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INFRASTRUCTURE, GOVERNMENT & HEALTHCARE

John Wheatley College

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

Audit: Year ended 31 July 2007
11 December 2007

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

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If at any time you would like to discuss with us how our services can be improved or if you have a complaint about them, you are invited to contact David Watt, who is the engagement leader for our services to the College, telephone 0141 300 5695, email david.watt@kpmg.co.uk who will try to resolve your complaint. If your problem is not resolved, you should contact Lorraine Bennett, our Head of Audit in Scotland, either by writing to her at Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2EG or by telephoning 0131 222 2000 or email to lorraine.bennett@kpmg.co.uk. We will investigate any complaint promptly and do what we can to resolve the difficulties. After this, if you are still dissatisfied with how your complaint has been handled you can refer the matter to Russell Frith, Director of Audit Strategy, Audit Scotland, 110 George Street, Edinburgh, EH2 4LH.

Executive summary

This report summarises our work for the 2006-07 year and our findings in relation to our audit of the financial statements, financial reporting and corporate governance arrangements.

Financial statements

On 11 December 2007 we issued an audit report expressing a qualified opinion on the financial statements of the College for the year ended 31 July 2007. Our audit opinion was qualified in respect of the adjustments and disclosures that would be required to comply with FRS 17. In all other respects our opinion was unqualified.

Management has accounted for the College's participation in the Strathclyde Pension Fund ("the Fund") on a defined contribution basis under FRS 17. Management believe that the College cannot identify its share of assets and liabilities in the Fund on a reasonable and consistent basis. In our view, the College's share of the underlying assets and liabilities in the Fund can be identified on a consistent and reasonable basis and its participation should therefore be accounted for as a defined benefit scheme. This conclusion has been reached by drawing on the work of our actuarial staff and has involved specific discussions with the scheme actuaries and the facts presented by them.

Accounting for the College's participation in the Fund as a defined benefit pension scheme would increase the College's net assets at 31 July 2007 by £93,000 (2006: £545,000 decrease), increase its surplus for the year by £60,000 (2006: reduce the surplus by £13,000) and increase its total recognised gains and losses for the year by £579,000 (2006: £189,000).

Our opinion on the regularity of transactions was unqualified.

Other financial statement areas

The East End campus was completed during the year at a total cost of £13.6 million. In line with accounting standards, management engaged an independent firm of chartered surveyors to value the East End campus, resulting in an increase of £417,380 compared to the cost of construction.

The College has a shared services agreement with Glasgow City Council covering library services and information technology facilities in an area of the College's Easterhouse campus. The College's external valuer confirmed that the carrying value of the Easterhouse campus is appropriate and that the right of access given to the Council is offset by the corresponding benefit gained by the College through access to Council facilities.

Financial position

The College has reported a surplus of £35,000 for the year to 31 July 2007 against a forecast surplus of £46,000. Gross income and expenditure increased by 11% compared to 2005-06, with additional operating expenses being matched by similar levels of additional income. None of movements in the surplus outturn were significant, demonstrating the existence and operation of the College's financial management and reporting processes.

The College is forecasting a surplus of £50,000 in 2007-08, which is consistent with its long term strategic plans.

Governance and strategy

The College has comprehensive and robust corporate governance arrangements including:

- formal evaluation of arrangements against 'the principles of good governance for public bodies' every second year and assessment against the Scottish Executive's on-board toolkit in intervening years;
- the corporate strategy identifies a number of values that set the tone of the organisation, including commitment and leadership, sustainable development, equal opportunities, accountability, sound governance, continuing professional development, quality enhancement and inclusiveness;
- a very comprehensive Board of Management report, which exceeds the requirements of SORP 2003 and demonstrates commitment to transparent public reporting;

There are no significant weaknesses disclosed in the statement on internal control, and no significant control weaknesses were identified through our work on the control systems within the College. The approved internal audit programme for 2006-07 has been completed and the internal auditors have concluded that the College has in place "*an adequate framework of control over the systems they examined*".

