Annual Audit Report

to the Board of Management and the Auditor General for Scotland
West College Scotland
Year ended 31 July 2019

MAZARS

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

Mazars LLP
100 Queen Street
Glasgow
G1 3DN

The Joint Audit and Finance & General Purposes Committee
West College Scotland
Paisley Campus
Renfrew Road
Paisley
PA3 4DR

19 November 2019

Dear Members

Annual Audit Report – Year ended 31 July 2019

We are pleased to present our Annual Audit Report for the year ended 31 July 2019. The purpose of this document is to summarise our audit conclusions.

The scope of our work, including identified significant audit risks and other areas of management judgement, was outlined in our Audit Strategy Memorandum which we presented on 23 May 2019. We have reviewed our Audit Strategy Memorandum and concluded that the original significant audit risks and other areas of management judgement remain appropriate.

We would like to express our thanks for the assistance of the finance team during our audit.

If you would like to discuss any matters in more detail then please do not hesitate to contact me.

Yours faithfully

Lucy Nutley
Mazars LLP

1. EXECUTIVE SUMMARY

Purpose of this report and principal conclusions

This Annual Audit Report sets out the findings from our audit of West College Scotland ('the College') for the year ended 31 July 2019, and forms the basis for discussion at the Joint Audit and Finance & General Purpose Committee meeting on 19 November 2019.

Our responsibilities are defined by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice ('the Code') issued by Audit Scotland. Subject to the satisfactory completion of the outstanding work, at the time of issuing this report we have the following conclusions:

Opinion on the financial statements

We have issued an unqualified opinion, without modification, on the financial statements on 10 December 2019.

Opinion on regularity

We have issued an unqualified regularity opinion on 10 December 2019, meaning that in our opinion, in all material respects the expenditure and income recognised in the financial statements have been applied for the purposes intended.

Opinion on other requirements

We have issued an unqualified opinion on the matters prescribed by the Auditor General for Scotland on 10 December 2019. Namely that the remuneration and staff report, performance report and governance statement have been properly prepared in accordance with the relevant legislation.

Wider scope work

We have concluded as follows against each of the four wider scope dimensions. The College has:

- effective arrangements, including budgetary control, that help the Board members scrutinise finances;
- adequate financial planning arrangements in place. A long-term operational funding gap was previously identified by the College as well as a need for significant capital investment to maintain building standards and therefore ensure continued revenue income based on student numbers. There has been no development in obtaining capital investment funding during the year and the risk of reduced performance as a result of a deteriorating estate remains;
- governance arrangements in place that provide appropriate scrutiny of decisions made by the Board; and
- an effective performance management framework in place that supports progress towards the achievement of value for money.

Misstatements and internal control recommendations

Section 3 sets out the internal control recommendations that we make, together with an update on any prior year recommendations.

Section 4 outlines the misstatements noted as part of our audit as at the time of issuing this report. If any additional misstatements are noted on completion of the outstanding work, these will be reported to the Joint Audit and Finance & General Purpose Committee in a follow-up letter.

1. EXECUTIVE SUMMARY (CONTINUED)

Adding value through the audit

We recognise that all of our clients want us to provide a positive contribution to meeting their ever-changing business needs. Our aim is to add value to West College Scotland through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way we aim to help the College promote improved standards of governance, better management and decision making and more effective use of limited financial resources.

Status of our audit work

We have completed our work on the financial statements and wider scope work for the year ended 31 July 2019.

Our audit approach

We provided details of our intended audit approach in our Audit Strategy Memorandum in May 2019. We have not made any changes to our audit approach since we presented our Audit Strategy Memorandum.

1. EXECUTIVE SUMMARY (CONTINUED)

Materiality

Materiality is an expression of the relative significance or importance of a particular matter in the context of financial statements as a whole. Misstatements in financial statements are considered to be material if they, individually or in aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

We set materiality at the planning stage of the audit at £1,157k using a benchmark (2%) of Total Revenues. Our final assessment of materiality, based on the final financial statements and qualitative factors is £1,180k, using the same benchmark.

