James Watt College

Annual Audit Report to the Board of Management and Auditor General for Scotland

Audit for the year ended 31 July 2010

CONTENTS

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EXECUTIVE SUMMARY

Financial Highlights

The College achieved a deficit of £426k (2009 surplus of £568k) on its income and expenditure account for the year prior to FRS17 adjustments for the Strathclyde Pension Scheme (SPF). On 22 June 2010 the Chancellor announced a change in the methodology for calculating future pension increases which are now being linked to the Consumer Price Index (CPI). In accordance with the treatment recommended by Hymans Robertson LLP, the effect of this change has been taken through income and expenditure account as a negative past service cost of £1,423k. The net effect of the FRS17 adjustments in total is a credit of £976k (2009 debit of £317k) to income and expenditure account taking the overall surplus for the year to £550k (2009 £251k).

The financial statements disclose retained general reserves of £10.79m (2009 £7.25m). The 2010/11 financial forecast return anticipates a surplus of £46k, excluding adjustments in relation to FRS 17.

Corporate Governance

From our review of Corporate Governance arrangements within the College, we believe the Corporate Governance statement to be neither misleading nor inconsistent with other information made available to us during the course of the audit process. The Corporate Governance statement does not disclose any significant weaknesses in the systems of internal control.

Internal auditors Henderson Loggie concluded that the College operates adequate and effective internal control systems as defined in the audit needs assessment.

The Operating and Financial Review provides a comprehensive account of the College's activities and meets the requirements of the Statement of Recommended Practice Accounting for Further and Higher Education 2007 ("SORP 2007").

Financial Statement Audit

We have completed our audit work in respect of the financial statements of the College and are satisfied that they present a true and fair view of its financial position for the year ended 31 July 2010. Following approval of the financial statements by the Board of Management on 15 December 2010 our audit report will express unqualified opinions on (i) the financial statements of the College for the year ended 31 July 2010 and (ii) regularity.

In preparing the accounts on a going concern basis, the Board of Management is satisfied that the SFC will provide sufficient funding to enable the College to operate for at least 12 months from the signing of the accounts.

Management provided draft financial statements and supporting working papers in line with the agreed timetable. The draft financial statements and supporting documentation were complete and of a good standard.

The 2009/10 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.

OVERVIEW, SCOPE AND INDEPENDENCE

Overview

• The purpose of this report is to highlight and explain key issues arising from our audit of the financial statements of James Watt College ('the College') for the year ended 31st July 2010.

•This report covers those matters we believe to be material in the context of our work. It was prepared from general information obtained during the audit process, including management accounting information and discussion with management and staff of the College. It has been prepared solely for the use of the College and the Auditor General for Scotland and should not be shown to any other person without our express permission in writing. We do not accept responsibility for this report to any other person and we hereby disclaim any and all such liability. We do not, in preparing this report, accept or assume responsibility for any other purpose or to any other person to whom it is shown or into whose hands it may come save as expressly agreed by our prior written consent. If others choose to rely on the contents of this report, they do so at entirely their own risk.

• 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 2010. 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.

Significant Accounting and Audit Issues

Detailed below are the key accounting and audit issues identified during our work:

- FRS 17 - CPI
- Addition Fee Waiver
- Estates Strategy
- SUM's Achievement
- Accounting Treatment of Early retirals
- Lecture Theatre Depreciation

Unadjusted Audit Differences

We are required by International Standard on Auditing (UK & Ireland) 260 to bring to your attention audit adjustments that we have identified but we are not proposing to adjust and which the Board of Management is required to consider. A schedule of such adjustments is included in Appendix 1. We have not included items under £3,840 which we consider to be clearly trivial. Total unadjusted audit differences identified by our audit work would not alter the reported surplus but represent reallocations within the Income & Expenditure Account and Balance Sheet respectively. The Board will need to consider the materiality of these identified misstatements in the context of the financial statements taken as a whole.

OVERVIEW, SCOPE AND INDEPENDENCE Continued...

