

# Perth College

**Annual Audit Report to the  
Board of Management and the  
Auditor General for Scotland -  
year ended 31 July 2019**

**February 2020**



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## About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Auditor General for Scotland has appointed us as external auditor of Perth College (the College) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and our responsibilities as set out within Audit Scotland's Code of Audit Practice. This report is for the benefit of the College and is made available to the Auditor General for Scotland and Audit Scotland. This report has not been designed to be of benefit to anyone except the recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) 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, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients

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If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Diane McGiffen, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

## Key Conclusions from our 2018/19 audit

<p>Financial statements: Audit Opinion</p>	<p>We have concluded our audit of the College's consolidated financial statements for the year ended 31 July 2019. A significant number of adjustments were processed as part of the audit. Appendix F outlines the 31 processed adjustments, along with two unadjusted audit differences arising from the audit.</p> <p>Following substantial revision as part of the audit process, we concluded the other information subject to audit, including parts of the Remuneration Report and the Governance Statement were appropriate.</p>	<p>A M B E R</p>
<p>Presentation and disclosures</p>	<p>We did not receive draft financial statements in line with our agreed timetable and the financial statements and disclosures required substantial revision to allow us to conclude that they were materially compliant with the requirements of the Scottish Funding Council's 2018/19 Accounts Direction. The College was unable to produce financial statements by the 31 December 2019 deadline.</p>	<p>A M B E R</p>
<p>Wider Scope: Financial Management</p>	<p>The College has experienced significant turnover within the finance team over a period of 18 months. In December 2018, the previous Chief Operating Officer left the College. These factors have had a significant impact on the capacity and capability of the finance team and the College's ability to provide the Board with the strategic financial planning support that it needs. During the year, Board members highlighted that key financial reports provided late or verbally undermined their ability to fully discharge their responsibilities.</p> <p>In our view, there is significant scope to improve the quality of financial reporting by providing focused analysis on significant budget movements, the impact of key strategies and the forecast outturn position. Our work has identified ongoing weaknesses in internal controls, including lack of effective management review. The College did not fully participate in the NFI exercise within the timetable set by Audit Scotland and NFI is not yet embedded within the College's Fraud Policy and Response Plan.</p>	<p>R E D</p>
<p>Financial Sustainability</p>	<p>The College submitted its Financial Forecast Return to the Scottish Funding Council in September 2019. The Board received insufficient time or support to be able to challenge key assumptions effectively. The FFR has not been subject to the level of scenario planning we would expect. In our view, the FFR does not present a robust medium term financial plan and cannot, therefore provide adequate assurance to the Regional Strategic Body or the Scottish Funding Council that financial risks are being managed effectively.</p> <p>The College has established ambitious plans to diversify income within the draft Business Development and International strategies. While these strategies are work in progress, financial monitoring reports provide insufficient detail at this stage to allow the Board to track the delivery of key strategies. All strategies of this nature present a risk that income will not be delivered as planned. The College must therefore ensure that financial monitoring reports are robust and aligned to the delivery of strategic plans.</p>	<p>R E D</p>

Governance and  
Transparency

While the College has a number of key features of good governance in place, there is a risk that Board members are not provided with enough support or information to fully discharge their responsibilities. The Board did not consider financial monitoring reports or the risk register during the year. We also noted a number of significant decisions, including the structure of the Senior Management Team and the use of settlement agreements, were not, in our view, subject to adequate scrutiny.

Management's assessment of compliance with the Code of Good Governance identified two areas of non-compliance. The College also disclosed a number of other significant control weaknesses within the Governance Statement, including the failure to produce and finalise financial statements by the deadline set within the Accounts Direction. We also note that the College's internal auditors have drawn attention to limited progress made to date in implementing internal audit recommendations.

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Value for Money

The College has reviewed the effectiveness of balanced scorecard reporting during 2018/19, but the current scorecard does not provide metrics for key indicators. The Board received only an interim performance report for 2018/19; 40% of targets that can be measured have not been achieved.

Significant procurement weaknesses were identified and disclosed within the College's governance statement.

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# Introduction

## Our key contacts:

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## Purpose of this report

In accordance with the Public Finance and Accountability (Scotland) Act 2000 (“the Act”), the Auditor General for Scotland appointed EY as the external auditor of Perth College (“the College”) for the five year period 2016/17 to 2020/21.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both members of the Board of Management and the Auditor General for Scotland, and is presented to those charged with governance. This report is provided to Audit Scotland and will be published on their website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the College. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our Annual Audit Plan.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the College employs best practice and where practices can be improved. We use these insights to form our audit recommendations to support the College in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. Such areas we have identified are highlighted throughout this report together with our judgements and conclusions regarding the College’s arrangements.

## Our independence

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as the College’s external auditor.

## Scope and Responsibilities

The Code sets out the responsibilities of both the College and the auditor (summarised in Appendix A). We outlined these in our Annual Audit Plan, which was presented to the Audit and Risk Committee on 14 May 2019.

Our Annual Audit Plan set out an overview of our audit scope and approach for the audit of the 2018/19 financial statements. Planning is a continuous process and changes were required to the audit approach outlined in the plan. These changes were triggered following:

- continued significant changes in personnel within the finance team;
- concerns raised by internal audit with respect of payroll system;
- correspondence received by Audit Scotland during the course of the audit; and
- late provision of compliant financial statements and relevant working papers

As a result, changes were made to the level of materiality that we applied during the audit. Tolerable error was reduced from 75% to 50% of planning materiality.

Overall Materiality	Tolerable Error	Reporting threshold
<b>£460,000</b>	<b>£230,000</b>	<b>£23,000</b>
1.9% of the College's gross expenditure	Materiality at an individual account level	Level that we will report to committee

As outlined in our Annual Audit Plan, based on considerations around the expectations of financial statement users and qualitative factors, we apply a lower materiality level of £1,000 to the audited section of the Remuneration Report. We also apply professional judgement to consider the materiality of Related Party Transactions to both parties.

### Financial statement audit

We are responsible for conducting an audit of the College's financial statements. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; relevant Auditing Standards and applicable Practice Notes issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland. Our findings are summarised in Section 2 of this report.

### Wider Scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on dimensions of wider scope public audit. During our planning procedures we assessed the College as meeting the definition of a smaller body for the purposes of our wider scope audit consideration. As a result of the risks identified following initial audit fieldwork, our assessment was amended and we extended our work to consider financial management and value for money. In 2018/19 we have therefore formed judgements and conclusions on all four dimensions of wider scope public audit:

- Financial management;
- Financial sustainability;
- Governance and transparency; and
- Value for money.

Our findings against each dimension are summarised in Section 3 of this report.



# Financial Statements audit

## Introduction

The annual financial statements provide the College with an opportunity to demonstrate accountability for the resources at its disposal, and report on its overall performance in the application of those resources during the year. We are responsible for conducting an audit of the financial statements of the College and provide an opinion on the financial statements as to:

- whether they give a true and fair view of the state of affairs of the College and its group as at 31 July 2019 and the deficit for the year then ended;
- whether they have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- whether they have been prepared in accordance with the requirements of the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council, the Charities and Trustee Investment (Scotland) Act 2005, and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

This section of our report summarises the audit work undertaken to support our audit opinion, including our conclusions in response to the significant and other risks identified in our Annual Audit Plan.