Threshold	Initial threshold £'000	Final threshold £'000
Overall materiality	1,157	1,180
Performance materiality	926	944
Trivial threshold for errors to be reported to the Audit Committee	35	35

The assessment of what is material is a matter of professional judgement and is affected by our perception of the financial information needs of the users of the financial statements. In making our assessment we assume that users:

- have a reasonable knowledge of business, economic activities and accounts;
- have a willingness to study the information in the financial statements with reasonable diligence;
- understand that financial statements are prepared, presented and audited to levels of materiality;
- recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
- will make reasonable economic decisions on the basis of the information in the financial statements.

We consider materiality whilst planning and performing our audit based on quantitative and qualitative factors.

Performance Materiality

Our audit testing is based on a level of performance materiality, which is a percentage of overall materiality, but also dependent on the level of inherent risk assessed on the area being tested. It is lower than overall materiality as it helps to reduce the risk that the total of the uncorrected or undetected misstatements does not exceed materiality for the financial statements as a whole. It is based on between 50 – 80% of overall materiality depending on the inherent risk level assessed. Our initial assessment of performance materiality is based on low inherent risk, meaning that we have applied 80% of overall materiality as performance materiality.

Misstatements

We aggregate misstatements identified during the audit that are other than clearly trivial. We set a level of triviality for individual errors identified (a reporting threshold) for reporting to the Audit Committee that is consistent with the level of triviality that we consider would not need to be accumulated because we expect that the accumulation of such amounts would not have a material effect on the financial statements. This level was set at 3% of materiality.

2. AUDIT OF THE FINANCIAL STATEMENTS

Set out below are the significant findings from our audit. These findings include:

- our audit conclusions regarding significant risks and key areas of management judgement outlined in the Audit Strategy Memorandum;
- our comments in respect of the accounting policies and disclosures that you have adopted in the financial statements. On page 8 we have concluded whether the financial statements have been prepared in accordance with the financial reporting framework and commented on any significant accounting policy changes that have been made during the year;
- any further significant matters discussed with management; and
- any significant difficulties we experienced during the audit.

Significant risks and key areas of management judgement

As part of our planning procedures we considered the risks of material misstatement in the College's financial statements that required special audit consideration. Although we report identified significant risks at the planning stage of the audit in our Audit Strategy Memorandum, our risk assessment is a continuous process and we regularly consider whether new significant risks have arisen and how we intend to respond to these risks. No new risks have been identified since we issued our Audit Strategy Memorandum.

Management override of controls

Description of the risk

In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.

How we addressed this risk

We addressed this risk through performing audit work over:

- Accounting estimates impacting on amounts included in the financial statements;
- Consideration of identified significant transactions outside the normal course of business; and
- Journals recorded in the general ledger and other adjustments made in preparation of the financial statements.

Audit conclusion

Satisfactory assurance has been gained in respect of presumed risk of management override. We have no matters to report.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Revenue recognition

Description of the risk

There is a presumption under International Standards on Auditing that there is a significant risk of fraud and error in the timing of revenue recognition leading to the material misstatement of revenue overall. This is because revenue is an area of particular focus by users of financial statements and can be subject to judgements as to when grant income should be recognised and if clawback conditions apply to the funding.

The risk above applies only to the non-grant income generated by the College. The risk has been rebutted in relation to the grant income received by the College, given the highly regulated nature of this income, and therefore the low inherent risk associated with it.

How we addressed this risk

We addressed this risk through performing audit work over

- The design and implementation of controls management has in place to ensure income is recognised in the correct period;
- Cash receipts around year end to ensure they have been recognised in the appropriate year;
- The judgements made by management in determining when non government grant income is recognised; and
- Obtaining counterparty confirmation for major non-government grant income.

Audit conclusion

Satisfactory assurance has been gained in respect of the presumed risk of revenue recognition. We have no matters to report.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Expenditure recognition

Description of the risk

For public sector organisations, the same risk in relation to fraud and error in respect of the timing of recording of transactions can apply to the recognition of non-payroll related expenditure and contractual obligations.

The pressure to manage expenditure to ensure that budgeted outcomes are achieved increases the risk surrounding fraudulent reporting of expenditure.

