates Strategy has been made available on the College website.</p> <p>Addressing the backlog maintenance for all campuses is a key deliverable in the Estates Strategy.</p> <p>In addition, we obtained and reviewed the backlog maintenance funding return submitted to the SFC.</p> <p><b>Audit Assessment: closed</b></p>



# Appendix E: Follow up of prior year recommendations (cont.)

This section of our report summarises our assessment of the College's progress against the recommendations that we identified during our 2017/18 audit.

Prior year recommendations			
No.	Recommendation / grading	Management response/ Implementation timeframe	Our assessment of progress
4	<p>The College needs to develop a medium-term financial plan to address forecast underlying deficits to support the College's financial sustainability.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>The College's financial plans have been prepared in line with SFC direction to fully utilise the resource available to it, including the Cash Budget for Priorities. Have said that, we acknowledge that this leaves little flexibility to meet unforeseen circumstances and management intends to create flexible headroom in future years to allow for innovation and emerging issues.</p>	<p>A Financial Plan covering the period 2019-2024 was presented and approved by the Regional Board in June 2019. The basis of this financial plan was the underlying work and consideration of the five-year financial forecasts prepared in the form of the template Financial Forecast Return (FFR) required by the SFC.</p> <p>See further detail at Financial Sustainability section of report.</p> <p><b>Audit Assessment: closed</b></p>

# Appendix F: Adjusted errors identified during the audit

This appendix sets out the significant adjustments processed in the financial statements finalisation. There were no significant unadjusted audit differences identified.

Adjusted differences				
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Adjustment relating to job evaluation funding for 2018/19 confirmed by SFC resulting in both income and expenditure being accrued (nil overall impact)</i>	Cr SFC Grant in Aid £591,317		Dr Accrued Income £591,317
		Dr Payroll expenditure (Admin salaries, superannuation & NI) £591,317		Cr Other Accruals £591,317
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
2	<i>Adjustment relating to the increase in land and buildings valuation as a result of the valuers desk top exercise as at 31 July 2019</i>			Dr Fixed Assets £2,530,000
			Cr Unrealised surplus of revaluation of land and buildings £2,530,000	

# Appendix G: Unadjusted errors identified during the audit

This appendix sets out the unadjusted errors identified which were over the reporting threshold. There were no significant unadjusted audit differences identified. We concur with management's view that the differences are not material and we do not consider these to require adjustment.

Adjusted differences				
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Projected error identified from accruals testing (value of error identified from sample testing totalled £304.06 which related to costs associated to post year end)</i>	Cr Expenditure £59,195		Dr Accrued expenses £59,195

# Appendix H: Timing and deliverables of the audit

We deliver our audit in accordance with the timeline set by the College, in accordance with guidance from Audit Scotland. Below is a timetable showing the key stages of the audit and the deliverables through the 2018/19 audit cycle.

	Audit Activity	Deliverable	Timing
MAR			
APR	➤ Review of current issues impacting the College throughout the audit process	Periodic current issues return submission	22 March 2019 8 November 2019
MAY	➤ Audit planning and setting scope and strategy for the 2018/19 audit	Annual audit plan	May 2019
JUNE			
AUG	➤ Walkthrough visit	Completion of internal documentation	1 July 2019
SEPT	➤ Review progress of the NFI exercise	Submit NFI questionnaire	30 July 2019
OCT	➤ Year-end substantive audit fieldwork on unaudited financial statements	Audited financial statements	October 2019
NOV	➤ Conclude on results of audit procedures and finalise Annual Audit Report	Issue Annual Audit Report	31 December 2019
DEC	➤ Issue opinion on the College's financial statements	Submit Audit Scotland Minimum dataset request	

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