Glasgow College of Nautical Studies
Report to the Board and the Auditor General for Scotland

Year ended 31 July 2009

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1 Executive Summary

Introduction

- The purpose of this report is to highlight and explain key issues arising from our audit of the financial statements of Glasgow College of Nautical Studies ('the College') for the year ended 31st July 2009.
- The matters raised in this report, are only those which have come to our attention arising from or relevant to our work that we believe need to be brought to your attention. Our audit work is designed to enable us to form an audit opinion on the financial statements of the College and it should not be relied upon to disclose all irregularities that may exist nor to disclose errors that are not material in relation to the financial statements.
- This report has been prepared solely for use by the Board of Management of Glasgow College of Nautical Studies and the Auditor General for Scotland.
- We have completed our audit work in respect of the financial statements for the year ended 31 July 2009 and will be issuing an unqualified audit opinion for the year.

Scope of Work

- The accounting rules and regulations applied to Further Education Colleges are specifically laid out in various documents as discussed in section 3 of this report. We can confirm that the College is in compliance with the regulations and disclosures required to be made in the financial statements in respect of these documents.

Corporate Governance Arrangements

- The corporate governance statement within the College's financial statements states that the College has been fully compliant with guidance on corporate governance for the year ended 31 July 2009. We identified no issues of concern in relation to fraud and irregularity nor did we identify any major errors or weaknesses during our audit. In general the College's systems of internal control appear to be adequate.

Compliance with Scottish Funding Council ('SFC') Accounts Direction

- We can confirm in preparing the financial statements the College has complied with the Accounts Direction for Scotland's colleges and universities issued under circular SFC/35/2008.

Conclusion

- The audit of Glasgow College of Nautical Studies was performed in accordance with relevant legal and regulatory requirements and with International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland. This report has been issued to College management and will be considered by the Audit Committee.

Acknowledgement

- The 2008/09 audit process brought us into contact with a number of staff within the College. We wish to place on record our appreciation of the co-operation extended to us by those personnel.

2 Introduction

Purpose of Report

- This report has been prepared in connection with our audit of the financial statements of the College for the year ended 31 July 2009. This report summarises the principal matters that have come to our attention during the course of the audit.

- The contents of the report should not be taken as reflecting the view of BDO LLP except where explicitly stated as being so. To a certain extent, the content of this report comprises general information which has been provided by, or is based on discussions with, the management of the College. Except to the extent necessary for the purposes of the audit, this information has not been independently verified.

- One of the purposes of this report is to record features of the year's activities, the way they are treated in the financial statements and the comments thereon provided to audit staff by the College's staff.

Audit Bodies

- The Auditor General, a royal appointment on the nomination of the Scottish Parliament, plays a key role in holding the Scottish public spending bodies to account for the proper, efficient and effective use of public money.

- Audit Scotland is an independent statutory body which was set up in April 2000 to provide assistance and support to the Accounts Commission and to the Auditor General for Scotland in the exercise of their respective functions. The Auditor General is responsible for securing the audit of the Scottish Executive, Further Education Colleges and other public bodies.

- BDO LLP was appointed by Audit Scotland as external auditor to Glasgow College of Nautical Studies for 5 years covering the financial years 2006/07 to 2010/11. This report summarises our audit work for 2008/09 and details how the requirements of the Statement of Responsibilities and the Code of Audit Practice have been met by the College and by BDO LLP.

College Responsibilities

- The College is publicly accountable for the conduct of business and the stewardship of funds under its control. The College's Board of Management is therefore responsible for:

  - establishing adequate corporate governance procedures;
  - ensuring funds from the SFC are used only for the purposes for which they have been given and in accordance with the Financial Memorandum with the SFC and any other conditions which the SFC may from time to time prescribe;
  - ensuring that there are appropriate financial and management controls in place to safeguard public funds and funds from other sources;
  - safeguarding the assets of the College and taking reasonable steps to prevent and detect fraud and other irregularities;
  - securing the economical, efficient and effective management of the College's resources and expenditure;
  - maintaining proper accounting records and preparing financial statements which give a true and fair view of the financial position of the College at the year-end and its income and expenditure for the year.