How our audit addressed this risk

We have undertaken a range of substantive procedures including:

- The design and implementation of controls management has in place;
- Testing of non-payroll expenditure around the year end to ensure transactions are recognised in the appropriate year;
- Testing material year end payables, accruals and provisions; and
- Reviewing judgements about whether the criteria for recognising provisions are satisfied.

Audit conclusion

Satisfactory assurance has been gained in respect of the risk of expenditure recognition. We have no matters to report.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Enhanced Risks

Enhanced risks can arise from significant events occurring in relation to the period under review. The College has undertaken a voluntary severance scheme during financial year 2018/19. The scheme is approved by the Scottish Funding Council for operation up to the 31 July 2019. This has been assessed as an area of audit focus due to the funding received from the Scottish Funding Council to undertake the scheme and the significant costs associated to ensure that the College can achieve the savings identified.

Voluntary Severance Scheme

Description of the risk

The SFC has agreed to provide the College with strategic funding in 2018/19 for a voluntary severance scheme, as part of the College's Transformation Plan. An initial strategic grant of £300k was awarded, with a further £700k agreed, that will be used to fund severances in the period to 31 July 2019.

How our audit addressed this risk

We will consider the procedures in place in relation to the operation of the voluntary severance scheme:

- the severance pay amounts and how these have been calculated
- the communication of the voluntary severance scheme to those affected
- whether the funding received to fund the voluntary severance scheme has been utilised in accordance with the grant conditions; and
- the accounting treatment of payments and disclosures made in the financial statement.

Audit conclusion

Our audit work provided satisfactory assurance in respect of the valuation, accounting treatment and disclosure of the voluntary severance scheme. We have no matters to report.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Key Areas of Management Judgement
Key areas of management judgement include accounting estimates which are material but are not considered to give rise to a significant risk of material misstatement. These areas of management judgement represent other areas of audit emphasis.

Valuation of Land and Buildings

Description of area of focus

The College holds land and buildings with a net book value of £107m as at 31 July 2018.

In line with the requirements of the Government Financial Reporting Manual, the College has adopted a formal revaluation policy of an external valuation every five years, with a desktop, interim valuation performed during the five year period. As the full valuation was performed as at 31 July 2018, no revaluation is planned in the current year.

The College policy meets the requirements of the FE SORP that assets are valued sufficiently regularly so that the carrying value of the asset is not materially different from its fair value. The College is required to assess on an annual basis whether there are indicators of impairment to asset at the reporting date.

How our audit addressed this area of management judgement

We will undertake a range of substantive procedures including:

- Review of management's assessment as to whether the value still reflects the prior year valuation;
- Review of the reconciliation between the College's asset register and general ledger; and
- Consider the College's impairment review process for land and buildings

Audit conclusion

Our audit work provided satisfactory assurance in respect of the valuation of land and buildings at the reporting date. Further details can be found at page 12 in relation to significant matters discussed with management regarding the College's policy of review of useful economic life of revalued assets.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Valuation of Pension Liabilities

Description of area of focus

The College makes contributions to two pension schemes – the Scottish Teachers Superannuation Scheme (STSS) and the Strathclyde Pension Fund (SPF). While both are defined benefit schemes, it is not possible to identify the College's share of the underlying assets and liabilities in the STSS and it is therefore accounted for as a defined contribution scheme. The College's share of the SPF's underlying assets and liabilities is identifiable and is recognised in the accounts.
Given the scale of the liability recognised, a misstatement in the reported position could be material to the financial statements.

How we have addressed this area of management judgement

We have addressed the risk by

- Considering the arrangements put in place, including the controls, for making estimates in relation to pension entries in the financial statements; and

- Consider the reasonableness of the actuary's assumptions used in providing the College with information in the financial statements through the use of our internal experts

Audit conclusion

Nationally, in all Local Government Pension Scheme (LGPS) valuations for accounting purposes, during 2018/19 two matters have been identified:

- The impact of Guaranteed Minimum Pension (GMP) equalisation may not be fully included (GMP concerns the minimum pension which an occupational pension scheme has to provide for those employees who were contracted out of the State Earnings-Related Pension Scheme (SERPS) between 6 April 1978 and 5 April 1997. The amount is said to be 'broadly equivalent' to the amount the member would have received had they not been contracted out.); and

- The impact of a legal case held during the year (known as the McCloud case), concerning potential age discrimination in relation to transition provisions introduced as part of pension reform measures may not be fully included.