The Office of the Scottish Charity Regulator ("OSCR") recently reported the results of its pilot review and the College was identified as one of two organisations that do not meet the requirements. The report concluded that "*John Wheatley College has exclusively charitable purposes and provides public benefit. However, the Charity Test was not met as its constitution expressly permits Scottish Ministers or a Minister of the Crown to direct or otherwise control its activities.*"

OSCR praised the systems in place at the College and formally reported that "*The College had absolutely no difficulty in providing supporting materials. It [the College] produced nothing new and was able to use materials which it produced for other quality audits or satisfy the governance standards which apply to public bodies in Scotland. … Almost all documentation required was already available and in the public domain on the College's web-site.*"

During the period since confirmation of the outcome, management has maintained regular communication with stakeholders and interested parties, including OSCR, Scottish Ministers, and the local community planning partnership, in relation to the potential impact of losing charitable status.

We understand that the Scottish Government is committed to ensuring that further education colleges retain charitable status, but the method by which this will be achieved remains unclear at this time.

Introduction

Audit framework

2006-07 was the first year of our five-year appointment as external auditors of John Wheatley College ("the College"). This report to the Board of Management of the College and the Auditor General for Scotland summarises our opinion and conclusions and highlights significant issues arising from our work.

In accordance with Audit Scotland's *Code of Audit Practice*, the scope of the audit was to:

- provide an opinion on the College's financial statements and, as required by relevant authorities, the regularity of transactions;
- review and report on (as required by relevant legislation, the Code and any guidance issued by Audit Scotland):
  - the College's corporate governance arrangements as they relate to: its review of systems of internal control; the prevention and detection of fraud and irregularity; standards of conduct, and prevention and detection of corruption; and its financial position
  - the College's arrangements to achieve Best Value
  - other aspects of the College's arrangements to manage its performance, as they relate to economy, efficiency and effectiveness in the use of resources.

The framework under which we operate under appointment by Audit Scotland was outlined in the audit plan for the year discussed with the College's audit committee.

Basis of information

External auditors do not act as a substitute for the Board of Management's own responsibilities for putting in place proper arrangements to account for its stewardship of resources made available to it and its financial performance in the use of those resources, to ensure the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the effectiveness of those arrangements and, through the principal, to make arrangements to secure Best Value.

Acknowledgement

Our audit has continued to bring us into contact with a range of College staff. We wish to place on record our appreciation of the co-operation and assistance extended to us by staff during the first year of our work in the discharge of our responsibilities. We also note the high quality of the College's preparation for the audit and co-operation of the chief finance officer and his team.

Financial commentary

This section of our report summarises the main features of the financial statements and key movements from the prior financial year.

Income and expenditure account

The surplus for the year of £35,000 is 0.4% of total income (2005-06, £22,000). Based on 2005-06 financial statements the sector average is around 2%. The College is therefore slightly below the sector average. However, it currently has a balance of £789,000 in general reserves and is classified as financially secure by the Scottish Funding Council.

Income

Total income increased by £895,000 (11%). The increase is primarily due to increases in Scottish Funding Council and other grants. The most significant movements were:

- increase in Scottish Funding Council recurrent grant of £545,000;
- £161,000 of new build grant income recognised in 2006-07 to meet the revenue costs associated with the move to the new campus;
- increase in the release from deferred capital grants of £132,000; and
- increase in Greater Easterhouse learning network grant income of £58,000.

The majority of income is received from the Scottish Funding Council, but the College has also increased external income from European grants, although this is forecast to fall in future years. The following table identifies the sources of income in 2005-06 and 2006-07.