Our Annual Audit Plan was considered by the Audit and Risk Committee on 14 May 2019. The plan highlighted two areas that we identified as a significant risk of material misstatement or fraud risk:

- the risk of fraud in revenue and expenditure recognition (significant risk); and
- misstatements due to fraud or error (fraud risk).

The plan also highlighted three areas of higher inherent risk within the 2018/19 financial statements:

- Valuation of Property, Plant and Equipment and capital funding;
- Pension Liability and Asset Valuation; and
- Remuneration report disclosures.

Following notification of an internal audit into the payroll system and associated concerns regarding the reliability and accuracy of data within the payroll system, our risk assessment was reassessed. This led to payroll expenditure also being assessed as a significant risk for the purposes of the audit.

## Compliance with financial reporting requirements

As part of our oversight of the College's financial reporting process, we report on our consideration of the quality of working papers and supporting documentation prepared predominantly by the finance team to support the audit.

The financial statements are prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder issued by the Scottish Funding Council, the Charities and Trustees Investment (Scotland) Act and regulation 14 of The Charities Accounts (Scotland) Regulations 2006 (as amended).

## Presentation and quality of financial statements

Exhibit 1 outlines the significant difficulties experienced in receiving draft financial statements for audit. Our previous Annual Audit Reports in both 2016/17 and 2017/18 noted the importance of providing complete financial statements, including front end narrative sections, at the start of the audit. Throughout 2018/19, the College finance team experienced significant staff turnover, which we understand impacted management's capacity to provide the financial statements in line with the initially agreed timetable. This contributed to our revised risk assessment and consideration of the College's overall financial management arrangements, which we report upon within Section 3.

The draft financial statements provided by management were not fully updated from the prior year and did not incorporate new requirements as outlined in the Scottish Funding Council's (SFC) 2018/19 Accounts Direction. We made a significant number of suggestions to enhance presentation and readability, and to ensure compliance with disclosure requirements. We also identified areas where statements were not factually accurate. We are satisfied that management addressed all material comments in the finalised version of the financial statements.

While we worked with the finance team to ensure that the final financial statements are materially compliant with the requirements outlined in the SFC's 2018/19 Accounts Direction, the SORP and FRS 102, the readability and usefulness to the reader must be an ongoing area of focus and improvement in future years, as well as the processes implemented by management to ensure compliant financial statements of a good quality are prepared in a timely manner in advance of the year end audit.

## Group financial statements

The College prepares group financial statements, consolidating the results of the College and its subsidiary undertaking, AST (Engineering) Limited. We are satisfied that the consolidated financial statements have been prepared appropriately with inter-company transactions eliminated in line with accounting requirements. We have also substantially completed the audit of the subsidiary financial statements and expect to issue an unqualified audit opinion.

We have considered the arrangements in respect of the Perth College Development Trust (the Trust). During 2018/19, the Chair and Chief Executive became Trustees. Our updated assessment of the Trust concluded that as the College is now able to exert control over the Trust, the Trust should form part of the College group financial statements. In 2018/19 we agreed with management that this would be an unadjusted misstatement on the basis that the Trust financial position at 31 July 2019 is immaterial to the College's financial statements.

**Recommendation 1:**  
Significant improvements are required to the financial closedown procedures and preparation of the financial statements to ensure timely and accurate completion of financial statements.

Exhibit 1: Timeline for the financial statements

Date	Event	Audit Impact
14 May	Annual Audit Plan agreed <ul style="list-style-type: none"> <li>• Timetable for the audit agreed, including date for final audit fieldwork.</li> </ul>	-
17 September	Internal audit payroll report <ul style="list-style-type: none"> <li>• Series of errors identified by Internal Audit, including errors in National Insurance contributions.</li> </ul>	<ul style="list-style-type: none"> <li>• Additional procedures planned for payroll.</li> </ul>
21 October	Start of audit fieldwork (Visit 1) <ul style="list-style-type: none"> <li>• Client Assistance Schedule issued to Head of Finance set deadline for working papers to be complete by 14 October.</li> <li>• No financial statements available for College or AST and working papers subject to change.</li> <li>• Informed that Head of Finance had resigned.</li> <li>• National Insurance error quantified by Head of Finance as £108,000.</li> </ul>	<ul style="list-style-type: none"> <li>• On 25 October, we contacted the College Vice Principal to raise concerns about lack of preparedness and timescales for the audit committee.</li> <li>• We reviewed and reduced materiality from 75% to 50%.</li> <li>• Payroll reassessed as a significant risk.</li> <li>• Wider scope risk assessment reviewed and scope extended to include Financial Management.</li> <li>• EY team suspended onsite fieldwork on 1 November 2019.</li> </ul>
6 November	Update Call between Finance Team and EY <ul style="list-style-type: none"> <li>• We noted that no financial statements had been prepared and that significant journals, including fixed asset additions and disposals had not been posted and debtors and creditors were incomplete.</li> <li>• Previous Head of Finance, new Head of Finance and Vice Principal committed to produce financial statements by 15 November 2019.</li> </ul>	<ul style="list-style-type: none"> <li>• We agreed to remain off site to allow the Finance Team to focus on the preparation of financial statements.</li> </ul>
18 November	EY audit team onsite fieldwork resumed (Visit 2) Financial Statements received on 15 November 2019, but significant areas where they were non-compliant, including: <ul style="list-style-type: none"> <li>• Key FReM requirements missing such as Performance Analysis, Parliamentary Accountability and Audit Report and Directors Report.</li> <li>• SFC 2018/19 Accounts Direction requirements missing including Cash Budget for Priorities, Depreciation Budget for Government Funded Assets and membership and attendance of the Board.</li> <li>• Other errors and omissions within the Remuneration Report and Corporate Governance Statement.</li> <li>• AST (College Subsidiary) financial statements not prepared.</li> </ul>	<ul style="list-style-type: none"> <li>• Meeting held with Principal and Finance Team to update on progress.</li> <li>• Meeting held with Vice Principal and Finance Team.</li> <li>• Guidance and support provided to update the financial statements.</li> <li>• Significant level of errors identified which led to extended testing, hindered by the College's paper based systems.</li> </ul>