Mazars actuaries have reviewed the accounting assumptions used by SPF's actuaries in 2018/19. They identified that the impact of GMP equalisation was not fully included as an assumption in the fund valuation.

In our view, both GMP and McCloud give rise to at least a constructive obligation, which is required to be recognised under FRS102. Management has obtained an additional actuarial valuation of the potential impact of the cost of GMP equalisation which has been assessed as being a £190,000 increase in liabilities.

The College and audit team had agreed the initial set of assumptions to be used in arriving at the final LGPS valuation as part of pre-audit planning. The assumption in relation to GMP was, in agreement with the College, amended as part of the audit review process to ensure that the College position was in line with all other organisations in that GMP was to be included in the valuation. On receipt of the updated valuation management, in agreement with the audit team, do not consider that this amount is material to the financial statements, and we have therefore recorded an uncorrected misstatement on page 14.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Qualitative aspects of the entity's accounting practices

We have reviewed the College's accounting policies and disclosures and concluded they comply with the requirements of the 2015 Statement of Recommended Practice: Accounting for Further and Higher Education and the Government Financial Reporting Manual 2018/19 , appropriately tailored to the College's circumstances.

Draft financial statements were received from the College on 16 September 2019 at the start of audit fieldwork. The draft annual report was received during the course of the fieldwork, as agreed in the audit timetable. Both draft financial statements and draft annual report were of a good quality.

Producing quality supporting working papers is a crucial part of compiling financial statements that are complete and materially accurate. They also support the delivery of an efficient audit. Working papers provided for audit were of a good standard and staff were responsive to our requests during the audit.

Significant matters discussed with management

- **Review of useful economic life of revalued assets**

Land and buildings are held at fair value by the College. Depreciated replacement cost is used as a measure of fair value by the College during the years where no revaluation is carried out so long as the depreciated value is not considered to be materially different from that of the fair value. During the work performed in the year on the value of land and buildings it was noted that the useful economic life of underlying assets applied by the College and thus the level of depreciation charged in the year differs from that indicated by the most recent valuation carried out.

The difference identified in the current year between the depreciation charged using the asset lives suggested by the valuers and those used by the College, is not material. However, if a revaluation is not undertaken in 2019/20 (and it is not scheduled to take place) and the current rate of depreciation is applied, there is the potential that the differing measures used could result in a material difference.

This should be considered by management so that appropriate steps are taken in advance of the reporting date for 2019/20 to gain assurance that the depreciated value is not materially different from fair value or to reassess the useful economic life of assets and the annual depreciation charged.

Significant difficulties during the audit

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

3. INTERNAL CONTROL RECOMMENDATIONS

The purpose of our audit is to express an opinion on the financial statements. As part of our audit we have considered the internal controls in place relevant to the preparation of the financial statements. We do this in order to design audit procedures to allow us to express an opinion on the financial statement and not for the purpose of expressing an opinion on the effectiveness of internal control, nor to identify any significant deficiencies in their design or operation.

The matters reported are limited to those deficiencies and other control recommendations that we have identified during our normal audit procedures and that we consider to be of sufficient importance to merit being reported. If we had performed more extensive procedures on internal control we might have identified more deficiencies to be reported or concluded that some of the reported deficiencies need not in fact have been reported. Our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

Priority ranking	Description	Number of issues
1 (high)	In our view, there is potential for financial loss, damage to reputation or loss of information. This may have implications for the achievement of business strategic objectives. The recommendation should be taken into consideration by management immediately.	nil
2 (medium)	In our view, there is a need to strengthen internal control or enhance business efficiency. The recommendations should be actioned in the near future.	nil
3 (low)	In our view, internal control should be strengthened in these additional areas when practicable.	1

Recommendations

Employee pension contribution rates- Level 3

During the course of the audit work performed on staff costs, we identified an incorrect rate applied to an employee pension contribution. This was investigated by the College and determined to be an isolated instance and steps have been taken to rectify. We would recommend that the College takes an additional step to reconcile the employee contributions applied to monthly payroll to ensure consistent.