	2006-07 £'000	***2005-06 £'000***	**2006-07 %**	***2005-06 %***
Scottish Funding Council grants	7,559	*7,074*	85	*88.5*
Tuition fees and education contracts	201	*223*	2	*3*
Other operating income	1,058	*628*	12	*8*
Bank interest	56	*54*	1	*0.5*
Total income	**8,874**	***7,979***	**100%**	***100%***

Other operating income has increased as a proportion of total income in 2006-07, mainly due to the increase the third party grants, other than from the Scottish Funding Council, as outlined above.

Expenditure

Overall, total expenditure has increased by £882,000 (11%), which is in line with the increase in income. The increase is primarily due to increases in staff costs and other operating expenses. The most significant movements were:

- £266,000 increase in expenditure on wages and salaries;
- £225,000 increase in premises expenditure, including depreciation; and

- £196,000 increase in revenue project costs.

The majority of expenditure is incurred on staff costs. The following table identifies the key elements of expenditure in 2005-06 and 2006-07.

	2006-07 £'000	***2006-06 £'000***	**2006-07 %**	***2005-06 %***
Staff costs	5,454	*5,146*	62	*65*
Other operating expenditure	2,798	*2,296*	32	*29*
Depreciation	587	*515*	6	*6*
Total expenditure	**8,839**	***7,957***	**100%**	***100%***

Other operating expenditure has increased as a proportion of total expenditure, mainly due to costs relating to the new East End campus, the majority of which were met by specific funding.

Balance sheet

The College has reported an increase in net assets of £5,816,000 during the year. The balance sheets at 31 July 2006 and 2007 are summarised as follows:

	2006-07 £'000	***2005-06 £'000***
Fixed assets		
Land and buildings	21,108	*7,045*
Land and buildings under construction	-	*8,479*
Equipment	856	*256*
Current assets		
Stock	15	*17*
Debtors	759	*1,769*
Cash at bank and in hand	119	*1,417*
Creditors due within one year	(1,049)	*(2,990)*
Net current assets	**(156)**	***213***
Creditors due after one year	-	-
Provisions for liabilities and charges	(128)	*(129)*
Net assets	**21,680**	***15,864***
Deferred capital grants	18,303	*14,001*
General reserve	789	*141*
Revaluation reserve	2,588	*1,722*
Total	**21,680**	***15,864***

Significant movements during the year include:

- increase in fixed assets due to completion of the East End campus (£5,982,000);
- decrease in debtors, creditors and cash, all of which were abnormally higher in 2005-06 due to the new campus project (net decrease of £369,000); and
- increase in the valuation of the East End and Easterhouse campuses (£1,187,000).

Financial forecasting

The financial forecast return submitted to the Scottish Funding Council in June 2006 forecast a surplus of £46,000 to 31 July 2007. The actual outturn was a surplus of £35,000. The following table summarises the movements during the year.

	£'000
2006-07 forecast outturn per the financial plan	**46**
Additional Scottish Funding Council grants	24
Reduction in tuition fees	(4)
Additional other income	338
Additional other operating expenses	(311)
Reduction in staff costs	69
Additional depreciation following the revaluation of fixed assets at 31 July 2006	(127)
2006-07 actual outturn at 31 July 2007	**35**

Analysis of the reconciliation between the forecast and actual outturn identifies that additional operating expenses were matched by similar levels of additional income. The additional depreciation as a result of the revaluation exercise would not have been known in June 2006 when the forecast was reported. The remainder of the movements were not significant, demonstrating the existence and operation of the College's financial management and reporting processes.

The following table summaries the forecast income, expenditure and cash balances for the College for 2007-08.

	£'000
Income	8,893
Expenditure	(8,843)
Forecast surplus for the year ending 31 July 2008	**50**
Cash balance at 31 July 2007	119
Forecast cash balance at 31 July 2008	606
Forecast movement in cash during 2007-08	**487**

The increase for 2007-08 is based on a rise in Scottish Funding Council grants, which are offset by an anticipated reduction in other income and a rise in staff costs, resulting in a forecast surplus £50,000.

The increased cash balance is primarily due to the receipt of debtor balances relating to funding of the new campus, for which the cash expenditure on the campus was incurred during 2006-07.