Auditors' Responsibilities and Approach

- We are required to report to the Board of Management of the College and to the Auditor General for Scotland on the financial statements of the College. Our responsibilities are to:

    - provide an opinion, to the extent required by the relevant authorities, on the financial statements of the College and the regularity of transactions in accordance with standards and guidance issued by the Auditing Practices Board.

    - review and report on the requirements of Audit Scotland's Code of Audit Practice (March 2007), regarding the College's corporate governance arrangements relating to:

        - the College's review of its systems of internal control

        - the prevention and detection of fraud and irregularity

        - standards of conduct, and prevention and detection of corruption

        - its financial position.

    - obtain an understanding of the accounting and internal control systems in place in the College sufficient to allow the audit to be planned and an effective audit approach developed.

- Our audit work is designed to enable us to form an audit opinion on the financial statements of the College and it should not be relied upon to disclose all irregularities that may exist nor to disclose errors that are not material in relation to the financial statements.

3 Scope of Work

- We took reasonable steps to plan and carry out the audit to ensure that the above responsibilities were met and that we complied with the requirements of Audit Scotland's Code of Audit Practice.

- In essence the scope of our work is similar to that applied to a limited company audit, however, the accounting rules and regulations applying to Further Education Colleges are specifically laid down in various documents as detailed below.

Financial Memorandum

- This memorandum sets out the terms and conditions under which the Scottish Funding Council will make payments to the Board of Management of Colleges of Further Education out of funds made available by the First Minister of Scotland. We can confirm the College fully complies with the terms and conditions of the memorandum.

Accounts Direction

- In preparing its annual accounts the College is required to comply with the directions of the Scottish Funding Council (SFC). The Accounts Direction is designed to ensure that disclosures in the financial statements of all colleges follow best practice. We can confirm the College's financial statements comply with the Accounts Direction.

Guidance on Audit

- Audit Scotland's Code of Audit Practice (March 2007) sets down Audit Scotland's requirements for both internal and external audits. In carrying out our audit work we are also required to comply with International Standards on Auditing (UK and Ireland) and to take cognisance of any relevant Practice Notes and other guidance and advice issued by the Auditing Practices Board. We also comply with relevant ethical standards and guidance issued or adopted by the relevant professional accountancy bodies and any supplementary guidance issued by Audit Scotland.

Statement of Recommended Practice (SORP)

- We can confirm that the financial statements of the College, are in general in compliance with the requirements of the 2007 SORP: Accounting for Further and Higher Education.

- Additional guidance on the content of the Operating and Financial Review (OFR), the inclusion of which is recommended within the 2007 SORP, was issued by the Scottish Funding Council on 2 October 2009. This guidance states that it would be helpful if a core set of performance indicators could be incorporated within the OFR to meet best practice and facilitate comparisons between the performances of different colleges. The College has taken cognisance of this guidance and has included the core set of performance indicators within its OFR.

- One of the key areas of emphasis within the 2007 SORP that has had an impact on the College is the College treatment of FRS 17:

  This year for the first time the College has elected to account for the Strathclyde Pension Fund (SPF) as a defined benefit fund per FRS 17 as the scheme's actuaries assessed that they were able to identify the College's share of the assets and liabilities on a fair and reasonable basis. This actuarial valuation shows that the College had an FRS 17 pension deficit of £2,129k as at 31 July 2009 which has now been shown as a liability on the balance sheet. The comparative figures have been restated accordingly with an FRS 17 liability having been introduced into the balance sheet as at 31 July 2008.

The College is accounting for the Scottish Teachers' Superannuation Scheme (STSS) as if it were a defined contribution scheme. This accounting treatment is consistent with the view taken by the scheme's actuaries.

4 Audit Findings

Preparation of Financial Statements

- The financial statements and the required working papers were ready for audit on 2 November 2009, in line with the agreed timetable. The working papers supplied were of a good standard.

Audit Opinion

- We are satisfied that the financial statements of the College present a true and fair view of its financial position as at 31 July 2009. Following approval of the financial statements by the Board of Management on 3 December 2009 our audit report expresses unqualified opinions on (i) the financial statements of the College for the year ended 31 July 2009 and (ii) regularity.

Financial Commentary

- This section summaries the main financial features and key movements from the prior year.