Potential effects

The application of incorrect pension contributions rates might result in a material misstatement of staff costs if this affected a high volume of staff members. This may also mean the College are not abiding by the terms of staff contracts, leaving themselves open to legal action and reputational damage.

Management Response

The College has implemented a revised procedure which ensures that a temporary staff members employee pension contributions are calculated and checked on a monthly basis. The revised procedure also includes spot checks on the calculated amounts. This revised operating procedure has been verified by the external auditors and therefore the recommendation has been fully implemented.

4. SUMMARY OF MISSTATEMENTS

Unadjusted misstatements

We set out below the misstatements identified above the level of trivial threshold of £35k.

The College obtained an additional valuation of their share of the SPF pension liability to incorporate costs of Guaranteed Minimum Pension (GMP) equalisation as an assumption in the valuation. This has indicated an increase in the liability of £190k. Management do not consider this amount material and have not adjusted the financial statements.

		Statement of Comprehensive Income and Expenditure		Balance Sheet	
		Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1	Dr: Re-measurement of defined benefit liability	190			
	Cr: Long term liabilities (Pension deficit)				190
	The additional pension liabilities arising from incorporation of GMP costs in the pension valuation				
	Total	**190**	**-**	**-**	**190**

Disclosure amendments

A number of disclosure amendments were discussed and agreed with management, including:

- Consistency of financial data in Performance Report with Financial Statements
- Remuneration and Staff Report data
- Accounting policy note disclosures in line with FRS 102 guidance

5. WIDER SCOPE

Our approach to wider scope work

The Code requires us to conclude and make a judgement on the four dimensions of wider scope work. These are:

- financial sustainability;
- financial management;
- governance and transparency; and
- value for money.

In 2018/19 we have also considered the following risk areas as they relate to the College:

- EU withdrawal
- Changing landscape of public financial management
- Dependency on key suppliers
- Openness and transparency

We do not consider that any of the above constitute a significant risk for the College at this point, but will continue to monitor.

5. WIDER SCOPE
FINANCIAL MANAGEMENT

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

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

Financial performance
FE/HE SORP position

	2018/19 £'000	2017/18 £'000
Operating income	58,991	58,724
Staff costs	(43,148)	(41,878)
Operating expenditure	(19,011)	(19,916)
Operating Deficit for the year (FE/HE SORP basis)	**(5,960)**	**(3,070)**

Staff cost increases are primarily driven by the FRS 102 pension cost actuarial adjustment. The above table shows the financial performance of the College for 2018/19 and 2017/18 under the FE/HE SORP. Despite a deficit being shown over both years:

- The College achieved its financial targets and spending was in line with the plan;

- There were no significant changes to the reported position during the year; and

- The student credit target was exceeded confirming the level of funding in the financial statements.

Adjusted operating position

The table above sets out the financial position in accordance with the SORP requirements. The table overleaf reflects the 'adjusted operating position' as required by the Accounts Direction set by the SFC. The adjusted operating position removes more volatile accounting entries, such as the valuation of pensions. Full details of the adjustments included are shown in the Performance Report within the Annual Report and Financial Statements.

5. WIDER SCOPE
FINANCIAL MANAGEMENT (CONTINUED)

	2018/19 £'000	2017/18 £'000
Deficit before other gains and losses	(5,960)	(3,070)
Add back:		
- Depreciation (net of deferred capital grant release)	3,518	2,980
- Non-cash pension adjustment (service cost)	2,444	1,241
- Non-cash pension adjustment (Interest cost)	390	732
- Loss on disposal of assets	129	153
Deduct:		
- Non government capital grants	-	(1,529)
- Loan repayments	(495)	(488)
Adjusted operating position - surplus	**26**	**19**

The Accounts Direction issued by the SFC for 2018/19 required Colleges to submit the adjusted operating position calculation with draft accounts to the SFC for review before the accounts are signed off.

The table above indicates that once the non cash and other applicable adjustments are made, the College has achieved a modest operating surplus in the current and prior year. This demonstrates that the College has operated within its budget for the 2018/19 and 2017/18 years. Loss on disposal of assets relates to the demolition of certain buildings by the College as part of its estates rationalisation and reflects the net book value of buildings prior to disposal. These losses are in line with the College's Estates Strategy.

