

Scottish Further and Higher Education Funding Council

Report on the 2008/09 Audit

5 August 2009



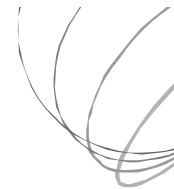
AUDIT SCOTLAND

Scottish Further and Higher Education Funding Council

Report on the 2008/09 Audit

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Key messages

In 2008/09 we looked at the key strategic and financial risks being faced by the Scottish Further and Higher Education Funding Council. We audited the financial statements and we also reviewed the use of resources and aspects of performance management and governance. This report sets out our key findings.

Financial statements

We have given an unqualified opinion on the financial statements of the Scottish Further and Higher Education Funding Council for 2008/09. We have also concluded that in all material respects, the expenditure and receipts shown in the financial statements were incurred or applied in accordance with applicable enactments and relevant guidance, issued by Scottish Ministers.

Financial position and use of resources

The Scottish Further and Higher Education Funding Council had a deficit of £3.8 million in 2008/09 which was covered by a transfer from reserves. This is the difference between the expenditure for the year of £1,765.3 million and the government funding received of £1,761.5 million. The Scottish Further and Higher Education Funding Council operated within the budget limits set by the Scottish Government for capital expenditure and operating expenditure.

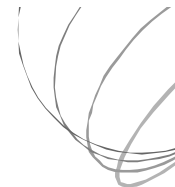
Scottish Ministers have agreed a budget of **£1,702.7** million for 2009/10, a **decrease of 3.3%** on 2008/09.

The Scottish Further and Higher Education Funding Council original targets under the Efficient Government Plan for the three years to 2007/08 were £95 million of cash-releasing and time-releasing efficiencies. The actual efficiency savings achieved to 31 July 2007 were £46 million of cash-releasing and £58 million of time-releasing efficiencies, giving a total of £104 million. A further £39 million of cash-releasing and £73 million time-releasing savings are anticipated in the year to 31 July 2008. Future efficiency savings are set at 2% per annum, as part of the budget settlement from the Scottish Government for the next three years. The delivery of these efficiency savings together with other budget pressures in the medium term are a significant challenge for the Scottish Further and Higher Education Funding Council.

Governance and accountability

Corporate Governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. Overall the corporate governance and control arrangements for the Scottish Further and Higher Education Funding Council operated satisfactorily during the year, as reflected in the Statement on Internal Control.

We examined the key financial systems which underpin the organisation's control environment. We concluded that financial systems and procedures operated sufficiently well to enable us to place reliance on them.



Looking forward

The final part of our report notes some key risk areas and issues for the Scottish Further and Higher Education Funding Council going forward. We have highlighted a number of national issues which affect all public sector bodies including the Scottish Further and Higher Education Funding Council, including the National Performance Framework and the introduction of Scotland Performs; the impact of international financial reporting standards; and the review of data handling arrangement in public bodies across Scotland. The Scottish Further and Higher Education Funding Council also faces significant financial pressure over the next three years to achieve financial balance and achieve efficiencies. The effects of the recession on Further and Higher Education Institutions, particularly pay pressures and the decline of the property values, as well as the introduction of reforms arising out of the New Horizons Report, will all continue to represent a significant challenge to the Scottish Further and Higher Education Funding Council.

The assistance and co-operation given to us by Council members and staff during our audit is gratefully acknowledged.

Audit Scotland
5 August 2009



Introduction

1. This report summarises the findings from our 2008/09 audit of the Scottish Further and Higher Education Funding Council. The scope of the audit was set out in our Audit Plan, which was presented to the Audit and Compliance Committee on 19 November 2009. This plan set out our views on the key business risks facing the organisation and described the work we planned to carry out on financial statements, performance and governance. Appendix B details our findings from the review of the main risks.
2. We have issued a range of reports this year, and we briefly touch on the key issues we raised in this report. Each report set out our detailed findings and recommendations and the Council's agreed response. Appendix A of this report sets out the key risks highlighted in this report and the action planned by management to address them.
3. Best value duties apply across the public sector and, in central government, best value is a formal duty on all accountable officers. Audit Scotland has adopted a generic framework for the audit of best value across the public sector and throughout this report we comment on aspects of the Scottish Further and Higher Education Funding Council arrangements.
4. Our comments are made on the basis of information made available in the course of the annual audit. We do not make an overall best value judgement because we do not have enough evidence to conclude on all relevant areas. Our intention is to build up the corporate assessment over time. This report is the first step towards that goal.
5. Another building block for our assessment of best value is the national study programme carried out by Audit Scotland on behalf of both the Auditor General for Scotland and the Accounts Commission. We mention the key findings from all relevant reports, and the implications for the Scottish Further and Higher Education Funding Council, throughout this report. Full copies of the study reports can be obtained from Audit Scotland's website, www.audit-scotland.gov.uk.
6. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by management and Council members of the Scottish Further and Higher Education Funding Council during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website.



Financial Statements

7. In this section we summarise key outcomes from our audit of the Scottish Further and Higher Education Funding Council's financial statements for 2008/09 and the accounting issues faced. The financial statements are an essential means by which the organisation accounts for its stewardship of the resources available to it and its financial performance in the use of those resources.

Our responsibilities

8. We audit the financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position of the Scottish Further and Higher Education Funding Council and its expenditure and income for the period in question;
 - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
 - the consistency of the information which comprises the Management Commentary and the unaudited part of the Remuneration Report included in the Annual Report with the financial statements; and
 - the regularity of the expenditure and receipts.
9. We also review the statement on internal control by:
 - considering the adequacy of the process put in place by the Chief Executive as Accountable Officer to obtain assurances on systems of internal control;
 - assessing whether disclosures in the statement are consistent with our knowledge of the Scottish Further and Higher Education Funding Council.

Overall conclusion

10. We have given an unqualified opinion on the financial statements of the Scottish Further and Higher Education Funding Council for 2008/09.
11. As agreed the unaudited accounts were provided to us on 5 May 2009, supported by a comprehensive working paper package. We concluded our audit within the agreed timetable and provided our opinion to the Audit and Compliance Committee on 5 August 2009 as timetabled.