Income and expenditure account

- The College made a surplus of £144,000, 0.9% of total income (2007/08: £378,000 (as restated) 2.3%) in respect of the year ended 31 July 2009. The sector average for 2007/08 was 2.9%.

Income

- Total income decreased by £226,000 (1.4%). There has been a £53,000 increase in SFC grants with significant reductions of £137,000 and £155,000 in other grant income and investment income respectively.

- The table below summarises the main sources of income for 2008/09 and 2007/08.

	2008/09	**2007/08**	**2008/09**	**2007/08**
	£'000	**£'000**	**%**	**%**
Scottish Funding Council Grants	7,492	7,439	46%	45%
Tuition Fees and Education Contracts	5,810	5,728	36%	35%
Other Grant Income	185	322	1%	2%
Other Operating Income	2,536	2,605	15%	16%
Investment Income	314	469	2%	2%
Total Income	**16,337**	**16,563**	**100%**	**100%**

- The percentages of total income received from the various sources of income remain relatively consistent with 2007/08. The College is substantially less dependant on SFC Grants than other Colleges delivering over 45,000 WSUMs. From review of the 2007/08 SFC performance indicators, total SFC grant income is normally in the region of 76% for colleges in this category.

Expenditure

- Total expenditure increased by £7,000 in comparison to 2007/08. The most significant movement is in relation to an increase in staff costs of £467,000, although there have been reductions in other operating expenses of £683,000 to offset this. Other increases include a £116,000 increase in depreciation and a £107,000 increase in interest payable.

- The table below summarises the main sources of expenditure for 2008/09 and 2007/08.

	2008/09	2007/08	2008/09	2007/08
	£'000	£'000	%	%
Staff costs	11,587	11,120	71%	69%
Other Operating Expenses	3,709	4,392	23%	27%
Depreciation	775	659	5%	4%
Interest payable	122	15	1%	<1%
Total Expenditure	**16,193**	**16,186**	**100%**	**100%**

- Proportionately expenditure remains broadly in line with 2007/08.

Balance sheet

- Net assets at 31 July 2009 are £19,796,000 (31 July 2008: £20,422,000)

- The balance on the income and expenditure account carried forward as at 31 July 2009 is a surplus of £6,068,000 (31 July 2008: £5,330,000).

- The balance on revaluation reserve carried forward as at 31 July 2009 is a surplus of £12,537,000 (31 July 2008: surplus £12,935,000).

- The balance on the restricted reserve carried forward as at 31 July 2009 is £174,000 (31 July 2008: £171,000).

- The balance on the pension reserve carried forward as at 31 July 2009 is £2,129,000 (deficit) (31 July 2008: £96,000 (deficit) (as restated)).

- The balance on deferred capital grants carried forward as at 31 July 2009 is £3,146,000 (31 July 2008: £2,082,000).

Cash Flow

- During 2008/09 the College experienced a net outflow of cash of £177,000 (2007/08: inflow of £516,000).

Financial Forecasting

- The original budget for 2008-09 forecast an operating surplus for the year of £646,000. This was revised to £211,000 in the Financial Forecast Return 2009. There were various movements on forecast as set out below. Fluctuations in income have been in the main offset by a careful monitoring of costs.

Financial Forecasting

	2008/09
	£'000
2008-09 forecast outturn	211
Reduction in SFC grant income	(1,287)
Increase in tuition fees	840
Increase in other grant income	185
Reduction in other income	(90)
Increase in investment income	29
Increase in payroll costs	(240)
Reduction in operating costs	625
Increase in depreciation	(7)
Increase in interest payable	(122)
2008/09 actual outturn at 31 July 2009	**144**

- The following table summarises the forecast income, expenditure and cash balances for the College for 2009/10.

	£'000
Income	15,892
Expenditure	16,168
Forecast deficit for the year ending 31 July 2010	(276)
Cash balance at 31 July 2009	6,939
Forecast movement in cash during 2009/10	733
Resulting cash balance at 31 July 2010	7,672

Funding Council Grant income is expected to fall in 2009/10 per the Financial Forecast Return due to the strategic growth program in association with the SFC coming to an end in 2008/09. ESF funding is also expected to decrease significantly. As the college continues to overachieve in relation to funded WSUMs, the staff costs are expected to remain high and produce a deficit in 2009/10. The forecast cash movement is positive as the forecast deficit for the year includes a depreciation charge of £683k.