Impact of Depreciation Budget

The Statement of Comprehensive Income and Expenditure is prepared under the FE/HE SORP, which does not permit the inclusion of the non-cash budget for depreciation. Colleges may show a deficit equivalent to net depreciation as a result of having to meet Government accounting rules.

	2018/19 £'000	2017/18 £'000
Operating Surplus/Deficit for the year (FE/HE SORP basis)	(5,960)	(3.070)
Add: Depreciation budget for government funded assets (net of deferred capital grant) for academic year	3,518	2,980
Operating (Deficit)/Surplus on Central Government accounting basis	(2,442)	(90)

The table above shows a deficit when the impact of the depreciation budget is taken as the only adjusting factor to the financial position. The operating position table at the top of the page reflects further, more volatile adjustments that show an operating surplus. The College is currently considered to be operating sustainably within its funding allocation.

5. WIDER SCOPE
FINANCIAL MANAGEMENT (CONTINUED)

Budgetary process

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

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

Internal controls

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

We have also considered the work of internal audit, from individual reviews of financial systems and their annual audit opinion on the control framework in place at the College. Internal auditors Scott-Moncrieff provided a high level of assurance on arrangements to send budget returns to the Scottish Funding Council (SFC).

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

Prevention and detection of fraud and irregularity

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

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

National Fraud Initiative

The College participated in the 2018/19 National Fraud Initiative (NFI) exercise. Data was submitted in line with timescales and the Audit Committee have been informed of the exercise. No significant findings or issues arose from NFI during the 2018/19 audit process.

5. WIDER SCOPE
FINANCIAL SUSTAINABILITY

Dimension

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

Our conclusion

West College Scotland has adequate financial planning arrangements in place. A long-term operational funding gap was previously identified by the College as well as a need for significant capital investment to maintain building standards and therefore ensure continued revenue income based on student numbers. There has been no development in obtaining capital investment funding during the year and the risk of reduced performance as a result of a deteriorating estate remains.

Identified significant risks to our wider scope work

As part of our planning procedures we considered whether there were significant risks that would impact on any of the four areas of our wider scope work that would require special audit consideration. We set out the identified risk to this area of wider scope work and how we addressed the risk.

Financial Sustainability

Description of the risk

The College has identified that in order to deliver a balanced budget for 2018/19 and beyond, it will require to make significant savings over the 5 year period from 2018/19.

How we addressed the risk

We have addressed the risk by:

- Reviewing the forecast financial position in the 5 year financial plans submitted to SFC;
- Reviewing the financial and resource implications of any voluntary severance scheme proposed to be run by the College;
- Alternative plans being considered by the College to ensure a balanced budget is achieved;
- Reviewing the financial reporting arrangements in place at the College; and
- Progress made with plans to replace the Greenock and Paisley campuses, alongside the impact on finance performance

Wider scope conclusion

The College and its Board have a clear view of financial challenges and long term risks faced. A funding gap of £4m has been identified by the College over the next five years. Efficiency savings have been implemented during 2018/19 mainly through voluntary severance schemes to address the funding gap.

The College estate was previously identified as requiring significant capital investment to bring the current estate up to condition B standards (£33m over the next 10 years) or approximately £200m to replace both the Paisley and Greenock campuses. Outline business cases have been submitted to the Scottish Funding Council for replacement of the two campuses, but to date, these have not progressed to full business cases. There is a risk that without further revenue funding to support estates maintenance or capital funding to support replacement, the financial position of the College may deteriorate.

5. WIDER SCOPE
FINANCIAL SUSTAINABILITY (CONTINUED)

Financial Planning

The College prepares a 5 year budget and forecast which is scrutinised by the Finance and General Purposes Committee and approved by the Board. The plan includes assumptions about inflation in the short and medium term and highlights other financial stability risks. The College is very clear on the risks to financial sustainability it faces and the uncertainty of funding over the medium and long term associated with the ending of ESF funding, the funding support impacts of national bargaining and estates maintenance funding.