Issues arising from the audit

12. As required by auditing standards we report to the Audit and Compliance Committee that the main issues arising from our audit of the financial statements. The key issues were as follows:

WSUM data reviews

13. The risk of errors in data submitted by institutions to the Scottish Further and Higher Education Funding Council has been removed from the current Risk Register. During our audit we reviewed the effectiveness of the Scottish Further and Higher Education Funding Council's rolling programme of inspection visits which have been subsequently suspended after the issue of ineligible college courses. We found that although the reports resulting from these visits identified weaknesses in college processes, they did not make suggestions for improvement or result in follow up action that ensured that these weaknesses had been remedied.

Action Point 1

Grant clawback

14. The Scottish Further and Higher Education Funding Council are currently discussing a clawback from a college relating to payments for courses which have been deemed ineligible. As we consider this is a material amount in terms of disclosure, we consider that it should be reflected in the accounts to comply with the Financial Reporting Manual and FRS12.
15. A grant clawback for £304,000 from a university had been omitted from the balance sheet.

Early retirement costs provision

16. There is no provision for early retirement costs in the financial statements although there were five individuals at the 2008/09 year end to whom the Scottish Further and Higher Education Funding Council was committed to make early retirement payments. In the absence of this provision estimated at £152,000, the Scottish Further and Higher Education Funding Council's balance sheet is non-compliant with FRS 12 *Provisions, Contingent Liabilities and Contingent Assets*.

Fixed asset economic lives

17. Over £1 million of the £1.5 million of fixed assets in the Fixed Assets Register are still in use but have been fully depreciated, suggesting that fixed asset useful economic lives are not realistic. We recommend that officers review the appropriateness of the current policy of economic lives of assets in time for the 2009/10 accounts.



Additional long-term borrowing consent for property development

18. Jewel and Esk College was due to receive proceeds from the sale of the Eskbank Campus as part of the development of its new campus. The subsequent decline in the commercial property market created difficulties for the developer in financing the agreement. The Scottish Further and Higher Education Funding Council granted long-term borrowing consent to the College to meet the shortfall. We note that additional loan support will be necessary and that the loan will not be underwritten by the Scottish Further and Higher Education Funding Council in accordance with its Financial Memorandum.

Management Letter

19. A management letter with minor items arising out of the final audit process will be produced in due course together with an action plan. The items have been discussed and agreed with management at our wash-up meeting on 25 June. The major points raised include the items discussed at paragraphs 15 to 17. These will be followed up in 2009/10 to confirm that improvements have been made.

Regularity

20. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors that requires us to certify that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers. We have been able to address the requirements of the regularity assertion through a range of procedures, including written assurances from the Accountable Officer as to his view on adherence to enactments and guidance. No significant issues were identified for disclosure.

International financial reporting standards (IFRS)

21. As announced by the Chancellor in the 2008 Budget report on 12 March 2008, Government departments and other public sector bodies will report using International Financial Reporting Standards (IFRS) from 2009/10. The Scottish Government announced on 25 April 2008 that all Scottish Government Departments, Executive Agencies, Health Bodies and Non-Departmental Public Bodies would be required to produce shadow IFRS based accounts for financial year 2008/09. This was to include a restated balance sheet as at 1 April 2008.
22. In terms of the audit of the IFRS opening balance sheet at 1 April 2008, there were two key dates to achieve as outlined below:
- **28 November 2008** – opening 2008 IFRS-based balance sheet were to be presented to auditors for dry-run audit



- **28 February 2009** – dry-run audit of opening balances was to be completed, resulting in a letter to management highlighting the work done, auditors' findings and areas for further work.
23. The opening balance sheet and supporting documentation were submitted by the Scottish Further and Higher Education Funding Council for audit for review by the deadline date of 28 November 2008. The restated balance sheet and supporting working papers were comprehensive.
24. We made some recommendations for the delivery of the next stage of IFRS reporting – the production of the shadow accounts for 2008/09, and will consider progress on these when we review the shadow accounts later in 2009. These included:
- **Financial Instruments** – the Scottish Further and Higher Education Funding Council should continue to review assets and liabilities in order to ensure that all financial instruments are recognised, presented, measured and disclosed in accordance with IAS 39 Financial Instruments: Recognition & Measurement; and
 - **Leases** – the Scottish Further and Higher Education Funding Council will have to continue to monitor material contracts to ensure leases are correctly classified, and adapt the disclosure note on operating lease payments to comply with IAS 17 Leases.



Use of Resources

25. Sound management and use of resources (people, money and assets) to deliver strategic objectives is a key feature of best value. This section sets out our main findings from a review of the Scottish Further and Higher Education Funding Council:
- financial position;
 - financial management; and
 - management and use of information and communications technology (ICT).
26. We also refer to National Studies carried out by Audit Scotland that are relevant to the operations of the Scottish Further and Higher Education Funding Council.

Financial Position

Outturn 2008/09

27. The Scottish Further and Higher Education Funding Council is funded on a financial year basis but distributes funds to institutions on an academic year basis (i.e. from August to July each year). The level of funds distributed in any financial year therefore depends on the expenditure profiles of the relevant two overlapping academic years. Expenditure in any financial year can be higher or lower than the level of funding provided for that year.
28. **Operating Cost Statement** - For 2008/09 the Scottish Further and Higher Education Funding Council had a deficit of £3.8 million. This is the difference between the total expenditure for the year of £1,765.3 million and the funding received from the Scottish Government of £1,761.5 million. Where expenditure exceeds the funds provided, the excess is funded from the reserves held for distribution at the end of the previous financial year.
29. The total grant-in-aid received in 2008/09 comprised £1,752 million for distribution to Higher Education Institutions and Colleges (2007/08: £1,837 million) and £9.2 million for the Scottish Further and Higher Education Funding Council's running costs (2007/08: £8.4 million). The Scottish Further and Higher Education Funding Council's net expenditure on running costs was £8.9 million, resulting in a £0.3 million increase to the running cost reserve.
30. **Balance Sheet** - The Scottish Further and Higher Education Funding Council's balance sheet at 31 March 2009 shows net assets of £25.9 million (31 March 2008 net assets of £29.7 million). The



movement is caused by the deficit described above. The FReM requirement to account for grant-in-aid as a credit to reserves has resulted in expenditure less other operating income for the year of £1,765 million (2007/08: £1,829 million). The grant-in-aid and other grants credited to reserves for the year was £1,762 million (2007/08: £1,846 million). There has been a reduction in total reserves of £3.8 million.