Going Concern Basis

- In preparing the accounts on a going concern basis the Board of Management is satisfied that SFC will provide sufficient funding to enable the College to operate for at least twelve months from 3 December 2009.

Performance Indicators

- The Scottish Further Education Funding Council's ('SFEFC') financial security campaign was announced in December 2002, its principal objective being that all colleges would report underlying operating surpluses by the end of 2005-06. Financial security is defined as the ability, on a continuing basis, to generate operating surpluses reliably and as planned, and through that accumulate a reasonable level of financial reserves. The college must also generate sufficient cash to finance its operations and meet its liabilities; regular operating surpluses would ensure this.

- Under the terms of the financial memorandum between SFC and the College, it is the responsibility of the governing body "*to ensure that the institution strives to achieve best value from its use of public funds from all sources*". It is intended that the financial performance indicators used by the Funding Council, when set alongside other performance data, will support the college in seeking best value.

- The table opposite has been produced from the data published by the Funding Council in respect of the Financial Statements as at 31 July 2008. The formulae have then been applied to the 2008/09 Financial Statements.

	GCNS Factor 2008-09	GCNS Factor 2007-08	Group Average Factor 2007-08	Sector Average Factor 2007-08
Underlying operating surplus % of total income	0.4%	2.3%	3.7%	2.9%
Operating surplus % of total income	0.4%	2.3%	0.4%	1.3%
Designated plus I&E reserves % of total income	37.1%	32.2%	55.7%	22.9%
Historical cost surplus/ (deficit) % of total income	2.8%	3.8%	26.6%	8.9%
Current assets: Current liabilities	3.7	2.9	1.6	1.7
Interest Cover	0.5	25.2	5.4	3.9

Grant in Aid Funding

- The College had a WSUMS target for 2008/09 of 40,272. A final WSUM's figure of 47,320 was achieved, exceeding the target by 7,048 WSUMs. The College will not be required to refund any grant in aid funding.

Corporate Governance Framework and Statement

- The Board of Management has seven formally constituted committees which have specific terms of reference and act with delegated authority from the Board.

- We reviewed the College's corporate governance arrangements. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of the organisation. The college has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.

- From our review of Corporate Governance arrangements within the College we do not believe the Corporate Governance statement to be misleading or inconsistent with other information made available to us during the audit process.

System of Internal Control

- A review and assessment of the College's corporate governance arrangements was carried out. This assessment included a review of the College's committee minutes and completion of a number of standard checklists. The checklists cover issues relating to systems of internal control, arrangements for the prevention and detection of fraud and corruption, standards of conduct, issues of legality and the College's financial position.

- The College, in accordance with the Accounts Direction, has included in its financial statements, a statement covering the responsibilities of the Board of Management in relation to corporate governance.

- Our review of the statement concluded that it complies with guidance and is not inconsistent with other information we are aware of from our audit.

Prevention and detection of Fraud and Corruption

- The College's arrangements for preventing and detecting fraud and corruption were assessed during the audit. This assessment showed the arrangements to be operating satisfactorily. No frauds were identified by the College in 2008/09.

Review of Internal Audit

- Internal audit is a key element of the internal control system set up by management. A strong internal audit function is necessary to ensure the continuing effectiveness of the internal control systems established. The College therefore, needs to have in place a properly resourced internal audit service of good quality.

- Internal audit services are provided by Scott Moncrieff. An assessment was made of the adequacy of the internal audit input and it was concluded that we as external auditors were able to place reliance on the work of internal audit. Accordingly a certain amount of reliance was placed on the work of internal audit in the following areas during 2008/2009.

    - Budgetary control
    - Payroll and expenses
    - Audit of FES return

In November 2009, Scott Moncrieff issued the internal audit report for the year ended 31 July 2009. This concluded that, the College has an adequate framework of control, based on the systems examined.

Misstatements

- Some balance sheet reallocations were made following our audit work with the net effect on income and expenditure account being nil.
- There were no unadjusted misstatements of any significance uncovered in the course of our audit work.

