INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

Glasgow Metropolitan College

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

Audit: Year ended 31 July 2010

21 December 2010

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

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About this report
This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the Code").

This report is for the benefit of the Board of Management of Glasgow Metropolitan College and is made available to Audit Scotland (together "the beneficiaries"), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes, but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scope and objectives section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the beneficiaries) for any purpose or in any context. Any party other than the beneficiaries that obtains access to this report or a copy and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the beneficiaries.

Executive summary

Financial statements

We issued an audit report expressing unqualified opinions on the financial statements of the College for the year ended 31 July 2010. The Board of Management report is consistent with the financial statements and complies with the SORP in all material respects.

Management provided draft financial statements which were complete, of a high standard, and provided in line with the agreed timetable. No adjustments were required to be made to the draft financial statements provided for audit, with the exception of some additional narrative disclosure in respect of the College's merger with Central College Glasgow and Glasgow College of Nautical Studies from 1 September 2010.

Use of resources

The financial statements report a surplus for the year of £1.79 million, an increase of 5.3% compared to the previous year and £1.60 million higher than the projected outturn projected in the management accounts during the year. Income and expenditure were broadly in line with budget, with the better outturn position due primarily to the treatment of the pension adjustment for CPI-RPI which delivered a past service credit of £1.1 million to staff costs expenditure.

We conclude that the College has strong processes in place for budget setting and budget monitoring. Transitional funding has been made available by the Scottish Funding Council over the next two years to assist the merged College, but achievement of a surplus result will be dependent on bringing together three different budget monitoring systems within the merged institution, to ensure that consistent management information is available across all activities.

Corporate governance

We conclude that the College has strong governance arrangements in place. We reviewed the governance arrangements around proposals for and implementation of the merger and found them to be sound. This including tasking contractors to perform financial and legal due diligence on the merger. Risks associated with the merger were identified and monitored throughout the year. Revised arrangements for the merged College have yet to be fully agreed and implemented.

The corporate governance statement does not disclose any significant weaknesses in the systems of internal control which is consistent with our understanding.

Scope

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice* ("The *Code*"). This specifies a number of objectives for our audit.

Audit framework

This year was the fourth of our five-year appointment by the Auditor General for Scotland as external auditors of Glasgow Metropolitan College ("the College"). This report provides our opinion and conclusions and highlights significant issues arising from our work. We outlined the framework under which we operate, under appointment by Audit Scotland, in the audit plan overview discussed with the audit committee earlier in the year.

The purpose of this report is to report our findings as they relate to:

- the **financial statements** and our audit opinions;
- our review of 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, prevention and detection of corruption, and its financial position; and
- aspects of the College's arrangements to manage its **performance** as they relate to economy, efficiency and effectiveness in the use of resources.

Responsibilities of the College principal and board members and its auditors

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 the 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 accountable officer, to make arrangements to secure Best Value.

Action plan

This report includes an action plan containing areas for development or improvement identified during our financial statements audit fieldwork.

Acknowledgement

Our work continues to bring us into contact with a range of College staff and we wish to record our appreciation of the continued co-operation and assistance extended to us by College staff during our work.

Service overview; financial position

Introduction

The financial statements report a surplus for the year of £1.79 million, an increase of 113% compared to the previous year and £1.60 higher than the projected outturn projected in the management accounts during the year. Income and expenditure were broadly in line with budget, the better outturn position is due to the treatment of the pension adjustment for CPI-RPI (£1.1 million) and increase in Scottish Funding Council grants.

Income

Income for the year has risen by £363,000 compared to 2008-09, an increase of 1.36%, due to:

- Grants from the Scottish Funding Council ("the SFC") have risen by £997,000, an increase of 5.5% on the prior year. This is due to two reasons; firstly, because of an inflationary rise in the grant and secondly because of an increase in the level of Weighted Students Numbers ("WSUM's") delivered by the College. The College has seen an increase in learner numbers.
- Other operating income has fallen by £585,000 (22.6%). The College made a lower number of European Social Fund (ESF) grant claims during 2009-10 compared with 2008-09.
- The impact of the recession has resulted in a reduction in investment income of £350,000 (61%), whereas the balance of current investments has increased by £2m. The College safeguards its funds by making less risky temporary deposits to financial institutions, but this has seen the average interest rate that the College achieved for such investments fall from approximately 5% in 2008-09 to 2% in 2009-10.

Expenditure

Expenditure for the year has reduced by £601,000 (2.25%) compared to 2008-09. This is primarily due to the treatment of the pension adjustment for CPI-RPI as explained later. As a result, a negative past service credit of £1.1 million has been recognised within staff costs.