Governance and risk management

Introduction

Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all bodies.

Through the principal, the Board of Management is responsible for establishing arrangements for ensuring the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. The *Code* requires auditors to review and report on the College's corporate governance arrangements as they relate to:

- the College's reviews of its systems of internal control, including its reporting arrangements;
- the prevention and detection of fraud and irregularity;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- its financial position.

Management is responsible for establishing arrangements for the conduct of its affairs, including compliance with applicable guidance, ensuring legality of activities and transactions and monitoring the adequacy and effectiveness of these arrangements in practice.

Governance arrangements

The Board of Management has 16 full members and four co-opted members, who were invited to join the board based on their individual skills, such as capital and building management. There are seven standing committees, including capital investment, personnel and staffing, financial control, and audit, each of which is formally constituted and has its own terms of reference. This comprehensive governance structure – which includes non-executive, student and academic representation – is demonstrative of best practice and exceeds the minimum requirements of the Scottish Funding Council. The committee structure provides the Board of Management with the mechanisms to ensure appropriate oversight and monitoring of financial and academic activities.

In addition, a project management committee was established to oversee the management of the East End campus capital project. Its membership was augmented by co-opted members with highly specialist skills. This committee was disbanded when the project reached 'practical completion'.

The College has a number of values that are core to its operations and set the tone of the organisation from senior management. These are identified in the 2006-09 corporate strategy and include commitment and leadership, sustainable development, equal opportunities, accountability, sound governance, continuing professional development, quality enhancement and inclusiveness.

Risk management

The College's approach to risk management is based on guidance produced by the Chartered Institute of Public Finance and Accountancy for the further and higher education sectors in Scotland. The College's risk management strategy is owned by the Board of Management and all its standing committees. A risk register has been established and is a standing item on the Board of Management meeting agenda and is amended if discussion identifies previously unforeseen risks.

The College has also established a risk management committee, which meets regularly during the year to review the College's response to identified risks. The senior management team receives reports setting out key performance and risk indicators and considers possible control issues brought to their attention by early warning mechanisms which are embedded within the operational units and reinforced by risk awareness training. Risks are identified, prioritised and assessed according to likelihood and consequence; where there is no existing mitigating control in place measures are taken to address and mitigate the risk.

Systems of internal control

Corporate governance statement

The statement for 2006-07 provides details of the processes and controls and management highlight that the organisation is committed to exhibiting best practice in all areas of corporate governance. The corporate governance statement is informed by the results of internal consideration of the arrangements in place.

In line with best practice, the College formally evaluated its arrangements against 'the principles of good governance for public bodies' and reported the results to the Board of Management after the year end. This evaluation is discursive in nature, including detailed consideration of the depth of arrangements, and is performed every second year. The independent clerk to the Board of Management assesses governance arrangements against the Scottish Executive's on-board toolkit in intervening years. This process is based on a comprehensive checklist, but does not require the same consideration of the depth and nature of processes in place.

The audit committee requested that, as part of the audit needs assessment, internal audit review the corporate governance arrangements during 2006-07. The results of this review were positive and included only one low priority recommendation for improvement.

On an annual basis the principal writes to all budget holders informing them of their responsibility to notify the Board of Management of any control weaknesses or instances of maladministration falling under their remit. This is good practice, although accountability would be further enhanced if a positive return was requested.

The College has made a fully compliant corporate governance statement. We are required to review this to assess whether the description of the process adopted by the College in reviewing the effectiveness of the system of internal control is consistent with our understanding of the process and report any inconsistencies in our opinion. We are not required to provide an opinion on the College's system of internal control.

We have reviewed the corporate governance statement and consider it consistent with our understanding of the process followed by the College during the year.

Regularity

The Board of Management considers all incoming correspondence relevant to its strategic management role from the Scottish Funding Council and other regulatory or advisory bodies, including organisations such as the Association of Scottish Colleges and Audit Scotland. Relevant communication is also considered by the audit committee. This allows management to demonstrate the College's approach to considering incoming guidance and taking action where appropriate.