31. The Scottish Further and Higher Education Funding Council operated within the cash limited allocations of funds for distribution and running costs provided by the Scottish Government. The excess of expenditure over income of £3.8 million was funded from the opening reserves held for distribution at 31 March 2008 – see exhibit 1 below:

Exhibit 1 – Performance against funding allocation 2008/09 (£ million)

Limits	Allocation	Actual Outturn	Difference
Funding for institutions	1,752.3	1,756.4	4.1
Running costs	9.2	8.9	(0.3)
Total	1,761.5	1,765.3	3.8

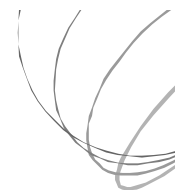
Financial sustainability and the 2009/10 budget

32. Scottish Ministers have agreed a grant-in-aid budget for the Scottish Further and Higher Education Funding Council of £1,703 million for 2009/10. This comprises:

Exhibit 2 – 2009/10 Resource Plan (£ million)

Limits	Budget
Current funding for Further Education Colleges	564.6
Capital Grants for Further Education Colleges	82.9
Current funding for Higher Education Institutions	944.6
Capital Grants for Higher Education Institutions	101.7
SFC Running Costs	8.9
Total	1,702.7

33. The Scottish Further and Higher Education Funding Council is expected to achieve 2% of efficiency savings per year from 2009/10 to 2011/12. Delivering efficiencies year on year while absorbing pay inflation and other cost pressures represents a significant challenge for the organisation.



Management and use of ICT

34. As part of the 2008/09 audit we had planned to carry out a 'Your Business @ Risk' survey of knowledge and attitudes to data security amongst Scottish Further and Higher Education Funding Council staff. We had originally planned to report the results in August. However, due to the decision by the Scottish Further and Higher Education Funding Council to allow additional time to complete the survey to increase the participation rate, we will not be able to conclude the report until September.

National Studies

35. Audit Scotland published three national studies relevant to the Scottish Further and Higher Education Funding Council's use of resources. These were *Use of consultancy services*, *Improving energy efficiency* and *Improving public sector purchasing*.

Use of consultancy services

36. Although the Scottish Further and Higher Education Funding Council was not involved in the field work for the national study that Audit Scotland carried out into the use of consultancy services, the lessons drawn from this study are relevant to the Council's operations.
37. The overall aim of the study was to review central government's use of consultancy services and to make recommendations to improve how the public sector's use consultants' knowledge, skills and resources to help deliver new services and initiatives quickly and expertly. The key findings were as follows:
- The public sector is strengthening the way it buys goods and services;
 - Central government does not have a clear strategy for its use of consultants or for linking use to its priorities or financial and workforce plans;
 - Central government could improve how it manages consultancy projects through more consistent and formal evaluation of consultants' work and learning more from them; and
 - Central government could make savings of up to £13 million a year through better planning and buying of consultancy services.
38. The report made a number of specific recommendations for public bodies. The key ones are:
- confirm they have clear processes for approving and recording the use of consultants and monitoring progress, and reinforce these as required;



- plan their use of consultancy services when developing their forward work programme to ensure that consultants are used where their knowledge and skills bring greatest value for money;
- always evaluate the option to use consultants against the option to use their own staff;
- gather and share consistent information on the consultancy skills bought and why consultants are used;
- select and use the most economical competition routes by using framework agreements, restricted competitions and closed tendering approaches when appropriate;
- evaluate the work of consultants more systematically and share findings from these reviews; and
- work closely with consultants to increase assurance on quality and make use of opportunities to learn from consultants and ensure knowledge transfer, where appropriate.

Improving energy efficiency

39. The Scottish Further and Higher Education Funding Council was one of the bodies which completed an electronic survey on its actions to improve energy efficiency, as part of an Audit Scotland national study. The study assessed how councils, NHS bodies and central government bodies were improving energy efficiency in relation to buildings and transport use. This included examination of a range of issues including whether public bodies demonstrate commitment to improving energy efficiency; how public bodies are performing against their objectives and targets for improving energy efficiency; and if public bodies are delivering continuous improvement in this area. The key findings from the study were:

- Funding has been made available by the Scottish Government and public bodies to improve energy efficiency. While energy consumption in buildings has fallen, spending on energy increased in the three years to 2006/07;
- There is a need for stronger leadership by the Scottish Government and within public bodies to improve energy efficiency and ensure that the necessary cultural and behavioural changes are made;
- A robust strategy is central to the coordination of activities to improve energy efficiency, however, there are inconsistencies in the quality of strategies being implemented; and
- There is a lack of formal monitoring and reporting of progress in improving energy efficiency by public bodies and the Scottish Government.



Improving public sector purchasing

40. The Scottish Further and Higher Education Funding Council and other bodies, including Advanced Procurement for Universities and Colleges Ltd. (APUC), were consulted as part of the information gathering process to produce the Audit Scotland report *Improving Public Sector Purchasing*. This report was published on 23 July and provided a position statement on progress made by the Public Procurement Reform Programme, which aimed at improving purchasing practice and making savings of about three per cent a year.
41. The report finds that the public sector in Scotland is improving its purchasing and has estimated it has saved a total of £327 million in the first two years of the Programme, which has cost £61 million so far to implement.
42. Because of the public sector's size and combined purchasing power, there is potential for it to buy goods and services more efficiently and deliver more significant savings through increased collaboration and better management. There has been progress in recent years but it has varied across the country and been slower than planned.
43. The report recommended that the use of collaborative contracts in the public sector should increase. These are a key feature of the Programme, but are being developed more slowly than expected. The health sector has been the most successful in this, introducing 150 new contracts and saving £54 million in the two years to 2007/08. Public bodies also need to ensure that staff have the appropriate skills and that better information and management systems are in place to facilitate more effective purchasing.
44. Audit Scotland will follow up this report with further audit work on public sector purchasing.