Key areas	Summary
Scope	The accounting rules and regulations applied to Further Education Colleges are specifically laid out in various documents as discussed on page 8 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. We can confirm that 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. The audit of James Watt College 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.
Independence	Under Auditing and Ethical Standards, we are required as auditors to confirm our independence to "those charged with governance". This term refers to the Board of Management in our view and we confirmed our independence to them in a letter on 15 April 2010. Our internal procedures are designed to ensure that all partners and professional staff are aware of relationships that may be considered to bear on our objectivity and independence as auditors. The principal statements of policies are set out in our Conduct of Professional Services Manual. In addition, we have issued supplementary written guidance and embedded the requirements of the Standards in our internal training programmes. The procedures require that audit engagement partners are made aware of any matters which may reasonably be thought to bear on the firm's independence and the objectivity of the audit engagement partner and the audit staff. We confirm that the firm complies with the APB Ethical Standards and, in our professional judgment, is independent and objective within the meaning of those Standards. In our professional judgement the policies and safeguards in place ensure that we are independent within the meaning of all regulatory and professional requirements and that the objectivity of the audit engagement partner and audit staff is not impaired. Should you have any comments or queries regarding this confirmation we would welcome their discussion in more detail.

AUDIT FRAMEWORK

Audit Framework

Audit Framework

BDO LLP was appointed by Audit Scotland as external auditor to James Watt College for 5 years covering the financial years 2006/07 to 2010/11. This year was the fourth of the five-year appointment by the Auditor General for Scotland as external auditors of James Watt College ("the College"). This report to the College Board of Management and Auditor General for Scotland provides our opinion and highlights issues arising from our work in relation to our audit work for 2009/10 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 .

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.

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.

AUDIT FRAMEWORK
Continued…

Auditor's Responsibilities and Approach

Audit Framework

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.

AUDIT FRAMEWORK
Continued…

Audit Framework

College Guidance

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. Our audit procedures identified no factors that would lead us to believe that the college does not comply with the terms and conditions of the financial 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

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.

FINANCIAL HIGHLIGHTS

Key areas	Summary
Financial Highlights	• **Income and Expenditure Account:** The College achieve a surplus of £550k, 1.4% of total income in respect of the year ended 31 July 2010 (2008/09: £251k and 0.6%, Forecast: £45k and 0.1%). This increase represented a £299k increase on the prior year and a £505k increase on forecast. The main reason for the increased surplus compared to the original budget relates to the incorporation of the FRS 17 adjustments for the Strathclyde Pension Scheme which resulted in a credit to Income and expenditure account of £976k. Total income decreased by £1.376m (3.5%) on the prior year. The decrease occurred mainly due to a reduction in tuition fees and investment income. • **Balance Sheet:** The financial statements report net assets at 31 July 2010 of £15.699m. The £3.46m increase on 2008/09 is mainly attributable to the actuarial gain of £2.996m reducing the pension deficit which has been dealt with through the Statement of Total Recognised Gains and Losses together with the surplus for the year of £550k. The balance on the Revaluation Reserve carried forward as at 31 July 2010 is a surplus of £13.904m (31 July 2009: £14.469m).
Cash Flow	During 2009/10, the College experienced a net inflow of cash of £1.502m (2008/09: outflow of £5.152m).
Financial Forecast	The initial 2009/10 financial plan forecasted a surplus of £45k. The difference between that which was forecast and achieved can in the main be explained by the impact of FRS 17 pension adjustments, an increase in the level of tuition fees offset by an increase in payroll costs re unbudgeted severance costs and bursary costs met by the College. The forecast of income and expenditure for the College for 2010/11 shows that income is expected to remain at a similar level to 2009/10 at £38.1m whilst expenditure (excluding any FRS 17 adjustments) is anticipated to fall, resulting in a small surplus of £46k before any FRS 17 adjustments are taken into account.