Internal audit

The approved internal audit programme for 2006-07 has been completed and the internal auditors have concluded that the College has in place "*an adequate framework of control over the systems they examined*".

Internal audit monitor the systems of internal control, risk management controls and governance processes in accordance with an agreed plan of input, and report their findings to management and the audit committee. Management is responsible for the implementation of agreed audit recommendations and internal audit undertake periodic follow up reviews to ensure that such recommendations have been implemented.

The College maintains an audit action plan documenting any high grade recommendations that are identified by internal audit. Items are only removed from the plan when the audit committee is satisfied that corrective action has occurred. This is in line with best practice and ensures that the committee has the opportunity to challenge and assess management action in response to recommendations raised. As at October 2007 the College audit action plan contains seven high grade recommendations. Management has taken action in response to all of these, which will be subject to follow up by internal audit during 2007-08.

The internal audit strategic plan for the period 2006-09 has been prepared based on the internal auditors' assessment of risk and College needs. An operational plan exists for each year within this period that identifies financial and non-financial systems, the risk analysis (high, medium or low) and the number of audit days in each year. The current year three plan has a number of inconsistencies in the frequency of review of systems assessed as high and medium risk. For example, payroll is assessed as 'high' risk and only subject to review once during 2006-09, but the debt collection process is assessed as 'medium' risk and is subject to review twice during the same period. The audit committee should ensure that the needs assessment reflects the College's own assessment of risk and the role and importance of individual financial and non-financial systems in achieving its strategic objectives.

The 2007-08 internal audit plan was discussed at the audit committee meeting on 8 November 2007. The plan was approved with a reduction of seven days. Three of these seven days relate to the audit of hardship and bursary statements, which is now performed by another firm of accountants following a value for money exercise. Members of the audit committee and internal audit agreed that at 24 days, the plan is appropriate based on their knowledge of other further education colleges. The reduction reflects a perceived reduction diminution of the risk the College faces.

Internal controls

Drawing on the work of internal audit, in accordance with our plan we undertook detailed testing in relation to both entity-level and key financial controls. We have identified some areas for enhancement. Recommendations are included in the action plan in appendix one and have been accepted by management. None of these recommendations are significant.

Testing of the design and operation of controls over significant risk points in terms of major financial systems confirms that controls are designed appropriately and operating effectively.

Charities and Trustee Investment (Scotland) Act 2005

The Charities and Trustee Investment (Scotland) Act 2005 ("the Act") came into force in April 2006, introducing new duties and responsibilities for the Office of the Scottish Charity Regulator ("OSCR"). Over time OSCR intends to undertake a rolling review of charities entered in the Scottish charity register to assess whether they meet, and continue to meet, the charity test: purposes will have to be charitable in the context of the charity test set out in section 7 of the Act and charities will have to show that they provide public benefit.

OSCR recently reported the results of its pilot review and that six of the eight organisations satisfied the 'public benefit' test. The College was identified as one of the two organisations that do not meet the requirements. The report concluded that "*John Wheatley College has exclusively charitable purposes and provides public benefit. However, the Charity Test was not met as its constitution expressly permits Scottish Ministers or a Minister of the Crown to direct or otherwise control its activities.*" OSCR's report clearly states that the results of the review cannot necessarily be applied to similar organisations, but there is an expectation within the sector that the charitable status of further education colleges is at risk because the ministerial control identified by OSCR exists in the Further and Higher Education (Scotland) Act 1992 (as amended by the Further and Higher Education (Scotland) Act 2002 ("the Act").

OSCR has given the College two years to resolve the issue of control that has been identified. This is clearly beyond the control of the College's Board of Management since it relates to changes which will require to be made to the statutory framework which applies to the further education sector in Scotland.