The budget and forecasting process performed in 2017/18, identified a potential funding gap, as reported in our 2017/18 Annual Audit Report. The College prepared and submitted a Business Transformation Plan to the SFC in order to obtain funding for a voluntary severance scheme. The Business Transformation Plan was implemented by the College during 2018/19 and £1m of funding was provided by the SFC for the voluntary severance scheme, which has taken place. There continues to be on-going dialogue between the College and the SFC in relation to the Business Transformation Plan and progress is regularly monitored by the Board. Some efficiencies achieved to date are included in the 5 year budget and forecast prepared by the College in 2018/19.

A summary of the College's five-year forecast is included in the table below.

	Forecast 2019/20 £'000	Forecast 2020/21 £'000	Forecast 2021/22 £'000	Forecast 2022/23 £'000	Forecast 2023/24 £'000
Total Income	56,128	56,323	56,441	56,521	50,536
Staff costs	42,721	43,001	43,326	41,414	42,378
Total other expenditure	13,128	13,035	12,818	13,443	12,494
Operating surplus/(deficit) before other gains and losses	**279**	**287**	**297**	**1,664**	**1,664**
Net depreciation spend	1,640	1,639	1,639	1,639	1,639
Efficiencies required to generate break even position	**1,386**	**1,377**	**1,367**	**-**	**-**
Projected underlying operating result	**25**	**25**	**25**	**25**	**25**

The table above indicates a funding gap has been identified of on average £1.3m each year for the following 3 years. With staff costs contributing around 76% of overall expenditure, this is the area identified by the College where potential longer term efficiencies could be made. A voluntary severance scheme was implemented during 2018/19 which is anticipated to deliver further efficiencies in 2019/20.

The College five-year plan forms the basis of the Financial Forecast Return (FFR) required to be submitted by the SFC annually. Generally, the same assumptions are used in both. The SFC FFR assumptions would reduce the estimated efficiencies required to be made by the College in years 2019/20, 2020/21 and 2021/22, but however creates the need for efficiencies from 2022/23 onwards. The key differences are in relation to;

- Increased employers contributions to Scottish Teachers Superannuation Scheme funding was forecast at 50% by the College. The SFC has since announced that the increase relating to 2019/20 will be fully funded and thus assumed fully funded in future years.
- The SFC funding formula was anticipated to be revised in 2022/23 which would have resulted in a decrease in credit activity for the College. SFC assumptions no longer include this revised formula. The removal of the revision has the impact of a reintroduction of staff costs that were not forecast with reduced activity.
- Voluntary severance costs associated with cessation of ESF funding is no longer included within the SFC assumptions.

5. WIDER SCOPE
FINANCIAL SUSTAINABILITY (CONTINUED)

Financial Planning (continued)

On consideration by the College of the revised assumptions they have concluded that this includes some uncertainties around funding for the increase to employers pension contributions and as such will continue to plan for the higher level of efficiencies in years 2019/20, 2020/21 and 2021/22 as per the above table.

The income included in the forecast presumes the College will achieve its full credit activity target. Should the College have a reduction in capacity as a result of its ageing estate and potential impairment of buildings there is a risk that credit activity targets may not be met.

Asset Management and Estates Strategy

Included in the operating costs in the previous table, are significant maintenance costs for the College estate, this is generally funded through estate lifecycle maintenance provided by SFC, although levels of funding have significantly decreased in recent years. West College Scotland operates from three primary locations in Clydebank, Greenock and Paisley across 12 operational buildings. Of this, only four buildings are graded at level 1 (excellent) for functional suitability. Seven buildings, at the Greenock and Paisley campuses require major repair or replacement. Recent estimates of cost to repair and maintain the Greenock and Paisley campuses at an acceptable condition are £20m and £11m respectively, spread over the next 10 years.

The College submitted Outline Business Cases (OBC) for the replacement of the Paisley and Greenock campuses to the Scottish Funding Council in October 2016 and October 2017 respectively. The estimated investment required to replace both campuses is approximately £200m. The OBC for the Greenock campus was revised during the year following discussions with Inverclyde Council with the final Local Development Plan recognising the requirement for a new college campus in Greenock but not specifying at what location. Dialogue continues with Inverclyde Council and also with Renfrewshire Council regarding the Paisley campus. The college also continues engagement with the SFC on progressing the outline business cases, but there has been no affirmative response to date.