FINANCIAL HIGHLIGHTS
Income and Expenditure Account

Income

- The table below summarises the main sources of income for 2009/10 and 2008/09.
- The College's WSUMs target for 2009/10 was 152,030 (including 2,230 for economic downturn) and there have been no issues over the delivery of this. As a result, the College will not be liable to repay any recurrent grant to SFC in 2010/11.
- A significant proportion of income (85%), is received from the Scottish Funding Council and the SFC source of income remains relatively consistent with 2008/09. Total SFC Grant income is normally in the region of 73% of total income, based on SFC 2007/08 statistics for colleges delivering over 75,000 WSUMs.
- A decrease in tuition fees and education contracts of £542k. This is mainly as a result of a reduction in overseas income with tighter immigration controls. There was also a reduction in funding from Skills Development Scotland for Skillseekers (which is in line with trends across other colleges and reflects a tightening of public body budgets) and a reduction in MCMC funding.
- A decrease in other income and investment income of £610k. This has arisen due to a 97% fall in Local Authority Grants from £144k to £5k due to reduced public sector funding, and low interest rates on the bank deposits during the year.

Income and Expenditure Account	31 July 2010 £'000	31 July 2009 £'000	Variance £'000
Scottish Funding Council Grants	32,510	32,734	(224)
Tuition Fees and Education Contracts	3,706	4,248	(542)
Other Income	1,830	1,969	(139)
Investment Income	67	538	(471)
Total Income	**38,113**	**39,489**	**(1,376)**
Expenditure (see analysis on next page)	**37,563**	**39,238**	**(1,675)**
Surplus	**550**	**251**	**299**

FINANCIAL HIGHLIGHTS
Income and Expenditure Account continued…

Expenditure

Total expenditure decreased by £1.675m (4.3%), in comparison to 2008/09, to £37.563m. The decrease in expenditure is, in the main, due to a decrease in staff costs with the most significant movements detailed as follows. The table below summarises the main categories of expenditure for 2009/10 and 2008/09:

- a decrease in staff costs of £1.294m mainly due to FRS 17 credits of £1.338m (2009 debits of £94k); and
- a decrease in other operating expenses of £48k which has primarily been achieved by cost cutting of overheads in both teaching activities and administration cost centres.
- an £86k decrease in the depreciation charge.
- a decrease in interest payable of £247k due to the low interest rates on the bank loan during the year.

Expenditure Analysis	31 July 2010 £'000	31 July 2009 £'000	Variance £'000
Staff Costs	24,449	25,743	(1,294)
Other Operating Expenditure	11,145	11,193	(48)
Depreciation	1,435	1,521	(86)
Interest Payable	534	781	(247)
Total Expenditure	**37,563**	**39,238**	**(1,675)**

FINANCIAL HIGHLIGHTS
Balance Sheet

The balance sheets shows an increase of £3.46m in net assets as at 31 July 2010 compared to the previous year end. Significant movements include:

- A decrease in tangible fixed assets of £787k. This is a result of the deprecation charge for the year of £1.435m being partially offset by the capital expenditure in the year of £649k including lecture theatre expenditure, concourse re-modelling, and Finnart tower and library expenditure.
- An increase in cash of £1.502m. This is primarily a result of the receipt of £4.2m of capital grants less capital expenditure of £649k, loan repayments of £1.461m and the net cash outflow from operating activities of £455k.
- An increase in creditors falling due within one year of £2.934m. The major components of this were an increase in capital grant deferred income of £3.5m and a reduction in accruals and deferred income of £496k.
- A decrease in creditors of £1.73m falling due after one year. £1m of the SFC loan was repaid in the year with a further £250k re-categorised as due within one year. Bank loan repayments of £478k were made.
- A decrease in the pension liability of £3.972m, which has been brought about mainly by past service gains as a result of using CPI and not RPI in the FRS 17 calculations together with an actuarial gain of £2.996m.

Balance Sheet Category	31 July 2010 £'000	31 July 2009 £'000	Variance £'000
Fixed Assets	24,608	25,395	(787)
Stock/Debtors	2,185	2,204	(19)
Cash	8,451	6,949	1,502
Creditors: Amounts falling due within 1 year	(11,447)	(8,513)	(2,934)
Creditors: Amounts falling due after 1 year	(3,890)	(5,618)	1,728
Pension Liability	(4,208)	(8,180)	3,972
Net Assets	**15,699**	**12,238**	**3,461**