The Board of Management has been proactive in its participation in the rolling review, from volunteering to be part of the review to considering the final outcome. OSCR praised the systems in place at the College and formally reported that "*The College had absolutely no difficulty in providing supporting materials. It [the College] produced nothing new and was able to use materials which it produced for other quality audits or satisfy the governance standards which apply to public bodies in Scotland. … Almost all documentation required was already available and in the public domain on the College's web-site.*"

The Board of Management understands the reasons supporting OSCR's view and has not appealled against the decision because the issue is beyond its control.

During the period since confirmation of the outcome of OSCR's review the Board of Management has continued to discuss the potential impact of losing charitable status. There would be additional direct costs of losing tax exemptions and an indirect impact of a potential reduction in the College's ability to secure external funding that is solely available to charities. In addition, the College has maintained regular communication with stakeholders and interested parties, including OSCR, Scottish Ministers, and the local community planning partnership. We understand that the Scottish Government is now formally committed to ensuring that further education colleges retain charitable status, but the method by which this will be achieved remains unclear at this time.

We will continue to liaise with the College over further developments during 2007-08.

Management has drafted an annual report to the Board of Management acting in its capacity as trustees of a charity, which will be discussed before the end of the current calendar year. This report will formally document how the College has met its charitable objectives during the year. This demonstrates management's awareness of the dual status and responsibility of the College as a further education institution and as a charity.

Board of Management report

The Board of Management report is a very comprehensive report on the College's activities and exceeds the requirements of SORP 2003. Management include commentary on the expected areas of financial position, capital investment and student numbers. In addition, comments are included on the following areas, demonstrating commitment to transparent public reporting:

- best value and social responsibility;
- responsiveness and consultation, in particular the involvement of the College and its staff in local community and planning groups in addition to the expected discussions with local authorities and Scottish Enterprise Glasgow, which are required by statute;
- joint working, including the continuing agreement with Glasgow City Council to share library and information technology facilities in Easterhouse;
- sustainable development, which is demonstrated by the introduction of an environmental management system to the new East End campus, which has a range of sustainable technologies to reduce energy consumption, including water re-cycling, bio-mass energy production, air-source heat pumps, high levels of insulation, photovoltaic cells, solar heating and both active and passive energy control systems); and
- environmental reporting.

The revised SORP, issued in 2007 and effective for the year ending 31 July 2008, requires the inclusion of an operating and financial review ("OFR") in the financial statements which should follow best practice as set out in the Reporting Statement 'the operating and financial review' issued by the Accounting Standards Board in January 2006. The impact on the College and the effort required to implement this change is significantly lessened as a result of the volume and nature of information currently reported. We have agreed to discuss the specific requirements of the revised SORP with management in advance of the 2007-08 audit.

Prevention and detection of fraud and irregularity

The College's financial regulations detail measures put in place to prevent instances of fraud. The College has a whistle blowing policy in place to encourage staff to bring suspected frauds to notice and to ensure that prompt and effective action is taken.

The College has an over-arching anti-fraud policy in addition to policies and procedures in individual financial and operational areas. However, staff were unable to find a copy during our audit fieldwork and the document has not been updated for a number of years. Management should ensure that the anti-fraud policy is readily available to all staff and that it is included in the system of regular review of other College policies.

Significant frauds would be reported to the appropriate board committee. Management has not reported any material instances of fraud or irregularity in 2006-07.

Standards of conduct

The College has comprehensive human resources policies and procedures which are readily accessible to staff on the intranet. There is also a formal register of interests for recording members of the board of management and senior managers' interests. This is regarded as best practice and assists in demonstrating consideration of independence in decision-making and the awarding of contracts.

Best Value

The 2006-07 planning guidance for further education colleges issued by Audit Scotland indicated that there was no requirement for auditors to undertake performance audit or other Best Value studies during the year.

The College utilises a best value approach developed as part of the Scottish Executive's efficient government initiative to satisfy publicly the requirements of the Financial Memorandum between the Board of Management and the Scottish Funding Council.