Tight financial control over other operating expenses have kept these in line with the prior year.

	2009-10 £'000	2008-09 £'000
Income		
Scottish Funding Council grants	20,806	19,809
Tuition fees and education contracts	4,811	4,511
Other operating income	2,003	2,588
Investment income	223	573
	27,843	27,480
Expenditure		
Staff costs	17,650	18,209
Other operating expenses	5,942	6,151
Depreciation	2,340	2,292
Interest payable	119	-
	26,051	26,652

Service overview; financial position (continued)

Balance sheet

The balance sheet shows an increase in net assets as at 31 July 2010 compared to the previous year end. Significant movements include:

- An increase in tangible fixed assets of £839,000 is due primarily to the addition of the Marine Skill Centre during the year for which the College has contributed one third of the total amount in partnership with the two colleges it has merged with. This also explains the increase in deferred capital grants.
- Within the debtors balance there is accrued income of £426,000 for a (ESF) grant that the College has applied for. However, the College is awaiting the outcome of the ESF's review of its application and at the time of writing no payment has been made. The College is confident of the claim being successful and that it will receive the funds. It is our understanding that this is consistent with other colleges in the sector, as a result of a change in methodology in the way ESF assesses and approves grants.
- Cash and short term investments have increased by £2 million. The College has a policy of investing surplus cash balances in order to maximise returns, at a minimum exposure to risk.

Accounting for pensions

In its June 2010 budget, the UK government announced that it intended for future increases in public sector pension schemes to be linked to changes in the consumer prices index ("CPI") rather than, as previously, the retail price index ("RPI"). The College has considered the Strathclyde Pension Fund scheme rules and associated members' literature and has concluded that, this change is a change in benefits and so has recognised the resulting credit (£1.1 million) in the income and expenditure account.

At the date of these financial statements, the Urgent Issues Task Force ("UITF") is in the process of consulting widely on the accounting treatment for this change and is expected to issue an Abstract towards the end of 2010. Should the Abstract call for a different accounting treatment it may be necessary to reflect any change in the financial statements for the following year.

	2010 £'000	2009 £'000
Tangible fixed assets	31,693	30,854
Stocks	14	18
Debtors	1,493	1,392
Short term investments	11,000	9,000
Creditors: Amounts falling due within one year	3,119	2,857
Provisions for liabilities and charges	1,323	1,296
Net assets (after pension liability)	**40,066**	34,917
Deferred capital grants	8,128	6,571
Revaluation reserve	20,924	21,631
Income and expenditure account	10,957	6,658
Restricted reserves	57	57
Total	**40,170**	34,917

Financial forecasts

Financial forecasting

Financial forecasting for 2009-10

The probable outturn for 2009-10 reported to the finance and estates committee in June 2010 was £191,000 against the original budget for the year of £231,000. The actual outturn position per the accounts was £1.79 million. This is due, in the main, to the pensions adjustment for CPI-RPI £1.1 million which is treated as negative staff costs within expenditure. Our review of the College's budget setting and monitoring processes confirms that the College is generally strong in its financial forecasting.

The following table reconciles the target outturn from the College's original budget to the actual outturn in the financial statements.

The surplus for the year increased by £1.56 million. The main variances are shown in the attached table.

Income

Income has been better than anticipated across all income lines except for investment income:

- SFC grants were higher than budgeted due to an inflationary increase in core SFC grant funding. The College received additional allocations for financial security and childcare. However, these were offset by a reduction of £1 million relating to an advance received in the previous year.
- Other increases include other grant income which was carried forward from the previous year.
- The College has also seen an increase in demand for its courses and therefore tuition fees have increased.

Expenditure

The key movement in expenditure is in staff costs. As mentioned above, the College has recognised a credit in staff costs of £1.1 million relating to the CPI-RPI adjustment. This is offset by additional costs in part time lecture costs and holiday pay.