Date	Event	Audit Impact
November	<p>Correspondence received from Audit Scotland</p> <ul style="list-style-type: none"> <li>A number of financial management allegations were made in correspondence to Audit Scotland and the Scottish Funding Council . The SFC requested that UHI Head of Internal Audit investigate and report.</li> </ul>	<ul style="list-style-type: none"> <li>Initial correspondence and calls with UHI Head of Internal Audit to allocate lead roles.</li> <li>Wider scope risk assessment reviewed and elected to apply full scope, including value for money.</li> </ul>
28 November	<p>Version 2 of the Financial Statements</p> <p>Significant remaining areas of non-compliance including:</p> <ul style="list-style-type: none"> <li>FReM Requirements: Parliamentary Accountability and Audit Report and Directors Report, Trade Union Facility Time disclosures.</li> <li>SFC 2018/19 Accounts Direction requirement: Cash Budget for Priorities, Depreciation Budget for Government Funded Assets and membership and attendance of the Board.</li> <li>Other errors and omissions within the Remuneration Report and Corporate Governance Statement.</li> <li>AST (Subsidiary) financial statements not prepared.</li> </ul>	<ul style="list-style-type: none"> <li>Additional review of Version 2.</li> <li>Significant payroll errors identified.</li> <li>Significant errors in accruals.</li> <li>Procurement anomalies identified.</li> </ul>
29 November	<p>Detailed progress meeting held between EY and College Finance Team</p> <ul style="list-style-type: none"> <li>Discussion with Board Secretary and Vice Principal led to arrangements for an extraordinary audit committee meeting.</li> </ul>	<ul style="list-style-type: none"> <li>Outstanding list provided to Finance Team.</li> <li>Audit Scotland advised that College would not be able to publish audited financial statements by the 31 December deadline</li> </ul>
4 December	<p>Update Meeting with Principal and Chair of the Board</p> <ul style="list-style-type: none"> <li>Progress summary discussed.</li> </ul>	<ul style="list-style-type: none"> <li>Ongoing working with UHI Head of Internal Audit.</li> <li>EY audit team withdrew again to allow Finance to work on outstanding areas.</li> </ul>
11 December	<p>Audit Committee</p> <ul style="list-style-type: none"> <li>Audit Partner in attendance to provide progress update.</li> <li>College management identified disclosures to be added to Corporate Governance Statement.</li> </ul>	<ul style="list-style-type: none"> <li>Additional senior involvement in meetings and providing feedback and support for governance disclosures.</li> </ul>
6 January	<p>EY audit team fieldwork resumed (Visit 3)</p> <ul style="list-style-type: none"> <li>Financial statements received, but continuing areas missing or non-compliant, including Cash Budget for Priorities, Adjusted Operating Position, errors and omissions within the Remuneration Report and Corporate Governance Statement.</li> </ul>	<ul style="list-style-type: none"> <li>Final testing undertaken.</li> <li>Impact of level of errors considered on overall materiality.</li> </ul>
5 February	<p>Updated Financial Statements Received</p> <ul style="list-style-type: none"> <li>SFC approval of Adjusted Operating Position received on 13 February 2020.</li> </ul>	<ul style="list-style-type: none"> <li>Additional review and comments on disclosure amendments</li> </ul>

Our testing was conducted over three visits and was impacted by the reduction in materiality, responding to the identified level of audit risk, the level of omissions and errors identified and the paper based systems at the College.

### Impact on the audit

As a result of the significant issues encountered, substantial changes were required to our audit approach. The key changes included:

- Reduction in the material level we applied to the financial statements audit. This significantly increases the level of testing applied as a result of balances being brought within the testing threshold;
- Reassessment of payroll as a significant risk;
- Additional testing as a result of errors identified, to provide overall assurance over balances;
- Key disclosures, including the Remuneration Report requirements were subject to significant revision throughout the audit process.
- Review of multiple versions of the narrative sections of the financial statements which had not been subject to sufficient quality review against the requirements of the SFC's 2018/19 Accounts Direction or HM Treasury Financial Reporting Manual.

Additionally, the time taken to undertake testing was higher than we would normally expect as a result of the paper based system in place within finance.

### Audit outcomes

Management made a number of adjustments following the start of our onsite audit work in relation to:

- the actuarial valuation of the LGPS liability;
- capital additions in the year and associated capital grants; and
- corrections to tuition fee income.

We identified two unadjusted audit differences arising from the audit that breached our reporting threshold. A significant number of adjustments were processed as part of the audit. 31 processed adjustments, along with two unadjusted audit differences arising from the audit. Appendix F identifies 31 adjustments that were processed as part of the audit, including eight that impacted the AST financial statements.

Following substantial revision as part of the audit process, we concluded the other information subject to audit, including parts of the Remuneration Report and the Governance Statement were appropriate.

Our overall audit opinion is summarised on the following page.

# Our audit opinion

Element of opinion	Basis of our opinion	Conclusions
<p><b>Financial statements</b></p> <p>The financial statements provide a true and fair view of the state of affairs of the College and its group at 31 July 2019 and of the deficit for the year then ended</p> <p>The financial statements are prepared in accordance with the financial reporting framework</p>	<p>We report on the outcomes of our audit procedures to respond to our assessed risk of misstatements, including significant risks within this section of our report. We did not identify any areas of material misstatement.</p> <p>We are satisfied that accounting policies are appropriate and estimates are reasonable.</p> <p>We have considered the financial statements against the financial reporting requirements, and additional guidance issued by the SFC and Audit Scotland.</p>	<p>We expect to issue an unqualified audit opinion on the 2018/19 financial statements for Perth College and its group.</p>
<p><b>Going concern</b></p> <p>We are required to conclude and report on the appropriateness of the use of the going concern basis of accounting</p>	<p>We conduct core financial statements audit work, including management's assessment of the appropriateness of the going concern basis.</p> <p>Wider scope procedures, including financial forecasts are considered as part of our work on financial sustainability.</p>	<p>We have no matters to report.</p>
<p><b>Other information</b></p> <p>We consider whether the other information in the financial statements is materially inconsistent with other knowledge obtained during the audit</p>	<p>We conduct a range of substantive procedures on the financial statements. Our conclusion draws upon:</p> <ul style="list-style-type: none"> <li>Review of committee minutes and papers, regular discussions with management, our understanding of the College and the sector.</li> </ul>	<p>We are satisfied that the annual report materially meets the core requirements set out in the Accounts Direction.</p>
<p><b>Report on regularity of income and expenditure</b></p> <p>We are required to consider whether in all material respects the income and expenditure in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by Scottish Ministers</p>	<p>Our procedures include:</p> <ul style="list-style-type: none"> <li>Understanding the applicable enactments and guidance issued by the Scottish Ministers.</li> <li>Performed detailed testing of income and expenditure testing to ensure transactions are in line with enactments and guidance</li> </ul>	<p>We have no matters to report, although we draw attention to procurement matters within our Value for Money assessment on page 33.</p>
<p><b>Matters prescribed by the Auditor General for Scotland</b></p> <p>Audited part of Remuneration Report has been properly prepared.</p> <p>The Performance Report and Annual Governance Statement are consistent with the financial statements and have been properly prepared.</p>	<p>We are required to report on whether the sections of the Remuneration and Staff report, and Accountability report have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and directions made thereunder by the Scottish Funding Council.</p>	<p>We have no matters to report.</p>
<p><b>Matters on which we are required to report by exception</b></p>	<p>We are required to report on whether:</p> <ul style="list-style-type: none"> <li>adequate accounting records have not been kept; or</li> <li>the financial statements and the audited part of the Remuneration and Staff Report are not in agreement with the accounting records; or</li> <li>we have not received all the information and explanations we require for our audit</li> </ul>	<p>We have no formal matters to report but we have made observations and recommendations on the quality of management records.</p>