Future studies

45. Later in 2009, Audit Scotland will be publishing *Delivering Efficiencies within the Public Sector* which will be relevant to the Scottish Further and Higher Education Funding Council. The report will provide an overview of the Scottish Government's 2005/06 - 2007/08 Efficient Government Initiative and will consider the extent to which public bodies are set up to deliver year on year efficiency savings.
46. Feedback relating to the Scottish Further and Higher Education Funding Council will be provided in due course where appropriate.



Governance and Accountability

47. High standards of governance and accountability, with effective structures and processes to govern decision-making and balanced reporting of performance to the public, are fundamental features of best value. This section sets out our findings arising from a review of the Scottish Further and Higher Education Funding Council arrangements.
48. Increasingly services are being delivered across the public sector through partnership working, sometimes involving complex governance and accountability arrangements. Best value characteristics also include effective partnership working to deliver sustained improvements in outcomes.

Overview of arrangements

49. This year we reviewed:
- key systems of internal control
 - internal audit
 - arrangements for the prevention and detection of fraud and irregularity, including standards of conduct.
50. We also refer to a National Study being carried out by Audit Scotland that is relevant to the operations of the Scottish Further and Higher Education Funding Council.
51. Our overall conclusion is that arrangements within the Scottish Further and Higher Education Funding Council are sound and have operated through 2008/09. We report that key controls were operating effectively, with the exception of checks on WSUM accuracy (paragraph 13), and that the Scottish Further and Higher Education Funding Council has adequate systems of internal control in place.

Systems of internal control

52. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In their annual report for 2008/09 KPMG, the internal auditors, are due to provide their opinion based on the internal audit work undertaken during the year. We will review their findings and take them into account in formulating our audit opinion.



53. As part of our audit we reviewed the high level controls in a number of the Scottish Further and Higher Education Funding Council's systems that impact on the financial statements. This audit work covered a number of areas including six main systems: main accounting, grants payable, staff costs, non-payroll expenditure, cash and bank and budgetary control. This assessment involved confirmation of management arrangements in each particular system followed by a walk through of sample data to ensure that the controls identified are in place and operating effectively. A number of minor items were reported in our Internal Controls Report and Interim Management Letter.

Statement on Internal Control

54. The Statement on Internal Control provided by the Scottish Further and Higher Education Funding Council Accountable Officer reflected the main findings from both external and internal audit work. This recorded management's responsibility for maintaining a sound system of internal control and set out the Scottish Further and Higher Education Funding Council approach to this.

Internal Audit

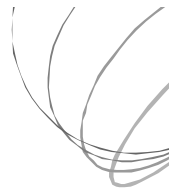
55. The establishment and operation of an effective internal audit function forms a key element of effective governance and stewardship. We therefore seek to rely on the work of internal audit wherever possible and as part of our risk assessment and planning process for the 2008/09 audit we assessed whether we could place reliance on the Scottish Further and Higher Education Funding Council internal audit function. We concluded that KPMG operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in number of areas during 2008/09, as we anticipated in our annual audit plan. This included reliance on aspects of internal audit's systems work to avoid duplication of effort.

Prevention and detection of fraud and irregularities

56. The Scottish Further and Higher Education Funding Council has appropriate arrangements in place to prevent and detect fraud, inappropriate conduct and corruption, including policies and codes of conduct for staff and Council members.

National Studies

57. In 2010, Audit Scotland will be publishing a national study on the role of Boards which will be relevant to the governance of the Scottish Further and Higher Education Funding Council.
58. Boards play a crucial role in ensuring that governance standards are maintained in public sector organisations. There are recent examples of the failure of public sector organisations to establish an adequate Board. We will assess how Board members are selected and whether the membership of



Boards is appropriate. In this study we will also review how the performance of Boards is measured and the arrangements for induction and training for non-executive members.

59. Feedback relating to the Scottish Further and Higher Education Funding Council will be provided in due course where appropriate.



Performance

60. Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance and value for money issues. Key features of best value include:

- setting a clear vision of what the organisation wants to achieve, backed up by plans and strategies to secure improvement, with resources aligned to support their delivery;
- a performance management culture which is embedded throughout the organisation and a performance management framework which is comprehensive and supports the delivery of improved outcomes.

61. In this section we comment on:

- the Scottish Further and Higher Education Funding Council corporate plan;
- performance against targets;
- performance management arrangements;
- risk management; and
- the Scottish Further and Higher Education Funding Council efficiency programme.

Vision and strategic direction

62. The Scottish Further and Higher Education Funding Council published its corporate plan for 2006 – 2009 in November 2006. The plan focused on seven key aims:

- Scotland's colleges and universities to offer fair access to a diverse range of learning programmes;
- Scotland's colleges to offer learning provision and programmes that are relevant to student lives and careers, society and the economy;
- Scotland's colleges and universities to offer high quality learning provision and programmes;
- Scotland's universities to provide a high quality and internationally competitive research base;



- Scotland's colleges and universities to generate effective knowledge exchange that stimulates innovation and development in public and private sector organisations and enterprises;
 - Scotland's colleges and universities to support Scotland's international ambitions; and
 - Scotland's colleges and universities and Funding Council to be highly effective, world-class organisations.
63. Following a period of consultation with stakeholder groups, a new Corporate Plan 2009/12 was launched by the Scottish Further and Higher Education Funding Council during the summer. The new Plan identifies seven outcomes to be delivered by the Scottish Further and Higher Education Funding Council and its partners; these outcomes map to the Government's National Performance Framework.

Performance overview

64. The Scottish Further and Higher Education Funding Council's 2008/09 Annual Report highlights some activities linked to the above Corporate Plan aims that have been undertaken during the year but does not report the performance of the Scottish Further and Higher Education Funding Council against its Corporate Plan aims.
65. The Scottish Further and Higher Education Funding Council established a performance measurement framework to measure performance against the Corporate Plan's aims. The management commentary gives details of the financial performance of the Scottish Further and Higher Education Funding Council. Although the management commentary describes the levels of activity it does not report the performance against the performance measures agreed in the 2006-09 corporate plan. Performance against these measures will be reported separately by the Scottish Further and Higher Education Funding Council in a separate Performance Evaluation which is due to be published later this year.