Financial statements audit

Audit opinion

On 11 December 2007 we issued an audit report expressing a qualified opinion on the financial statements of the College for the year ended 31 July 2007 and an unqualified opinion on the regularity of transactions reflected in those financial statements.

Qualified audit opinion

Financial reporting standard 17 'retirement benefits' ("FRS 17") paragraph nine states that '*Where more than one employer participates in a defined benefit scheme the employer should account for the scheme as a defined benefit scheme*'. This indicates that there is a presumption that a defined benefit scheme will be accounted for on a defined benefit basis unless one of the two possible exemption criteria is met, which are:

- employers contributions are set in relation to the current service period, i.e. not impacted by any past surplus or deficit of the fund; or
- the employer is unable to identify its share of the underlying assets and liabilities in the fund on a consistent basis.

The Board of Management accounts for the College's participation in the Strathclyde Pension Fund ("the Fund") on a defined contribution basis under FRS 17 in line with the treatment adopted in the prior year. The Board of Management believes that the College cannot identify its share of assets and liabilities in the Fund on a reasonable and consistent basis and that the College is therefore entitled to use the multi-employer exemption permitted by FRS 17, which allows a defined benefit scheme to be accounted for as it was a defined contribution scheme when a body cannot identify its share of the assets and liabilities in the pension scheme. The Board of Management has specifically considered this issue on a number of occasions and has concluded that, at present, a defined contribution approach is the most appropriate means of accounting for its participation in the Fund. These discussions have determined the Board of Management's accounting policy in these respects.

Consequently, the financial statements have been prepared on the basis of the accounting policy of charging pension costs to the income and expenditure account on the basis of contributions payable during the financial year.

In our view, the College's share of the underlying assets and liabilities in the Fund can be identified on a consistent and reasonable basis and its participation should therefore be accounted for as a defined benefit scheme. This conclusion has been reached by drawing on the work of our actuarial staff and has involved specific discussions with the scheme actuaries. The conclusion is based on consideration of the facts presented by the Fund's actuaries against the two specific exemptions outlined above:

- the common contribution rate takes into account any surplus or deficit in the Fund and differing contribution rates are calculated with regard to the circumstances of employers (or homogenous groups of employers) and allows for any surplus or deficit attributable to them;
- allocation of assets to individual employers can be performed on the basis that assets can be derived based on movements in the liabilities, which can be explicitly measured and allocated to individual employers, in addition to measurement of gains and losses on assets and liabilities, both of which are based on the experience of the individual employer during the year.

As a result, in our opinion, pension costs should be charged to the income and expenditure account on the basis of reflecting the cost of benefits earned in the period and its share of assets and liabilities in the Fund should be included within the balance sheet of the College.

Accounting for the College's participation in the Fund as a defined benefit pension scheme would increase the College's net assets at 31 July 2007 by £93,000 (2006: £545,000 decrease), increase its surplus for the year by £60,000 (2006: reduce the surplus by £13,000) and increase its total recognised gains and losses for the year by £579,000 (2006: £189,000).

Our audit opinion is qualified in respect of the adjustments and disclosures that would be required to comply with FRS 17.

In all other respects our opinion is unqualified. Our opinion on the regularity of transactions is also unqualified.

Except for the above adjustments and additional disclosures necessary to comply with FRS 17, the financial statements give a true and fair view of the state of affairs of the College as at 31 July 2007 and it is not believed that the absence of the adjustments has an impact on the College's underlying financial security.

Management has confirmed that they intend to review the appropriateness of the accounting treatment during 2007-08.

Regularity

There are no issues arising from the regularity audit. We have reviewed the minutes of the College's key committees, including the Board of Management and audit committee meetings. From these minutes, we have established that the College has sound procedures in place to ensure implementation of key guidance from the Scottish Funding Council, as well as other relevant laws and regulations.