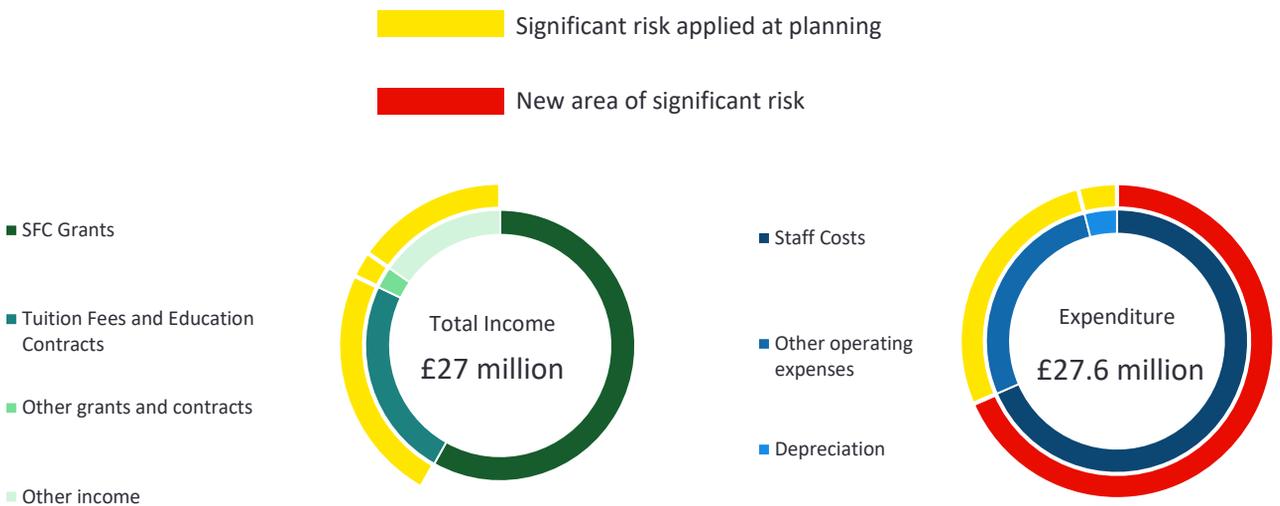
# Significant and fraud audit risks

## 1. Risk of Fraud in Income and Expenditure Recognition

As we outlined in our Annual Audit Plan, ISA (UK) 240 requires us to assume that fraud risk from income recognition is a significant risk. In the public sector, we extend our consideration to the risk of material misstatement by manipulation of expenditure.

In our audit planning, we rebutted the risk of improper recognition of Scottish Funding Council (“SFC”) core grant funding because there is no judgement in respect of this income stream. With regards to expenditure, we rebutted the risk of improper recognition of payroll expenditure at the planning stage however following the identification of weaknesses in the payroll system by internal audit, our assessment changed to incorporate the risk of improper recognition of payroll expenditure. The charts below highlight how our assessment impacts our testing strategy on the College’s financial statements.

Exhibit 2: Key components of the College’s income and expenditure



Source: 2018/19 Financial Statements: Statement of Comprehensive Income and Expenditure

Our testing identified significant misstatements relating to revenue and expenditure recognition. A total of 30 adjustments were required to the financial statements.

### Specific procedures relating to significant risks

We undertake specific, additional procedures over income and expenditure streams where we identified a significant risk, including:

- Review and challenge management's accounting estimates over revenue or expenditure recognition for evidence of bias.
- Review transaction listings for individually material balances as well as unusual items to agree to supporting documentation and third party evidence.
- Test a representative sample of transactions across the remaining income and expenditure population to ensure coverage of testing across all balances.
- Review and test income and expenditure to ensure it is accounted for in the correct financial period.
- Perform a search for material payments and receipts received after year end and ensured these had been accounted for in the correct period.

Our testing identified a number of errors within accrual accounting, where invoices had been processed incorrectly. The level of errors within our initial sample meant that additional testing was performed and we extended our cut off testing.

This level of error highlights the importance of the need for management to quality review both of individual journals, and of the draft financial statements.

### Deferred Income

As part of the 2018/19 planning process, College management identified a number of uncertainties in how it should account for and release deferred income. The Previous Head of Finance highlighted two income streams where information was available elsewhere in the College to support the release of income that had previously been deferred. We worked with the Head of Finance and the Vice Principal – External Engagement to assess the information available at the time of the preparation of the 2017/18 financial statements, and the timing of the completion of milestones. This resulted in a release of income relating to Foundation Apprenticeships (£223,398) and 2016/17 LUPS income (£118,977). We agreed with management that it was appropriate to release the income into 2018/19 as the overall level of income did not breach our materiality level in 2018/19 or 2017/18.

The lack of clear management records, and poor communication between the Finance Department and other departments within the College meant that Finance was unaware of milestone reporting for Foundation Apprenticeships. More generally, we noted that the process to track income streams needs to be strengthened to improve the quality of financial reporting across the College.

**Recommendation 2:**  
The Finance Team must ensure that quality assurance and review processes are in place throughout the year to reduce the risk of fraud or error.

**Recommendation 3:**  
The Finance Team should review the processes to record and track all sources of income.

# Additional Significant Risk Areas

## Payroll

In September 2019, the College's internal auditors drew attention to a number of errors within payroll, including an underpayment of national insurance contributions over the course of three years that was later estimated at £108,000.

While this balance was below our materiality level, in light of the nature of the errors, we reclassified payroll as a significant risk. The College's payroll costs amounted to £17.9 million in 2018/19 and account for around 70% of expenditure.

Management has set aside a provision of £250k within the financial statements to reflect their estimate of the impact across 6 years, along with any penalties that may be necessary.

## Our audit procedures

- Considered the work performed by the College's internal auditors and used this to tailor our audit approach to the most significant risk areas.
- Challenged management's assessment of the national insurance provision and the underlying data used to inform the estimate.
- Tested a sample of employee deductions to ensure both pay and deductions were accurate.
- Reconciled the payroll system to the financial ledger to ensure the completeness of payroll expenditure.
- Performed analytical procedures to ensure payroll costs are consistent with headcount and known pay changes.
- Challenged management's assessment of the annual leave accrual and the underlying data used to inform the estimate.

## Our findings

Our payroll testing identified a number of differences related to pension contribution testing including:

- Incorrect calculation of pensionable pay
- Incorrect rates used for calculating employee pension contributions
- Employees being enrolled in two pension schemes

Management have performed additional procedures, including asking internal audit to estimate the potential financial impact. As a result, we are content that any differences will not breach materiality for the purposes of the financial statements.

We did not identify any other audit matters to report.

# Other Inherent Risk Areas

Our Annual Audit Plan highlighted additional areas of inherent risk. We identified no further areas of risk as part of our audit procedures. The results of our procedures on inherent risk areas are summarised below.