Performance management

66. The Scottish Further and Higher Education Funding Council's Board meets nine times per annum and considers the organisation's performance with feedback provided by its nine specialised committees. Quarterly monitoring information is submitted to the Scottish Government.

Risk management

67. There are number of key challenges and risks for the Scottish Further and Higher Education Funding Council in delivering its plan. The Council has put in place robust systems for the identification and management of risk with the adoption of a single corporate risk register which identifies the high-level business risks to the Council and the controls or actions in place to manage each risk. The Audit and



Compliance Committee manages the risk register on behalf of Council. The challenge for the Council will be to continue to embed a risk aware culture within the organisation for the future management of existing and emerging risks in the medium to long term.

68. The main risk areas are:

- **Implementation of New Horizons proposals** – The Scottish Further and Higher Education Funding Council has embarked on a 3 year implementation plan which will see a new university funding mechanism in place. There are a range of risks associated with this process in terms of the formulation, development and implementation of funding policy and the risk that the New Horizons proposals fail to deliver against the outcomes identified in the new Corporate Plan.
- **The impact of the recession on the sector** – As unemployment rises, demand for college and university places and hardship support will increase. The financial health of colleges and universities is likely to come under increased pressure as budgets are tightened and capital projects are impacted by the downturn in the property market.
- **Monitoring the eligibility of funding requests and institutional compliance with grant conditions** – During the year the Scottish Further and Higher Education Funding Council identified some courses, funded in previous years, which were subsequently found to be ineligible. The Scottish Further and Higher Education Funding Council must ensure its funding and monitoring processes are sufficiently robust to mitigate this risk.

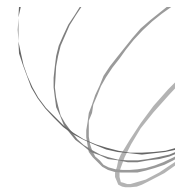
69. These risk areas are complex and comprise multiple issues which will require careful management to resolve. We have continued to monitor the Council's progress in each of these areas over the course of the year.

Efficiency

70. The Scottish Further and Higher Education Funding Council target for the Efficient Government Plan for the three years to 2007/08 was £95 million of efficiency savings. The actual savings achieved to 31 July 2007 was £104 million with an anticipated additional £112 million in the year to 31 July 2008.

71. In the next three years budget settlement, the Scottish Further and Higher Education Funding Council is required to make a 2% per annum efficiency savings. These will be challenging targets for the Scottish Further and Higher Education Funding Council to achieve.

72. We will continue to monitor the financial position and the actions taken by the Scottish Further and Higher Education Funding Council to manage these risks.



Looking Forward

73. The Scottish Further and Higher Education Funding Council faces a number of challenges in 2009/10, which include:

- **National Performance Framework** - The Scottish Government is continuing to develop its approach to performance management based on the National Performance Framework and local authority single outcome agreements. The National Performance Framework is an outcome-based approach that is publically reported on the Scottish Government's web site in the 'Virginia-style' model of performance measurement and reporting. This will include progress on overall delivery of the administration's purpose for Government, the five strategic objectives for Scotland and other aspects of the outcomes based National Performance Framework. We will consider how the Scottish Further and Higher Education Funding Council is addressing this developing area as part of the 2009/10 audit;
- **Efficiencies and future funding** - Budgets for 2009/10 and the immediate future will need to be managed within a tighter funding regime. This includes no scope for the application of end of year flexibility for the Government with HM Treasury until the next Spending Review; no option to transfer funds from capital to revenue; and the impact of the introduction of International Financial Reporting Standards (IFRS), particularly on leases and infrastructure accounting. The challenge for the Scottish Further and Higher Education Funding Council is to prioritise spending, identify efficiencies and review future commitments to ensure delivery of key targets and objectives;
- **Impact of the Recession** - This will affect the Scottish Further and Higher Education Funding Council and Further and Higher Education Institutions by increasing pressures on budgetary and financial control. Higher financial commitments arising out of the decline in property values and staff costs will have a significant effect. There will also be additional cost pressures from the rapidly increased demand for student places as unemployment builds up;
- **IFRS** - The timetable for IFRS implementation requires that central government accounts in Scotland to become IFRS compliant with effect from the 2009/10 financial year. As part of the timetable for the implementation for IFRS, shadow accounts will require to be produced for 2008/09 for audit review by 30 November. These processes will require significant resource to complete and it will be important that these issues are addressed early in 2009/10;
- **Data Handling** - The Scottish Government carried out a review of data handling arrangements in Scotland during 2007. The review considered current policies and procedures on data protection, consistency with government standards and local arrangements for implementation of procedures. A report published in June 2008 made recommendations for a higher level of



oversight and guidance from the Scottish Government and improved security of sensitive information. We will monitor the Scottish Further and Higher Education Funding Council's progress against recommendations due to be implemented during 2009/10;

- **New Horizons** - the Scottish Further and Higher Education Funding Council will need to develop a more strategic role in relation to Higher Education Institutions, balanced by a 'lighter touch' approach to monitoring, and managing its 3 year implementation plan effectively in consultation with stakeholders;
- **Course eligibility and WSUM statistics** – recent problems relating to the regularity of grant payments at Stow College suggest that there could be other courses where the appropriateness of funding may be questionable and where a more rigorous inspection regime might be appropriate;