Financial statements preparation

Management prepared draft financial statements and provided them to us in advance of the audit fieldwork. They were complete and prepared to a high standard. The Board of Management report was also presented to the College management team during the first week of October, resulting in minimal changes during or after the audit process. The standard of documentation prepared by the finance department to support the financial statements was of a high standard and available to the audit team on the first day of the fieldwork.

Fixed assets

East End campus

The East End campus was completed during the year. The total cost of £13.6 million, comprising balances brought forward of £8.5 million and additions during the year of £5.1 million, was transferred from assets under construction to land and buildings and depreciated from April 2007. The College accounts for fixed assets on a valuation basis under financial reporting standard 15 'tangible fixed assets', which requires that constructed assets are valued when they are brought into use. Management engaged an independent firm of chartered surveyors to value the East End campus, resulting in an increase of £417,380 compared to the cost of construction.

Shared services

The College has a shared services agreement with Glasgow City Council ("the Council") covering library services and information technology facilities in an area of the College's Easterhouse campus. During 2006-07 management considered the accounting requirements of FRS 15 and FRS 5 'reporting the substance of transactions'. They engaged external chartered surveyors to obtain a value of the right of access and confirmation of whether the agreement should impact the value at which the Easterhouse campus is carried in the financial statements. Written confirmation was received by management to confirm that the carrying value of the Easterhouse campus is appropriate and that the right of access given to the Council is offset by the corresponding benefit gained by the College through access to Council facilities. Management has disclosed the agreement in the financial statements. This accounting treatment is considered reasonable and meets the requirements of SORP 2003.

Report to those charged with governance

At the audit committee meeting on 4 December 2007 we discussed our "report to those charged with governance" which is required under International Auditing Standard 260. This dealt with relevant aspects of the College's financial statements production process, amendments to draft financial statements during the audit process, the treatment of uncorrected audit differences and the content of the representation letter to us.

Appendix – action plan

Priority rating for performance improvement observations raised		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the College or systems under consideration. The weakness may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the controls to meet their objectives in any significant way. These are less significant observations than grades one and two, but we still consider they merit attention.

No.	Issue and performance improvement observation	Management response	Officer and due date
1	The College's information technology security and contingency policies were last updated in 2004. Management should ensure that these are reviewed and updated on a regular basis to provide assurance that they meed the current needs of the organisation, particularly following recent structural changes at the Easterhouse campus and construction of the East End campus. *Grade two*	Accepted. The College will seek to review these policies during session 2007-08 for introduction early in session 2008-09.	Russell Boyd September 2008

No.	Issue and performance improvement observation	Management response	Officer and due date
2	The bank reconciliation for one of the access funds bank accounts at 31 October 2006 was not performed until January 2007. All bank reconciliations should be prepared and reviewed within five working days of the month end to demonstrate operation of this key control and mitigate the risk that errors are not identified and resolved in a timely manner. *Grade three*	The access fund accounts are not reconciled monthly as the bank does not provide bank statements for periods when there is no activity on the accounts. A reconciliation is prepared on receipt of the statement. This is considered adequate due to low value and volume of transactions. The maximum combined value is around £20,000 at the start of each period.	-
3	The College has a over-arching anti-fraud policy in addition to policies and procedures in individual financial and operational areas. However, staff were unable to find a copy during our audit fieldwork and the document has not been updated for a number of years. Management should ensure that the anti-fraud policy is readily available to all staff and that it is included in the system of regular review of other College policies. *Grade two*	The College will review its existing anti-fraud policy during academic / financial year 2007-08. The revised policy will be considered by the Board at its first meeting in session 2008-09 and implemented thereafter.	James Gow August 2008
4	The College staff organisational chart is not up to date. As a result, internal lines of reporting and accountability may not be clear to new members of staff. The chart should be reviewed to ensure that it is up to date and be readily available. *Grade three*	The College will update its organisational chart by end of January 2008,	Doreen Sneddon Human resources manager January 2008