	2009-10 Budget £'000
Target surplus per original budget	**(231)**
Increase in Scottish Funding Council grants	(264)
Increase in tuition fees and education contracts	(276)
Increase in other operating income	(216)
Reduction in investment income	196
Reduction in staff costs	(826)
Reduction in other operating expenses	(21)
Reduction in depreciation	(154)
Actual surplus per financial statements	**(1,792)**

Financial forecasts (continued)

Looking forward

Financial forecasting for 2010-11

The College prepared its 2010-11 budget and presented it to the finance and estates committee in June 2010. The College also prepared the 2010 Financial Forecast Return (FFR) for the Funding Council. Uncertainties around SFC funding and the potential impact of the merger which took place in September 2010 make it inherently difficult for the College to prepare forecasts going forward. In the budget, the College projected the following position:

	£'000
Income	26,776
Expenditure	26,713
Forecast surplus for the year ending 31 July 2011	**63**

The College is, therefore, predicting a surplus going forward. This is to be achieved despite a projected reduction in income from SFC grant funding (£328,000) and also ESF funding (£200,000). The College hopes to achieve a reduction in staff costs of £445,000 from a reduction in temporary teaching staff (£182,000) and classroom support staff (£160,000). It is anticipated that the cost of pension enhancements will reduce by £111,000. However, the measures will be offset by the cost of a pay award of £182,000.

There is still some uncertainty as to whether SFC will be able to provide the full level of grants for the 2010-11 financial year, which has been intimated in the SFC grant funding circulars received by the College. This could lead to some in-year reduction in funding in the final four months of 2010-11. Transitional funding has been made available by SFC over the next two years to assist the new College, but achievement of a surplus for the merged College will be dependent on bringing together three different budget monitoring systems within the merged College, to ensure that consistent management information is available across all activities.

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 College 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 corporate governance arrangements as they relate to:

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

College merger

Following Ministerial approval, the College completed the merger on 1 September 2010 with Glasgow College of Nautical Studies and Central College Glasgow to form the City of Glasgow College. We reviewed the governance arrangements around the implementation of the merger, particularly as the College had identified a number of risks and concerns around the governance arrangements at an early stage and worked with the shadow board and partner colleges to rectify them.

A shadow board was set up to oversee the arrangements for the implementation of the merger throughout 2009/10. Contractors were tasked with performing financial and legal due diligence to help the College ensure that the merger would be financially viable and to ensure that legal and governance requires are adhered to.

A merger risk assessment was also carried out and the shadow board reviewed this at each meeting.

The College is still to consider the governance arrangements under the merged College and we will review these arrangements as part of our 2010-11 audit.

Risk management

The board of management takes responsibility for overseeing risk management within the College, with the principal and senior management team acting as policy advisors. As part of the risk management process, the senior management team regularly considers risk and a risk assessment matrix is compiled and submitted to the audit committee. The risk assessment matrix identifies, prioritises and assesses risks to the College according to the likelihood and the impact of each risk. The audit committee meet regularly during the year to review the College's response to identified risks, including aspects of the proposed merger.

The College's approach to risk management is based on guidance produced by the Chartered Institute of Public Finance and Accountancy ("CIPFA") for the further and higher education sectors in Scotland.

The College merger provided much of the focus of risk management throughout 2009-10.

Governance and risk management (continued)

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 Scotland's Colleges and Audit Scotland. The audit committee also considers any applicable correspondence. The College therefore considers all incoming guidance received from these bodies, and can demonstrate that they take appropriate action when required. While there is procedures for monitoring all guidance issued, management should consider implementing a formal record of actions taken for each circular received to its existing log of circulars and guidance.

Prevention and detection of fraud and irregularity

The College has in place an over-arching fraud prevention policy, in addition to a whistle-blowing policy. Both policies are readily available to staff on the College's intranet and are also published on the College's website. The fraud prevention also includes a plan on the response to any frauds identified. Management has not reported any frauds, material or otherwise, during 2009-10. In addition to these policies, the College has implemented procurement and tendering procedures to ensure that the risk of financial irregularity is mitigated.

The Bribery Act 2010 will come into force next year. While not of direct applicability to the College in view of its status, it is suggested that the College's activities, particularly those overseas and using agents, should be subject to review against the Act's requirements as a matter of good practice. This would help identify if there are risks or areas where training and further guidance might be required.

Internal controls

In accordance with our audit plan, we undertook detailed testing in relation to both entity level and key financial controls. We relied on the work carried out on internal audit around tuition fees and debtors and student records. 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.

Internal audit

The approved internal audit programme for 2009/10 has been completed and the internal auditors have concluded that the College that there are no material weaknesses in the College's control environment.

Best Value / value for money

The 2009-10 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.

Appendix one – action plan

Priority rating for recommendations		
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 recommendation	Management response	Officer and due date
1	The Bribery Act 2010 will come into force next year. While not of direct applicability to the College in view of its status, it is suggested that the College's activities, particularly those overseas and using agents, should be subject to review against the Act's requirements as a matter of good practice. This would help identify if there are risks or areas where training and further guidance might be required.	Agreed action.	Vice Principal, Finance and Resources April 2011