	Our audit procedures	Our findings
<p><b>Valuation of Property Plant and Equipment</b></p> <p>The College's PPE portfolio totals £35.8 million. Our work focused on judgements in relation to the valuation of the College's land and buildings and treatment of deferred capital income.</p>	<ul style="list-style-type: none"> <li>Considered the work performed by the College's external valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work.</li> <li>We undertook procedures to align historic deferred grants to individual assets on the asset register. We confirmed that the deferred grant workings and fixed asset register are consistent</li> <li>We considered changes to useful economic lives as a result of the most recent valuation and tested to ensure that deferred grants are released in line with the assets useful life</li> <li>Analysed the source data and made inquiries at to the procedures used by management's specialist to establish the source data was complete.</li> <li>Challenged management's assessment of the estate valuation at the year end and any indicators of impairment.</li> <li>Verified that the specialist's findings have been correctly processed in the financial statements through testing of accounting entries.</li> <li>Reviewed the College's backlog maintenance estates plans, including consideration of possible indicators of impairment of the existing estate and whether backlog maintenance expenditure in the year had been correctly accounted for as capital or revenue expenditure.</li> </ul>	<p>We reviewed the assumptions used in the valuation of land and buildings for 2018/19. As part of that work we challenge the accuracy and appropriateness of assumptions, and agreed the workings to underlying asset information.</p> <p>Our testing identified a number of adjustments in relation to the disclosure of Assets Held for Sale and timing of additions, outlined in Appendix F.</p>

## Our audit procedures

### Valuation of Pension Liabilities

The College's pension fund deficit is a material estimated balance. Under the Higher and Further Education SORP (2015), the liability is disclosed on the College's balance sheet. At 31 July 2019, the College's share of the pension scheme net liability totalled £5.683 million (2017/18: £2.883 million).

Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. The information disclosed is based on the FRS 102 report issued to the College by the actuary. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

We have focused on the following areas, which are consistent with those of management:

- The reasonableness of the underlying assumptions used by the College's actuary, including those associated with recent judgements on McCloud and Guaranteed Minimum Pensions (GMP).
- Ensuring the information supplied to the actuary in relation to the College was complete and accurate.
- Ensuring the accounting entries and disclosures made in the financial statements were consistent with the actuary's report.

We have liaised with the appointed auditor of the Tayside Pension Fund to obtain assurances over the information supplied to the actuary in relation to the College.

We have assessed the work of the Pension Fund actuary including the assumptions they have used by utilising our in-house experts. We have assessed both the robustness of the methodology used to derive the key actuarial assumptions and the reasonableness and consistency of the assumptions underpinning such reports, using guidance available.

We performed additional testing on the College's share of the Fund pension assets at 31 July, performing roll forward procedures on its share of assets from 31 March to the College balance sheet date.

We assessed the approach taken by the actuary to account for the estimated impact of the recent rulings made around the McCloud judgement and various rulings around GMP.

## Our findings

The actuarial valuation report that the College obtained to support the draft financial statements had accounted for the impact of McCloud and the pre-2016 impact of GMP.

We have considered the reasonableness of the reported asset position and note that the actuary's estimated investment returns were consistent with actual investment returns for Tayside Pension Fund.

Assumptions used by the actuary and adopted by the College are considered to be generally acceptable. The sensitivities surrounding these assumptions have been correctly disclosed in the notes to the financial statements.

# Looking ahead

## Recommendation 4:

The College should conduct an impact assessment on the implementation of the revised SORP.

### **Updated Statement of Recommended practice: accounting for further and higher education 2019 edition**

The Statement of Recommended Practice (SORP): accounting for further and higher education has been updated to reflect the amendments made to FRS 102 following its triennial review in 2017. The revised SORP will be effective for financial periods beginning on or after 1 January 2019 and therefore will be applied by the College within their 2019/20 financial statements.

The triennial review was published by the Financial Reporting Council in December 2017. The majority of amendments were editorial in nature and clarified rather than changed accounting treatment. The amendments to the SORP follow a similar basis and it is not therefore anticipated that the College will be required to adopt substantive changes to accounting treatments. We do, however, expect that the College will be required to adopt a number of changes to disclosure requirements.

We will work with management during 2019/20 to ensure the correct application of the new requirements.



# Wider Scope Dimensions

## Introduction

Under Audit Scotland's Code of Audit Practice (May 2016), we are required to reach conclusions in relation to the effectiveness and appropriateness of the College's arrangements for wider scope audit dimensions. We apply our professional judgement to risk assess and focus our work on each of the dimensions.

As in previous years, and in accordance with Audit Scotland planning guidance, within the Annual Audit Plan we assessed that it was appropriate to classify the College as a smaller body for the purposes of our wider scope audit consideration, and our work would be limited to considering financial sustainability and the annual governance statement.

As a result of significant changes impacting the College, during audit fieldwork we reviewed and revised our risk assessment. Key factors influencing our wider scope assessment included:

- significant turnover within the finance team, including the resignation of the Head of Finance in October 2019;
- the impact of the College's updated financial planning; and
- correspondence received by Audit Scotland in relation to the College.

As a result, we extended the scope of our work to address each of the four wider scope audit dimensions.

## The Wider Scope dimensions

- **Financial Sustainability:** Considers the medium and longer term outlook to determine if planning is effective to support service delivery, including arrangements to develop viable and sustainable financial plans.
- **Financial Management:** Considers the effectiveness of financial management arrangements, including the adequacy of financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.
- **Governance and Transparency:** Considers the effectiveness of governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.
- **Value for Money:** Considers whether best value can be demonstrated in the use of resources, and that there is a clear focus on improvement.

The scope of our audit was significantly extended as a result of the identification of additional risks at the College.

# Financial Management

The College has experienced significant turnover within the finance team over a period of 18 months. In December 2018, the previous Chief Operating Officer left the College. These factors have had a significant impact on the capacity and capability of the finance team and the College's ability to provide the Board with the strategic financial planning support that it needs. During the year, Board members highlighted that key financial reports provided late or verbally undermined their ability to fully discharge their responsibilities.

In our view, there is significant scope to improve the quality of financial reporting by providing focused analysis on significant budget movements, the impact of key strategies and the forecast outturn position. Our work has identified ongoing weaknesses in internal controls, including lack of effective management review. The College did not fully participate in the NFI exercise within the timetable set by Audit Scotland and NFI is not yet embedded within the College's Fraud Policy and Response Plan.

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## Recommendation 5:

The College must review the capacity and capability within the Finance Team to ensure that skills gaps are addressed.

The Board needs to urgently ensure that there are appropriate arrangements established to provide strategic financial leadership.

## Finance Team

The College has experienced significant turnover within the finance team over a period of 18 months. In December 2018, the Chief Operating Officer (COO) left the College. College management elected to take the opportunity to release savings and enhance academic representation on the SMT, rather than replacing the position. Throughout the audit, we found that organisational knowledge has been significantly impacted by the departure of long-serving team members. In our view, the College's capacity to provide the Board with strategic financial planning has also been impacted by the loss of the COO role.

We have been unable to find evidence that the Board considered options for the finance team structure, but a paper to the Remuneration Committee in September 2019 refers to a number of alterations that were made to the responsibilities of the remaining Senior Management Team (SMT) members when the role of COO was removed from the structure in December 2018. We would expect a decision of this significance to be considered by the Board. We have also noted that none of the current members of the SMT has a financial background.