FINANCIAL HIGHLIGHTS
Financial Forecasts

Financial Forecasting

- The initial 2009/10 financial plan forecasted a surplus of £45k. The table below (bottom left) shows the reconciliation between the forecast outturn and the actual amount generated during the course of the year. The main reasons for the movement from the forecast to the actual outturn were as follows:
  - decrease in SFC grant income of £272k.
  - an increase in other sources of income primarily related to a higher than budgeted level of tuition fees.
  - an increase in payroll costs re unbudgeted voluntary severance costs of £700k.
  - bursary costs met by the College of £385k.
- The table below (bottom right) summarises the forecast income, expenditure and cash balances for the College for 2010/11.
- Income is expected to remain constant in 2010/11 whilst expenditure (excluding any FRS 17 adjustments) is anticipated to fall, resulting in a modest surplus of £46k, excluding FRS 17 adjustments. College expenditure will have to be monitored closely, in particular staff costs which represent 67% of forecasted College expenditure, in order to achieve the forecasted surplus.

Forecast vs. Actual	31 July 2010 £'000	31 July 2009 £'000
Forecast outturn per budget	**45**	**277**
Decrease in SFC grant income	(272)	1,069
Increase (/decrease) in other income	743	60
(Increase)/decrease in exceptional restructuring costs	(700)	(1,249)
(Increase)/decrease in payroll and other operating expenditure	(242)	411
FRS 17 adjustments	976	(317)
Actual outturn at year end	**550**	**251**

Forecast Income, Expenditure and Cash Balances for 2010/11	£'000
Income	38,082
Expenditure	(38,036)
Forecast surplus for the year ending 31 July 2011	**46**
Cash balance at 31 July 2010	8,451
Forecast movement in cash during 2010/11	(6,263)
Resulting cash balance at 31 July 2011	**2,188**

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters

FRS 17 - CPI

- On 22 June 2010 the Chancellor announced a change in the methodology for calculating future pension increases which are now being linked to the Consumer Price Index (CPI) rather than the Retail Prices Index (RPI) which was previously used. The effect of this change on the College share of the Strathclyde Pension Fund (SPF) comes through as a negative past service cost of £1.423m. The key question is whether this credit should be taken through income and expenditure account or taken to the statement of total recognised gains and losses. The Accounting Standards Board issued Urgent Issues Task Force information sheet number 90 entitled 'Accounting implications of the replacement of the Retail Prices Index with the Consumer Prices Index for Retirement Benefits' on 13 October 2010. The issue is whether the change gives rise to a different benefit (a change in benefit) or whether a different assumption is being applied to an unchanged benefit (a change in assumption). FRS 17 'Retirement Benefits' requires that a change in scheme liabilities arising from a change in benefit be recognised in the income and expenditure account. In contrast, it requires that a change in the scheme liabilities arising from a change in an assumption is part of actuarial gains and losses which should be recognised in the statement of total recognised gains and losses.
- The College has taken the view that the credit of £1.423m should be taken to income and expenditure account in accordance with actuarial advice from Hymans Robertson LLP.

BDO Conclusion

In this case the draft guidance is capable of interpretation either way and the accounting treatment hinges in part on whether there is a constructive obligation to pay pension increases linked to RPI in the SPF. We are satisfied that the College's accounting treatment of the £1.423m can be supported by reference to the draft UITF guidance and the advice given by Hymans Robertson LLP.

The consultation period for comments on the UITF draft abstract expired on 10 November 2010 and a final UITF document will be issued in due course and will hopefully provide clarity on the issue. If the final document requires that such credits be taken to the statement of total recognised gains and losses rather than the income and expenditure account, then the College accounting treatment will need to be adjusted next year by restating the comparative figures on the income and expenditure account. The balance sheet figures are unaffected.

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

Additional Fee Waiver - Recognition of Income

- With respect to fee waiver the college is not in a clawback position with regard to 2009/10, and due to the high level of demand amongst students the College is in a position to receive an additional fee waiver grant. Calculations were agreed showing that the College may receive an additional fee waiver grant of £528k. However, due to the economic downturn and the resultant increase in the number of students with fee waiver needs across the college sector, SFC may not be able to meet the demand from all colleges for additional fee waiver grant due to funding constraints.