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Risk Identified	Planned Action	Responsible Officer	Target Date
1.	<p>WSUM data reviews</p> <p>During our audit we reviewed the effectiveness of the Scottish Further and Higher Education Funding Council's rolling programme of inspection visits (suspended after the issue of ineligible courses at Stow College). We found that although the reports resulting from these visits identified weaknesses in college processes, they did not make suggestions for improvement or result in follow up action that ensured that these weaknesses had been remedied.</p> <p>There is an increased risk that data submitted to the Scottish Further and Higher Education Funding Council could be erroneous and therefore payments made on an incorrect basis.</p> <p><i>We recommend that the Scottish Further and Higher Education Funding Council:</i></p> <p><i>(a) considers re-instating the risk of errors in data submitted in the Risk Register; and</i></p> <p><i>(b) reviews its approach and reporting of audit visits to colleges to ensure that any weaknesses identified are corrected.</i></p>	<p>(a) This will be taken into account at the next meeting of the Council's Audit and Compliance Committee on 5 August 2009.</p> <p>(b) We are currently reviewing our approach to auditing data returns for funding purposes. The new approach is likely to be based around reinforcing colleges' own responsibilities in relation to fundable activity as set out in the FM with targeted audit follow-up informed by analysis of the FES data and any other relevant intelligence available to the Council.</p> <p>In relation to adherence to guidance on fundable provision in general, SFC is working with Scotland's Colleges to review a detailed statistical analysis of the most recent FES returns. This work will seek explanations for any data outliers and will identify what action, if any, is required to ensure there is a consistent application of the guidance, and consequent use of SFC funding to support college delivery. The outcome of this work will ultimately enable SFC to provide updated guidance for the FES audits including more specific advice on the quantitative and qualitative interpretation of FES data.</p>	<p>Gus MacLeod, Head of Corporate Governance</p> <p>Riona Bell, Director of Finance and Corporate Resources</p>	<p>5 August 2009</p> <p>31 December 2009</p>



Appendix B: Review of Risks Identified in the Audit Risk Analysis and Plan

Risk	Source of assurance	Planned audit action	Outcome
Financial Performance			
<p>1. Delivery of priorities</p> <p>The risk register identifies that the running cost budget allocated to the Scottish Further and Higher Education Funding Council (SFC) by the Scottish Government could be insufficient to deliver Ministerial priorities and expectations.</p>	<ul style="list-style-type: none"> • Prioritisation of use of available resources to support the delivery of the corporate plan. • Outputs from the performance measurement framework for the corporate plan. • Efficient and effective use of resources in line with the Efficient Government initiative. • Framework for reporting against Ministerial priorities based on the Management Statement with the Scottish Government, including annual reports and quarterly monitoring meetings. 	<ul style="list-style-type: none"> • Review of performance monitoring information relating to delivery of the Scottish Further and Higher Education Funding Council's corporate plan. • Review of outputs from performance measurement framework. • Review of annual report and quarterly monitoring information submitted to the Scottish Government. 	<ul style="list-style-type: none"> • SFC's performance review (based on 06/09 Corporate Plan) had not been published at the time of writing (due for publication later in 2009). • The quarterly reports submitted through the Chair's Committee were reviewed. • No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>2. Failure to reflect Scottish Government priorities</p> <p>There is a risk that the Scottish Further and Higher Education Funding Council will not adequately reflect the priorities of the Scottish Government and the university and college sectors in its corporate plan or in its funding allocations.</p>	<ul style="list-style-type: none"> • Paper to Council that proposed funding allocations are linked to SG strategic priorities and corporate plan objectives. • Regular meetings with SG Lifelong Learning directorate and senior staff. • Strategic dialogue meetings with university and college sectors 	<ul style="list-style-type: none"> • Review documentation of links between corporate plan, funding allocations and SG strategic priorities. 	<ul style="list-style-type: none"> • The new Corporate Plan 2009/12 has identified 7 outcomes which are linked with the SG's National Performance Framework and have been developed following consultation with stakeholders. The relevant documentation has been reviewed and no issues identified.
<p>3. Going Concern in the FE sector</p> <p>There is a history of going concern problems in a number of colleges and the implementation of FRS 17 has increased the deficit position in a number of cases.</p> <p>There is a risk that going concern problems could impact upon the delivery of further education services.</p>	<ul style="list-style-type: none"> • The Scottish Further and Higher Education Funding Council has issued guidance information for colleges and universities regarding the implementation of FRS 17. • Scottish Further and Higher Education Funding Council reviews the Recovery Plans of organisations with a deficit position and monitors progress against these plans. 	<ul style="list-style-type: none"> • Monitor the approach to the disclosure requirements of FRS 17 in further education institutions' accounts. • Review of Scottish Further and Higher Education Funding Council's monitoring of Recovery Plans. 	<ul style="list-style-type: none"> • 4 audit qualifications on the 07/08 College accounts of colleges were due to pension scheme accounting. The downturn in financial markets has increased pension scheme liabilities. We will continue to monitor this issue. • We confirmed that SFC is regularly monitoring the financial health of the bodies that it funds as evidenced by Council minutes. GMAP and FEDD are involved in recovery plans for those most at risk and mergers are being encouraged in some cases. No issues identified. • Given the economic downturn, we will continue to monitor events, the SFC response and follow-up closely.