The College's Head of Finance resigned in October 2019, shortly before the commencement of our final audit fieldwork. During the year, the Financial Accountant role was performed by a number of interim appointments, before the role was filled permanently in November 2019. We consider that the Finance Team overall has had insufficient knowledge and experience, particularly in financial accounting, since December 2018.

## Financial Reporting

## Recommendation 6:

Financial reporting must be significantly improved to support Board member scrutiny.

Financial updates were presented at each meeting of the Finance and General Purposes (F&GP) Committee. As we outline in Exhibit 3, financial reporting was inconsistent, late and often verbal.

The 2019/20 budget was not formally considered by the Board or F&GP Committee until the financial year had commenced. Similarly, the Financial Forecast Return was not formally approved until after it had been submitted to the SFC.

**Exhibit 3: Financial Reporting to Committees did not adequately support Board member scrutiny**

Committee	Papers Due	Late	Verbal	Commentary
February 2019 F&GP Committee	Management accounts: 6 months to 31 January 2019			Received 5 months to 31 December 2018
	Group Forecast			
May 2019 F&GP Committee	Management Accounts: 9 months to 30 April 2019			
	Group Forecast			
	2019/20 Indicative Budget			No papers provided. Action to present to June Board meeting
June 2019 Board of Management	2019/20 Indicative Budget			Paper removed from agenda. Verbal update provided. Chair asked for a note to be circulated from the Principal.
Sept 2019 F&GP Committee	Management accounts to 31 July			We understand an outline paper was tabled at the meeting
	2019/20 budget proposals			
	Financial Forecast Return to SFC			Due to be submitted to the SFC 30 September 2019
Oct 2019 Board of Management	2019/20 Budget			Considered by Board 4 months into the financial year
	Financial Forecast Return			Approved after submission to the SFC

Verbal and late papers to governance committees mean that Board members are given insufficient opportunity to perform their role effectively. The lack of timeliness of papers meant that insufficient scrutiny was given to the FFR prior to submission to the SFC. The Board was forced to seek additional information from the Principal outwith the Board cycle to provide assurance on the 2019/20 budget.

Source: Perth College Committee Papers 2019

Board members increasingly highlighted their frustration at the lateness of papers and noted that this impacted their ability to effectively and adequately scrutinise financial performance. Additional updates were requested from the Principal during 2018/19, and the Board has disclosed this as a significant concern within the Governance Statement.

We have reviewed financial updates presented during the year and, where possible, evaluated the quality of content provided. We note that the management accounts changed format during the year to provide additional detail. This level of detail may obscure key messages about the overall financial health of the College. There is significant scope to improve the quality of financial reporting by providing focused analysis on significant budget movements, and the forecast outturn position.

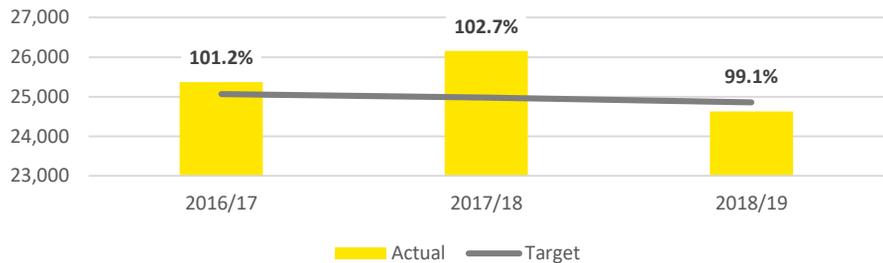
## Financial Performance

The College reported a consolidated deficit of £0.243 million for the year (2017/18: £1.45 million deficit). Following an actuarial loss of £1.7 million (2017/18: actuarial gains of £7.1 million), the College reported total comprehensive expenditure of £1.9 million (2017/18: £5.6 million income).

The College had an adjusted operating surplus after removal of non-cash accounting adjustments (relating to pension and capital accounting adjustments) of £1.27 million (2017/18: surplus of £1,000).

As Exhibit 4 demonstrates, in 2018/19 the College did not achieve the full allocation of credit targets. An activity target of 24,855 credits was allocated to the College from the SFC. The College achieved all of its core targets, but only 972 of the 1,200 European funding target.

**Exhibit 4: The College did not achieve all of its credit targets in 2018/19**



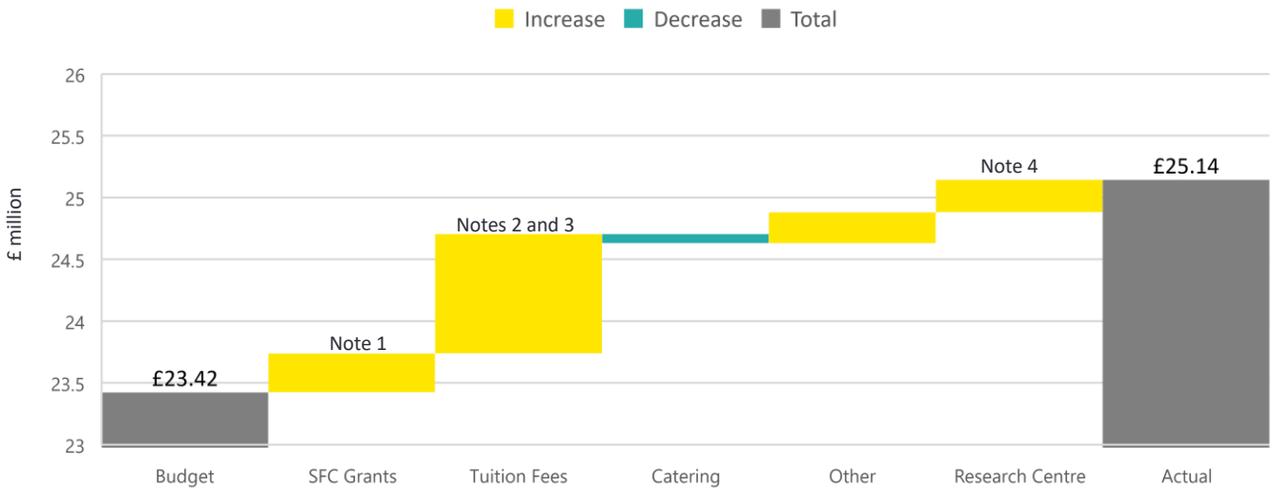
Source: Scottish Funding Council

## Financial Monitoring

The College's 2018/19 budget was approved in September 2018 by the Finance and General Purposes (F&GP) Committee. The College budgeted a group deficit of £127,000 prior to accounting for FRS 102 pension adjustments. The Head of Finance indicated that the actual position was broadly in line with budget within the financial monitoring reports until the final, tabled, management accounts paper in September 2019. This indicated that the College would achieve an underlying surplus of £491,000.

Exhibit 5, highlights that the key reason for the improved projection related to increased income. Income in 2018/19 was £1.7 million higher than budget, partly as a result of the release of deferred income as a result of previous weaknesses in record keeping and communication across the College.