BDO Conclusion

Management have recognised the fee waiver income of £528k within income in the financial statements and have made full provision against non recovery of the amount by debiting bad debts with the same amount. Whilst our preferred presentation would have been to exclude the £528k from both income and expenditure (income should not be reflected in the financial statements unless it is more likely than not to be received), we are satisfied that the net result is unaffected and is appropriate, as SFC have indicated that they cannot guarantee payment.

Estates Strategy

- An “Estates Strategy” paper was put to the Board of Management in April 2008. Decisions taken on the future use of the College’s estates could indicate the need for impairment in the current carrying values of the College’s land and buildings in 2009/10. The estates strategy is updated on a yearly basis and fully refreshed every five years; the most up to date strategy - from November 2009 - was obtained. This noted the progress on the targets set in the original estates strategy.

BDO Conclusion

Having reviewed the latest estates strategy document and discussed it with management, there is no indication that any of the properties at each campus require to be impaired at the year-end.

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

Lecture Theatre Depreciation

- A lecture theatre (a fixed asset addition in the year) with a cost of £263k was initially depreciated in full in the year (along with the full release of the deferred capital grant). The expenditure was at the Kilwinning Campus which was acquired previously under a Private Finance initiative (PFI) scheme. After discussions with BDO, the college agreed that the capital expenditure was of enduring benefit to the College and that both the depreciation and the deferred capital grant should be charged/released to income and expenditure account over a five year period.

BDO Conclusion

The capital expenditure together with the related depreciation and deferred capital grant have now been appropriately accounted for.

Accounting Treatment of Early Retirals

- Eight people took early retirement on 31 July 2010 and these people were not included in the FRS 17 liability as calculated by Hymans Robertson. An additional liability for these costs of £210k was calculated using the actuarial tables provided by SFC and then reflected in the financial statements. The pension liability in the balance sheet (£4,280k) consists of the liability per the Hyman Robertson's report (£3,998k) added to the liability for these early retirees (£210k).

BDO Conclusion

The College accounting treatment of the early retirals is reasonable in the circumstances and we consider the liability to be fairly stated in the balance sheet as at 31 July 2010.

KEY ACCOUNTING AND AUDIT MATTERS
From the Audit Planning Memo & Other Matters Continued…

James Watt College

SUMs Achievement
• SFC require the College to achieve total WSUMs within 2% of its target for the year to avoid being in a clawback position.
BDO Conclusion
The College certificate to SFC shows a WSUMs total for the year to 31 July 2010 of 156,207. This figure is in excess of its target for the year of 152,030 and accordingly there should be no clawback of SFC grant for non achievement of WSUMs target.

BDO

CORPORATE GOVERNANCE

Corporate Governance
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. The corporate governance arrangements of an organisation are the means by which strategy is set and monitored, managers are held to account, risks are managed, stewardship responsibilities are discharged and institutional sustainability is ensured. The Code of Audit Practice requires that auditors review and report on the College's corporate governance arrangements as they relate to: • the College's reviews of its systems of internal control, including reporting arrangements; • the prevention and detection of fraud and irregularity; • standards of conduct and arrangements for the prevention and detection of corruption; and • its financial position.
The Board of Management is required to report on their compliance with the "***Combined Code on Corporate Governance (June 2008)***". Looking forward we would draw your attention to the revised Corporate Governance Code published in June 2010 called ***"The UK Corporate Governance Code"*** and also to the Consultation Draft issued by CIPFA in May 2010 called **"Delivering Good Governance in Scotland's Colleges: A Framework"**.
Board of Management: has six formally constituted committees which have specific terms of reference and act with delegated authority from the Board (including the Audit Committee, Finance & Resources Committee, HR Development Committee, Learning & Teaching Committee, Remuneration Committee, and Nominations Committee). • ***Composition:*** the Board is comprised of 16 members as at 31 July 2010; hence, the Board has no more than the recommended maximum of 16 members. The skills of the members of the Board included those with relevant skills and expertise in finance, marketing, logistics, human resources and management consultancy. The College representatives include the Principal, a member of the teaching staff, a member of the support staff and a member of the student's union. The College follows the principle that the Board has a majority of members who are external and independent (i.e. neither staff nor student of the College). The College clerk to the Board of Management is performed by Sandy Adamson, thereby meeting the best practice that the role is held by an individual who is independent of College management. The recommended maximum period of office for board members of 12 years has been adhered to. • ***Timing:*** The Board exceeded the recommendation for meeting not less than 4 times during the year, with 4 meetings in 2009/10. Therefore, the Board met at sufficiently regular intervals during the course of the year in order to discharge its duties effectively.