Risk	Source of assurance	Planned audit action	Outcome
<p>4. Governance/ financial failure of college or institution</p> <p>The risk register notes that weaknesses in college and university governance, leadership and management – including financial failure - may undermine the Scottish Further and Higher Education Funding Council’s credibility.</p> <p>There is also a risk of failure by the Scottish Further and Higher Education Funding Council to act timeously in response to a financial or governance/ operational failure by a college or university.</p>	<ul style="list-style-type: none"> • Systems and controls put in place within Governance & Management Appraisal & Policy (GMAP) to monitor governance arrangements within further and higher education institutions. • Use of Further Education Development Directorate (FEDD) expertise and support from GMAP where appropriate. • The Scottish Further and Higher Education Funding Council has issued guidance on governance and management matters to colleges and universities. • Internal audit follow-up review of the robustness of the systems and controls within GMAP. 	<ul style="list-style-type: none"> • Monitoring of reports on Institutions’ progress and FEDD activities. • Review of external auditors’ management letters. • Examination of the Scottish Further and Higher Education Funding Council review of implementation of college governance changes. • Audit Scotland organises twice yearly meetings of the external auditors of all further education institutions. 	<ul style="list-style-type: none"> • We reviewed SFC’s monitoring of the financial health of institutions via Council minutes and Audit and Compliance Committee papers. • Overview of Scotland’s Colleges published April 2008. SFC response reviewed. Progress is being monitored by the Public Reporting Group of Audit Scotland. • SFC governance guidance reviewed. • FE Sector meetings in October 2008 and January 2009. • No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>5. Estates projects</p> <p>A Scottish Further and Higher Education Funding Council quarterly performance monitoring report commented that “Successful delivery of estates projects particularly by institutions with little experience of capital project management might prove difficult. There is a risk that colleges do not complete construction of projects as agreed.”</p> <p>There are risks of time and cost overruns which would negatively impact on the the Scottish Further and Higher Education Funding Council’s management of its capital programme.</p>	<ul style="list-style-type: none"> • A Property Support Service (provided by external expert firms) is in place to strengthen and broaden the level of advice for and monitoring of the capital programme. • Gateway approval process in place. • Capital Investment Committee involvement in prioritising and managing the capital programme. 	<ul style="list-style-type: none"> • Review of Property and Capital Funding branch monitoring procedures for the capital programme and the work of the Property Support Service. • Review of monthly reports on major projects and Capital Investment Committee minutes. 	<ul style="list-style-type: none"> • Monitoring by the Capital and Investment Committee was reviewed. • We note that following a survey commissioned by the SFC, a ‘Condition and Functional Suitability Survey of Scotland’s colleges’ has been produced which will provide the SFC with a factual base against which to prioritise future capital funding. • Sample of capital grant awards tested for appropriate monitoring. • No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>6. International Financial Reporting Standards</p> <p>The Scottish Further and Higher Education Funding Council is required to submit an IFRS-based 2008 opening balance sheet plus full IFRS-based shadow accounts for 2008/09.</p> <p>There is a risk that the Scottish Further and Higher Education Funding Council may not meet these deadlines for implementing IFRS.</p>	<ul style="list-style-type: none"> • The Scottish Further and Higher Education Funding Council plans for the implementation of IFRS. • The Scottish Further and Higher Education Funding Council is supported by SG guidance and training. • The Scottish Further and Higher Education Funding Council is being supported by PwC which is acting in a consultancy role with regard to the format of the financial statements. 	<ul style="list-style-type: none"> • Evaluate the Scottish Further and Higher Education Funding Council's plans for the introduction of IFRS and outcomes from PwC work. • Review the Scottish Further and Higher Education Funding Council's assessment of the accounting areas most likely to impact on the financial statements. 	<ul style="list-style-type: none"> • IFRS opening balance sheet audit review was satisfactory and report issued February 2009. 2 areas identified for attention – leases and financial instruments – but final audit was satisfactory in both areas. No outstanding issues identified.



Risk	Source of assurance	Planned audit action	Outcome
Governance and Internal Control			
<p>7. Performance Measurement</p> <p>There is a risk that the Scottish Further and Higher Education Funding Council fails to develop a performance measurement framework that is aligned with the SG's National Performance Framework (NPF) thus putting at risk its ability to deliver against NPF outcomes .</p>	<ul style="list-style-type: none"> The Scottish Further and Higher Education Funding Council is being supported by the SG in developing a performance measurement framework for its Corporate Plan which draws on the NPF. 	<ul style="list-style-type: none"> Monitor progress with the framework development. 	<ul style="list-style-type: none"> Work on developing a performance measurement framework is still ongoing; the new Corporate Plan 2009/12 has been aligned to the NPF.
<p>8. Corporate governance</p> <p>There is a risk that governance arrangements do not adapt to match the changing priorities of key stakeholders, particularly the Scottish Government. The JFTT New Horizons report seeks a new 'lighter touch' role for the Scottish Further and Higher Education Funding Council which presents challenges for the future in terms of its oversight relationship with fundable bodies.</p>	<ul style="list-style-type: none"> Internal audit review of Corporate Governance (08/09). Updated communications and external relations strategy in early 2008. Scottish Further and Higher Education Funding Council response to <i>New Horizons</i>. 	<ul style="list-style-type: none"> Review progress towards implementing the recommendations of the Internal Audit report in the light of changing national priorities. Review the updated communications and external relations strategy. Monitor Scottish Further and Higher Education Funding Council response and developments with regard to <i>New Horizons</i>. 	<ul style="list-style-type: none"> IA report 'Corporate Governance' reviewed; no major weaknesses identified and SFC implementation of recommendations ongoing. SFC's Communications and external relations strategy has not yet been finalised. SFC has developed a 3 year implementation programme for New Horizons. We reviewed this - no issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>9. Audit and Compliance Committee</p> <p>The Audit and Compliance Committee's wider remit, encompassing the Scottish Further and Higher Education Funding Council's compliance with legislation and regulation, data security, FOI and health and safety matters, poses a risk that its workload may not be achievable. This could be compounded by the introduction of 2 new members during the year.</p>	<ul style="list-style-type: none">• Scottish Further and Higher Education Funding Council training for audit committee members.• Development of Audit & Compliance Committee work plan with increased areas of coverage.	<ul style="list-style-type: none">• Review training for audit committee members.• Review progress towards revision of committee workload.	<ul style="list-style-type: none">• Audit and Compliance Committee papers reviewed. No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>10. Accountability and governance of colleges</p> <p>The Review of Scotland's Colleges: Accountability and Governance report, commissioned by the Scottish Government and published in 2007, makes a number of recommendations for improvement in the management of further education colleges.</p> <p>There is a risk of reputational damage and lack of confidence in the sector and to the Scottish Further and Higher Education Funding Council if the issues identified in the report are not addressed.</p>	<ul style="list-style-type: none"> An action plan involving the Scottish Government, Scottish Further and Higher Education Funding Council, Association of Scotland's Colleges (ASC) and Scottish Further Education Unit (SFEU) was produced to take forward the issues identified in the consultant's report. 	<ul style="list-style-type: none"> Review progress made towards the implementation of the consultant's recommendations. 	<ul style="list-style-type: none"> Progress reviewed. No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>11. Funding Methodologies review</p> <p>The risk register identifies a risk that the Council's review of teaching and research funding methodologies fails to produce an outcome that commands the confidence of a wide range of stakeholders leading to reputational damage and/ or a breakdown in relationships.</p> <p>The risk will be compounded by implementation of proposals from <i>New Horizons</i> and post-RAE changes.</p>	<ul style="list-style-type: none"> • Consultation document published which contains a timetable for the review and the steps to be taken. • A Teaching Funding Methodologies Review Advisory Group (TFMRAG) to the Chief Executive has been set up to oversee the work of the review. The group has established two sub groups dealing with different aspects of the review. • Regular liaison with the funding working groups of the Association of Scotland's colleges and Universities Scotland. • Research Excellence Framework consultation being carried out. 	<ul style="list-style-type: none"> • Review of progress made by the Scottish Further and Higher Education Funding Council in conjunction with outcomes from the Joint Future Thinking Taskforce on Universities. • Monitor developments re <i>New Horizons</i> and post-RAE proposals. 	<ul style="list-style-type: none"> • Progress with 2 new projects (<i>New Horizons</i> and colleges) reviewed and no issues identified. • Post-RAE proposals reviewed and no issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>12. Grant calculations</p> <p>The risk register records a high risk and medium residual risk of errors in information received from the sectors used in calculating grants</p>	<ul style="list-style-type: none"> • Audit of FES/SUM returns by colleges internal auditors and high level checks by Statistics branch and FE funding. • HE data is subject to various checks as listed in the risk register. 	<ul style="list-style-type: none"> • Audit testing will include a review of the extent to which the controls referred to in the risk register and circulars have been applied. 	<ul style="list-style-type: none"> • Grant testing reviewed controls over data. In the light of the issues arising at Stow College, recommendations were made on the risk register and the focus and reporting of college audit visits (Action Plan1).
<p>13. Grant clawback</p> <p>There is a risk that grant clawback amounts due are not identified, are incorrectly calculated, fail to take account of late changes, are incorrectly deducted from amounts payable or are incorrectly accounted for.</p>	<ul style="list-style-type: none"> • Systems are in place to request and analyse data from universities and colleges. Processes are explained in circulars and colleges and universities can check accuracy of the Scottish Further and Higher Education Funding Council calculations. 	<ul style="list-style-type: none"> • Grants audit testing will include a review of any residual clawback from 2008 circulars and audited returns, plus arrangements for recovery of amounts from 2009 circulars and audited returns. 	<ul style="list-style-type: none"> • Audit testing of clawback income and debtors found that the clawback debtor was understated by £304k. The accounts have subsequently been adjusted.
<p>14. Efficient government</p> <p>There is a risk that progress on the achievement of efficiency savings may not be adequately monitored; and that the Scottish Further and Higher Education Funding Council may not achieve its efficient</p>	<ul style="list-style-type: none"> • The Scottish Further and Higher Education Funding Council's running cost budget is managed to allow it to meet the 2% efficiency gain targets of the 	<ul style="list-style-type: none"> • Review progress in annual report. 	<ul style="list-style-type: none"> • The 2007-08 end year efficiency project manager statement was reviewed. The target savings for the 3 years were already exceeded by the end of year 2. No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
government targets.	SG Efficient Government programme.		
<p>15. Best Value</p> <p>Management arrangements may not be fully developed to meet the best value principles to support secure continuous improvement in performance.</p>	<ul style="list-style-type: none"> • Framework for reporting against Ministerial priorities based on the management Statement with the Scottish Government – including annual reports and quarterly monitoring meetings. • Development of a performance measurement framework for the Council's 2009/12 corporate plan which is intended to better evaluate and demonstrate outcomes. • Internal audit report May 2008. 	<ul style="list-style-type: none"> • Review progress in annual report. • Review the Scottish Further and Higher Education Funding Council evaluation of progress with the framework. • Review Internal Audit report 	<ul style="list-style-type: none"> • The performance measurement framework in the new Corporate Plan was reviewed, no issues identified. • The internal audit best value report was reviewed and no risks were identified.