<u>National estates survey</u>

Gardiner & Theobald were appointed by the Scottish Funding Council in January 2017 to provide a summary of the conditions of the estates within the Scottish Further Education sector. The total gross backlog for the sector estimated by the survey was £363 million. 10% of these costs were defined as urgent, requiring action within the next year, with the majority of the costs requiring action within 3-5 years.

The survey showed an estimate of £21.3 million of costs over the 5 year period from 2017-18 to 2022-23 for the West College Scotland estate, with £1.5m being identified as urgent. The most significant urgent costs identified relate to the Tower at Greenock, Finnart Street (£409k) and Renfrew South and Inchinnan North buildings at Paisley Campus (£377k and £253k respectively). This is consistent with the College's own estimates and Estates Strategy.

Priority maintenance funding of £3m was allocated to the College for 2018/19, this level of funding has been reduced to £1.7m for 2019/20. The College intends to use this funding in agreement with the SFC to address the areas of priority raised by the report in conjunction with estate projects that have been identified by the College itself to support a long term approach of the estates strategy.

The College estate requirements cannot be met through the SFC core funding. If the condition of the estate deteriorates to the extent that students cannot be attracted, there is likely to be a reduction in student numbers, which will in turn reduce the funding received by the College.

5. WIDER SCOPE
GOVERNANCE AND TRANSPARENCY

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

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

Governance arrangements

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

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

During 2018/19, the Board consisted of 17 members, 7 female (including the Principal) and 10 male. The Board continues to work towards a gender balance that meets with the objective of the Gender Representation on Public Boards (Scotland) Bill which was introduced by the Scottish Parliament in June 2017 with an implementation date of 2022.

The key committees comprises of, and are chaired by Board members, with each also containing the Principal, with the exception of the Audit Committee. In addition, the Chair of the Board is also not permitted to be a member of the Audit Committee. Appropriate College officers attend committees and present reports as required.

The Audit Committee has co-opted independent members, appointed for their specific skills and expertise. We have found this arrangement works well, and encourage the College to continue this, where possible.

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

The governance statement confirms the College's compliance with the 2016 Code of Good Governance for Scotland's Colleges.

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

Internal audit
An effective internal audit service is an important element of any organisation's governance arrangements. Internal audit provide the College with independent assurance on internal control and corporate governance processes. The internal audit function at the College is provided by Scott-Moncrieff. Internal audit have attended Audit Committees throughout the year and have produced 7 reports to support the overall Head of Internal Audit Opinion.

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

5. WIDER SCOPE
VALUE FOR MONEY

Dimension
Value for money concerns using resources effectively and continually improving services.

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

Performance management
The College delivered its Regional Outcome Agreement (ROA) target credits and achieved a small operating financial surplus. A small decrease in student attainment and attendance has been noted in the year, however this has anticipated to follow a sector wide trend. There is close monitoring of the delivery of the ROA and financial performance reports provide sufficient information to allow members to understand performance. Budget monitoring information provides a detailed analysis of variances allowing budget objectives to be achieved. Through delivery of the 2018/19 budget there is clear evidence that the College understands cost drivers and is in control of costs.

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

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

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

6. OUR FEES

Fees for work as the College's appointed auditor

We reported our proposed fees for the delivery of our work in our Audit Strategy Memorandum, presented to the Audit Committee in May 2019. Having completed our work for the 2018/19 financial year, we can confirm that our final fees are as follows:

Area of work	Proposed fee 2018/19	Final fee 2018/19
Auditor remuneration	£27,840	£27,840
Pooled costs	£1,540	£1,540
Contribution to Audit Scotland costs	£1,620	£1,620
Total Fee	**£31,000**	**£31,000**

We confirm that these fees are in line with the scale fee set by Audit Scotland. We also confirm that we have not undertaken any non-audit services for the College in the year.

APPENDIX A INDEPENDENCE

As part of our ongoing risk assessment we monitor our relationships with you to identify any new actual or perceived threats to our independence within the regulatory or professional requirements governing us as your auditors.

We can confirm that no new threats to independence have been identified since issuing the Audit Strategy Memorandum and therefore we remain independent.