CORPORATE GOVERNANCE
Continued…

Corporate Governance continued…

Board of Management continued…

- ***Responsibilities:*** It was noted that no one individual has unfettered powers of decision-making. Arrangements are in place to enable the chairman to hold meetings with the other non-executive governing body members without executives present when deemed appropriate.
- ***Development and Evaluation:*** Management are aware of the importance of ensuring that the new Board members have a timely induction and appropriate development programme. The Board reviews its effectiveness and undertakes a formal and rigorous evaluation of its own effectiveness and that of its committees at regular intervals.

Audit Committee: is comprised of 5 members as at 31 July 2010. The committee, with 4 non-executives, meets the recommendation that there be at least 2 independent non-executive members. With no qualified accountants, the Audit Committee has not met the recommendation that at least one member of the committee has recent and relevant financial expertise. It was noted that the Chair of the Board of Management was not also a member of the Audit Committee and that no member of the Audit Committee was also a member of the Finance Committee.

Remuneration Committee: is comprised of 5 members as at 31 July 2010. It is recommended that if the Chair of the Board of Management is a member of the Remuneration Committee they should not chair the committee. The College as yet does not follow this recommendation.

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.

CORPORATE GOVERNANCE Continued…

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 Henderson Loggie. An assessment was made of the adequacy of the internal audit output and it was concluded that we as external auditors were able to use the work of internal audit in planning our own procedures. Accordingly cognisance was made of the work of internal audit in the following areas during 2009/10:

- Budgetary Control
- Student Fees / Registry
- Business Development Unit Operations
- Business Process Review
- Cash Handling and SFC Grant Income
- Health and Safety
- EMA, Bursaries and WSUMs

In November 2010, Henderson Loggie issued the internal audit report for the year ended 31 July 2010. This concluded that the College operates adequate and effective internal control systems as defined in the audit needs assessment.

Risk Management

The Board has responsibility for the identification and management of risks facing the College. A risk assessment matrix of the exposure to risk, and the extent to which these risks are controlled, including implementation of actions to mitigate risk, is updated and presented to the Board of Management every quarter to review the College's response to identified risks. This identifies, prioritises and assesses risks to the College according to the likelihood and the impact of each risk.

CORPORATE GOVERNANCE
Continued…

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. The College has in place an over-arching fraud prevention policy, in addition to a whistle-blowing policy. Both of the 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. In addition to the aforementioned policies, the College has also implemented tendering and procurement procedures to mitigate the risk of financial irregularity.

Operating and Financial Review (OFR)

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. Two colleges have been identified as providing examples of good practice. James Watt College has included the required level of detail in its OFR. The college has considered how it can best implement the recommendations within this guidance going forward in order to present data that best reflects the key performance indicators being measured against targets set.