Risk	Source of assurance	Planned audit action	Outcome
Information Management			
<p>16. IT Security Policy</p> <p>The current ICT security policy, internet acceptable use policy and email acceptable use policy have been recently updated. Data handling guidance is being developed. Potential lack of staff awareness could result in the risk of financial loss, unavailability of services, legal exposure, and loss of confidence in the business's activities or the way it manages personal or other data.</p>	<ul style="list-style-type: none"> • The Scottish Further and Higher Education Funding Council are currently reviewing operational procedures with a view to providing documentation. Procedures will be introduced and reviewed where appropriate on an ongoing basis. • A suite of revised policies on Information Management, ICT Acceptable Use and ICT Monitoring has been introduced and is on intranet with guidance. • Staff are made aware of policy changes by being required to sign-off an ICT Acknowledgement form. In addition, awareness is raised every time a user logs on. 	<ul style="list-style-type: none"> • Completion, evaluation and reporting of findings of Your Business @ Risk Survey of SFC staff by specialist ICT auditor. • Monitor development of data handling policy. 	<ul style="list-style-type: none"> • YB@R survey has been delayed in order to increase staff response over summer period • Office of the Information Commissioner conducted an audit of SFC data control policies and procedures in July 2008. We reviewed their report, the SFC's resulting action plan and progress as reported to the Audit & Compliance Committee. • No issues identified.



Risk	Source of assurance	Planned audit action	Outcome
<p>17. Intranet/EDRMS</p> <p>The Scottish Further and Higher Education Funding Council has implemented new intranet and Electronic Document and Record (EDRMS) Systems which has significantly changed the way that its staff work.</p> <p>There are potential risks from these new systems with regard to record-keeping and staff awareness.</p>	<ul style="list-style-type: none"> • Audit Scotland's Scanning Solutions Report. • Monitoring by the Scottish Further and Higher Education Funding Council's Information Management Team. 	<ul style="list-style-type: none"> • Review progress made by the Scottish Further and Higher Education Funding Council since the Audit Scotland Report. 	<ul style="list-style-type: none"> • We reviewed the progress made on implementation of the EDRMS and the roll out of the proposed scanning solution. • We note that satisfactory progress has been made on EDRMS documentation and monitoring reports and that further work is being carried out on procedures for the deletion or movement of records. • A pilot exercise has been carried out on the proposed scanning solution and the results incorporated into the roll out plan. Training for all branches will begin in September. Risk assessment will be monitored during the full roll out by the Corporate Governance team. • No issues identified.