**Exhibit 5: The College’s income was significantly higher than budgeted within financial monitoring reports**



**Notes:**

1. SFC Grants increased primarily as a result of additional income related to curriculum development.
2. Income relating to LUPs European Social Fund exceeded management expectations. As a result of the likelihood of missing the target, no account was taken for LUPS income within the budget. Income of £272,000 was confirmed by UHI in December 2019. The potential volatility of this funding was noted by the F&GP Committee in March 2018, and an action was agreed to report the income separately within Financial Monitoring reports. This was not evident during 2018/19.
3. The Tuition fees and Education Contracts balance includes the release of 2017/18 deferred income relating to Foundation Apprenticeships (referred in Appendix F), totalling £223,398.
4. The release of research income grant relating to Mountain Studies was not fully budgeted, leading to an increase in income of £388,000.

Source: Perth College Management Accounts and External Audit 2018/19

**Systems of internal control**

The Board of Management is responsible for ensuring that an effective system of internal control is in place. Throughout our audit of the financial statements, we have tested the design and implementation of key controls related to areas of significant risk to the financial statements. This work has included documenting the key internal financial controls and performing walkthroughs to ensure controls are operating as designed. Our work has identified ongoing weaknesses in internal controls, including:

- Reliance on paper based systems, which led to problems in relation to the retention of financial records.
- Lack of segregation of duties, including inadequate review of journal entries and lack of purchase orders.
- Financial systems that have not been kept up to date, including the payroll system, or are not fit for purpose, such as the fixed asset register.
- Significant delay in the transition to the Government Banking Service leading to the maintenance of unnecessary bank accounts.

**Recommendation 7:**  
The College must improve key financial controls to ensure that the weaknesses identified are addressed at pace.

**Recommendation 8:**  
The College should ensure that the Fraud Response Plan is updated to reflect the investigation of matches identified through the NFI exercise.

### **National Fraud Initiative (NFI)**

NFI is a counter-fraud exercise co-ordinated by Audit Scotland and overseen by the Cabinet Office to identify fraud and error. The NFI exercise produces data matches by comparing a range of information held on public bodies' systems to identify potential fraud or error.

The College was asked to conduct a self assessment by the end of February 2019 to allow us to report on our assessment of the College's participation in the exercise to Audit Scotland in June 2019. The self assessment was not conducted and no testing was conducted on the matches identified until after Audit Scotland had written to the College on two occasions. We therefore concluded that the College has not fully participated in the NFI exercise within the timescales set by Audit Scotland and that it is not yet embedded within the College's Fraud Policy and Response Plan.

We do, however, note that the College has subsequently reviewed each of the matches highlighted during the NFI exercise, and as a result has concluded that there are no anomalies which require further investigation.

# Financial Sustainability

The College submitted its Financial Forecast Return to the Scottish Funding Council in September 2019. The Board received insufficient time or support to be able to challenge key assumptions effectively. The FFR has not been subject to the level of scenario planning we would expect. In our view, the FFR does not present a robust medium term financial plan and cannot, therefore provide adequate assurance to the Regional Strategic Body or the Scottish Funding Council that financial risks are being managed effectively.

The College has established ambitious plans to diversify income within the draft Business Development and International strategies. While these strategies are work in progress, financial monitoring reports provide insufficient detail at this stage to allow the Board to track the delivery of key strategies. All strategies of this nature present a risk that income will not be delivered as planned. The College must therefore ensure that financial monitoring reports are robust and aligned to the delivery of strategic plans.

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## The context for financial sustainability in the College sector

In June 2019, Audit Scotland published their annual report on the further education sector, *Scotland's Colleges 2019*. The report provides an overview of college finances based on the latest annual financial statements and financial forecast returns. The sector reported an improved, but marginal underlying surplus in 2017/18 but the report notes a widening gap between college's income and expenditure. Twelve incorporated colleges forecast recurring financial deficits by 2022/23.

Scottish Government revenue funding to the sector has increased year on year since 2016/17 in real terms, but this increase has solely related to funding the costs of harmonising staff terms and conditions. This means that there has been limited additional funding for cost pressures such as cost of living increases, increases in employer pension contributions and inflationary cost increases.

Reduced capital funding poses a risk to some colleges' ability to continue to deliver their core services in a safe environment and to invest in new technologies to generate efficiencies and enhance the student experience.

## Medium term financial strategy and plan

The College prepared five-year financial forecasts for the period 2019 to 2024 and submitted these to the SFC in the form of the template Financial Forecast Return ('FFR') in September 2019. The forecast was based on assumptions provided by the SFC in addition to College specific assumptions for areas such as the impact of EU withdrawal and other income. The assumptions were subject to review by the College's senior management team in late September 2019 and the Finance & General Purposes Committee considered a tabled update from the Head of Finance on 23 September 2019.

The Board of Management was presented with the FFR in October 2019, following submission to the SFC.

**Recommendation 9:**  
The Financial Forecast Return should be presented in sufficient time to ensure that the Board has an opportunity to influence key assumptions prior to submission.

**Exhibit 6: The College's FFR has been developed to forecast a balanced underlying position from 2020/21.**



Source: Perth College Financial Forecast Return, September 2019

**Financial Planning**

The Scottish Funding Council issued guidance on the assumptions and information required from Colleges in June 2019. The guidance is developed in conjunction with sector representatives to provide information on key assumptions to be applied to ensure that the SFC can understand the financial health and projections of the sector as a whole. We note within Exhibit 6, above, that projections within the College's FFR for staff costs have been reduced to reflect the savings required to return a balanced position, rather than as a result of an effective workforce plan. While a staffing model is in development, more work is needed to ensure that a workforce plan is in place that is driven by curriculum and development need. We note that consultation is underway to develop a targeted voluntary severance plan.

**Recommendation 10:**  
The College urgently needs to develop effective medium term financial planning. This should be supported by scenario planning and ongoing monitoring.

There are a number of significant developments underway over the period of the FFR. The College has ambitious plans in place within the Business Development Strategy and International Strategy to increase income, particularly from non-EU countries such as China, Japan and Kuwait. As a result, the FFR projects that other income will rise from £4.4 million in 2018/19 to £7.1 million. The College has also outlined plans to develop an aviation centre as part of the Tay Cities Deal.

All income generation strategies present a risk that they will not be delivered as planned, which may place additional pressure on the College's financial position. The International Strategy has principally been developed on the basis of the growth of students alongside new programmes with existing international partners. The College's international income forecast for 2019/20 is £0.876 million, 98.9% of the target set within the strategy, although the full impact of coronavirus is not yet clear.

There are, therefore, a number of significant variables that are outwith the College's control. The FFR has not been supported by the level of scenario planning that we would expect to see to allow effective scrutiny and challenge by the Board. While strong steps have been taken to diversify income, and to reduce the College's staff costs, in our view, the FFR does not present a robust medium term financial plan and cannot, therefore provide adequate assurance to the RSB or SFC that financial risks are being managed effectively.

### Key risks and uncertainties

The College has identified the 6 most significant risks that may impact the delivery of the FFR (Exhibit 7 below).