PREPARATION OF THE FINANCIAL STATEMENTS

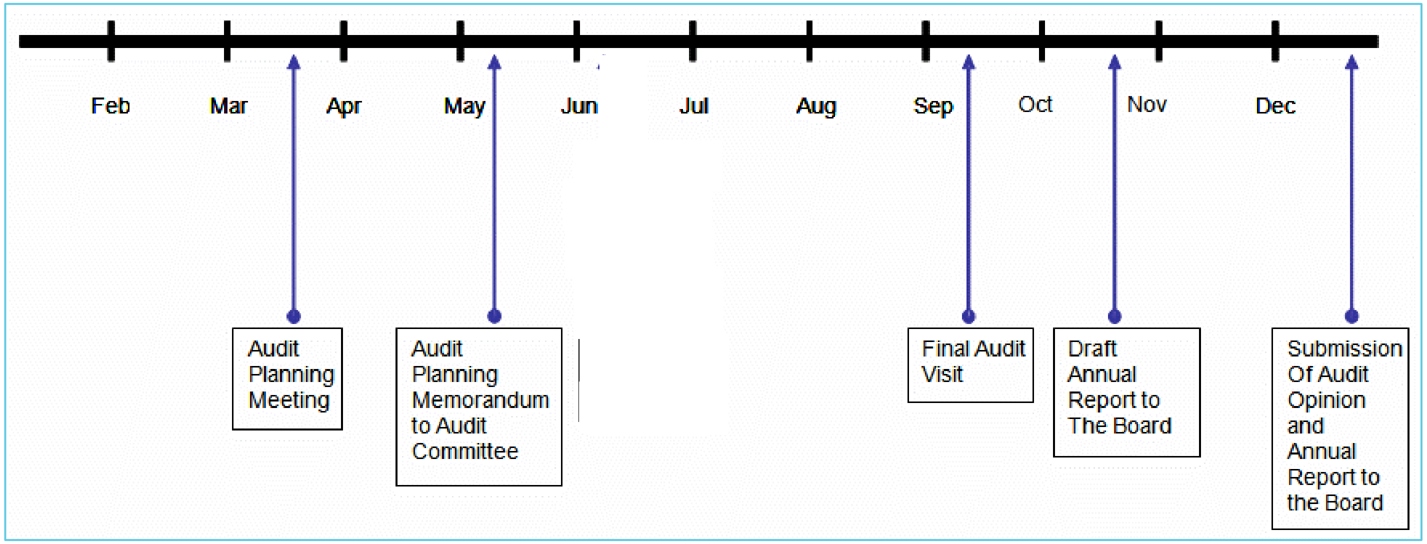
Preparation of the Financial Statements

Our Audit Planning Memorandum issued to the College in May 2010 outlined the various stages of the audit process, as set out in the timetable below. In relation to the key factors of the production of the financial statements, our assessment was as follows:

Completeness of Draft Financial Statements: We received a set of draft financial statements on 4th October 2010, the first day of audit fieldwork. The draft accounts were of good quality. Most issues were resolved by the end of fieldwork and a revised draft received on 4 November 2010. Any outstanding matters were amicably resolved prior to receipt of the final accounts and audit sign off.

Quality of Supporting Documentation: Prior to the beginning of our audit fieldwork, we issued an "Information to be Prepared by Client" request setting out the required supporting documentation to be in place for the beginning of audit field work. The supporting documentation that was received was of an extremely high standard with little requirement to obtain additional schedules from the Finance staff.

Response to Audit Queries: Management provided high quality and timeous responses to all of the audit queries that were posed to them, as in prior years.



APPENDIX 1
Unadjusted Audit Differences

Unadjusted Audit Differences

We are required by International Standards on Auditing 260 "Communication of matters to those charged with governance" to communicate all uncorrected audit differences, other than those we clearly believe to be trivial.

Total unadjusted audit differences identified by our audit work would not alter the reported surplus but represent reallocations within the Income & Expenditure Account and Balance Sheet respectively. The Board of Management will need to consider the materiality of these identified misstatements in the context of the financial statements taken as a whole. These are set in the table below:

		Income & Expenditure Account		Balance Sheet	
Unadjusted Audit Differences	**£'000**	**DR £'000**	**CR £'000**	**DR £'000**	**CR £'000**
Surplus for the Year before Audit Adjustments	550	•	•	•	•
Reallocation of the provision for the potential non-recoverability of the fee waiver debtor	-	528	528		
Reallocation of credit balances on debtors ledger to trade creditors rather than to other creditors	-			5	5
Total Adjustments	**-**	**619**	**619**	**5**	**5**
Surplus for the Year after Audit Adjustments	**550**				

The matters raised in our report prepared in connection with the audit are those we believe should be brought to your attention. They do not purport to be a complete record of all matters arising. This report is prepared solely for the use of the company and may not be quoted nor copied without our prior written consent. No responsibility to any third party is accepted.

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