Accounting and Internal Control System Weaknesses

- Two internal control systems weaknesses were identified during the course of our audit. These have been listed in section 5 of this report.

Qualitative Aspect of the College's Accounting Practice and Financial Reporting

- Our overall assessment, based on our work undertaken, is that the financial procedures of the College are adequate to enable annual financial statements to be produced in the prescribed form.

FRS 17 retirement benefits

- This standard was published in November 2000 introducing significant changes to the way in which colleges should account for defined benefit pension schemes. Full implementation of FRS17 – 'Retirement Benefits' was mandatory from 2005/06 year ends. The College participates in the Scottish Teachers Superannuation Scheme ('STSS') and the Strathclyde Pension Fund ('SPF') which are defined benefit pension schemes. All colleges treat the STSS scheme as a defined contribution scheme as there is general agreement that they are unable to identify their share of the scheme's assets and liabilities.
- In relation to the SPF scheme assets are currently apportioned based on the liability profile though employer assets have been tracked for each employer since 2002. The actuaries provided information on the College's interests in the scheme as at 31 July 2009. Management took the view that this information was sufficiently robust for it to account for its participation on a defined benefit basis.
- This was the first year in which the College incorporated the provisions of FRS 17 in the calculation of the pension liability. A prior year adjustment was made to introduce a pension asset and pensions reserve of £390,000 onto the balance sheet as at 1 August 2007. The 2007/08 financial statements have been adjusted in order to incorporate an FRS 17 pension liability of £96,000 as at 31 July 2008.
- The pension liability calculated with reference to FRS 17 in at 31 July 2009 was £2,129,000 (31 July 2008: £96,000).

Early retirement provision

- Included in the balance sheet is a provision for the cost of providing for early retirals. The College recalculated this early retirement provision using the actuarial tables guidance issued by SFC and an appropriate interest rate. This provision was included on the balance sheet as a provision for liabilities separate from the FRS 17 pension liability referred to above. This treatment is in accordance with SFC guidance on the completion of 2008/09 financial statements.

New Campus Glasgow Project

- In conjunction with three other colleges in Glasgow, the College is currently working on the New Campus Glasgow project. The college has capitalised their third share of the assets purchased on behalf of the New Campus Glasgow project in the year. The total capitalised in the College accounts in relation to this project was £1,158,000.

Financial Outturn

- Audit Scotland and SFC expect close scrutiny of the College's financial forecasting and achievement of the forecast financial outturn for 2008/09. Per the financial forecast return for the year 2008/09 the college anticipated that a surplus of £211,000 would be achieved. The final outturn per the draft financial statements shows a surplus for the year of £144,000.

Recognition of ESF income

- The College is accounting for ESF income in its income and expenditure account by matching income against relevant costs in accordance with its accounting policy. During the course of our audit work we uncovered no breaches of the conditions attached to the ESF claims and we received assurances from management that they were unaware of any breaches.

5 Internal control systems weaknesses

Credit control procedures

- When auditing trade debtors we noted that 29% of trade debtors (£206k before any bad debt provision) related to periods prior to April 2009.

- We recommend that the College credit control procedures are reviewed with a view to substantially reducing old uncollected debt.

Management response

- Accepted. In addition to increasing our bad debt provision to £80K we will review further the status of old, uncollected debt. The introduction of a '90 day 'rule for the sending of existing and new debt to debt recovery agencies together with increased dialogue with Heads of Department should minimise the need for future provisions.

Bank reconciliations

- Bank reconciliations take a considerable amount of time to complete and in some instances were not completed by the end of the month following the reconciliation date. Management attribute this to the volume of transactions and the number of unidentified receipts with which no remittance advices are provided.

- We recommend that College procedures be reviewed with a view to reducing the number of unidentified transactions which in turn should enable the bank reconciliations to be completed timeously.

Management response

- Accepted. Financial Controller to review list of unidentified items on a weekly basis with Senior Accountant An additional member of staff (0.5WTE) recently appointed with a remit to resolve such queries should reduce outstanding items.

6 Other Matters

- We have no other matters to report.

BDO LLP

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3 December 2009