#### Exhibit 7: The College has identified 6 key risks that pose a risk to the College's ability to achieve the FFR and thus impacting their ability to be sustainable in the medium term

Risk title	Description	Risk mitigating actions
Brexit	Perth College Senior Management Team (SMT) recognise the potentially material impact of the ongoing Brexit process to student numbers, EU based funding streams and consequently, the future financial sustainability of the College. SMT make specific note of the time bound guarantee by the SFC for EU Student Tuition Fees ending after 2020/21.	<b>International Delivery Strategy</b> <ul style="list-style-type: none"> <li>The second phase in 2019/20 sets stretch income targets for International income of £900k to be delivered by increases in established International partnerships in China and Japan.</li> <li>Phase 3 will commence in 2022. Countries identified as target emerging markets include Vietnam, Malaysia and Thailand.</li> </ul>
UHI Academic Partners' reliance on SFC core funding	Funding dependency is a material risk to the financial sustainability of the College. This reliance is further exacerbated by 95% of the student body being made up of home domiciled students.	<ul style="list-style-type: none"> <li>Business Development to focus on supporting the region in growth Industries such as Health &amp; Social Care and Construction and capitalise on already strong partnerships in Flexible Workforce Development, Foundation/Modern/Graduate Apprenticeship and wider Industry.</li> </ul>
Non-achievement of student number targets	As with all other Scottish Colleges, the College recognise the impact of the Widening Access Agenda on student recruitment numbers.	<ul style="list-style-type: none"> <li>Develop existing relationships with regional feeder institutions including Schools and local businesses.</li> <li>Full curriculum review to review, realign and optimise our academic delivery.</li> <li>Active participation in the UHI partnership model, with the objective of Partnership Sustainability.</li> </ul>
Estate condition and digital estate	The findings of the Backlog Maintenance Report carried out during 2017/18 demonstrates the immediate requirement of significant financial investment in the campus.	<ul style="list-style-type: none"> <li>Capital Funding to optimise value for money in all Estates works.</li> <li>Development of Digital Estate Strategy.</li> <li>Tay Cities Deal project for the creation of a purpose built Aviation Academy on the College Estate.</li> </ul>
Non-funded cost of living impacts	The financial impact of non funded National Bargaining Funding.	Strategic review of internal structures, full curriculum review and reassessment of all academic delivery approaches. It is planned to carry forward a small surplus from 2018/19 for the purposes of implementing a longer term financial sustainability plan through the creation of a re-aligned College structure.

Source: Perth College FFR September 2019

# Governance and Transparency

While the College has a number of key features of good governance in place, there is a risk that Board members are not provided with enough support or information to fully discharge their responsibilities. The Board did not consider financial monitoring reports or the risk register during the year. We also noted a number of significant decisions, including the structure of the Senior Management Team and the use of settlement agreements, were not, in our view, subject to adequate scrutiny.

Management's assessment of compliance with the Code of Good Governance identified two areas of non-compliance. The College also disclosed a number of other significant control weaknesses within the Governance Statement, including the failure to produce and finalise financial statements by the deadline set within the Accounts Direction. We also note that the College's internal auditors have drawn attention to limited progress made to date in implementing internal audit recommendations.

## Governance arrangements

The College has taken steps to improve governance arrangements. A review of Board effectiveness was undertaken in February 2019, which was supported by the College's internal auditors. The College also considered and reported on a self assessment against the quality framework "How Good is Your College?" in the Evaluation Report and Enhancement Plan for 2019-21. A number of the key requirements for good governance are in place, including :

- All Board and committee papers and minutes are available on the College's website to promote openness and transparency;
- The Chair has conducted an evaluation of the performance of individual members on a one to one basis;
- The Board has approved detailed terms of reference for its standing committees which are subject to regular review.

However, during our audit work we noted a number of instances where reporting to the Board was ineffective and may not support Board members' specific responsibilities as charitable trustees. Examples include:

- Key decisions on the structure of the Senior Management Team, including the use of settlement agreements, was not reported to the Board.
- In some instances, papers presented to the Board were not clear about the decisions that members were being asked to make and the minutes did not fully reflect the level of discussion.
- The 2018/19 budget was approved by the Finance and General Purposes Committee in September 2018. The Board did not consider budget papers, but noted the minutes of the relevant committee. The 2019/20 Budget was approved in October 2019, following the start of the financial year.
- The Board did not receive the risk register or financial monitoring updates in 2018/19.

**Recommendation 11:**  
We understand that the College will receive an external evaluation of its governance arrangements by December 2020. This review should consider the quality of reporting, and be informed by the specific responsibilities of charitable trustees.

## Annual Governance Statement

We reviewed the Governance Statement within the financial statements against the requirements outlined in the SFC's 2018/19 Accounts Direction. This includes the requirements to conclude on the College's compliance with the 2016 Code of Good Governance for Scotland's Colleges, or to explain any areas of non-compliance. Our consideration of the governance statement has included:

The College has disclosed a number of weaknesses within the Governance Statement.

- Ensuring that the College has met all requirements of the SFC's 2018/19 Accounts Direction
- Ensuring that the content of the statement is consistent with our understanding of the College's governance arrangements and any issues identified during the year
- Ensuring that the College has performed a self assessment of compliance with the Code of Good Governance for Scotland's Colleges and that this assessment is reflected.

As a result of this review, the College used the Governance Statement to make a number of disclosures about weaknesses identified during the year, including:

- Procurement weaknesses, including the lack of purchase orders and failures to comply with procurement rules (refer to Page 34);
- The failure to seek approval for settlement agreements, in line with the requirements of the Financial Memorandum;
- Payroll weaknesses identified by management and investigated by the College's internal auditors;
- Failure to comply with the Board's equality duties, including publication of the equality outcome and mainstreaming report by April 2019;
- Failure to produce financial statements in line with the deadline set within the 2018/19 Accounts Direction.

**Recommendation 12:**  
The College should review the quality of the Governance Statement against good practice guidance to ensure that it meets users needs.

Management's assessment of compliance with the Code of Good Governance noted two areas of non-compliance in 2018/19, which have also been disclosed within the governance statement.

The Accounts Direction 2018/19 drew attention to the *Good Practice Note on Improving the Quality of College Annual Report and Accounts – Governance Statements*, which was published by Audit Scotland in May 2019. There was no evidence of review against the good practice note to improve and streamline the Governance Statements. As a result, in our view, the Statement does not focus on how governance arrangements effectively manage risk to support the College's Corporate Strategy.

## Internal audit

The College's internal audit service provides an important source of assurance to inform management and the Board's assessment of the College's governance arrangements. We have reviewed the internal audit annual report for 2018/19. Internal audit's opinion for the year was based on its agreed audit plan for 2018/19, as amended and approved by the Audit Committee. For 2018/19 the annual statement of assurance notes that in Internal Audit's opinion, the College has adequate and effective arrangements for risk management, control and governance, with the exception of three significant issues identified during the year:

The HR and Payroll Systems, issued in September 2019, identified a significant number of issues regarding payroll transactions, with some staff being underpaid and others being overpaid. There were a range of weaknesses in existing processes including user access permissions, weaknesses that could allow HR and Payroll staff to generate unauthorised payments, and payroll variance reports and monthly payroll checklists were not always held on file or were not signed as evidence of formal review.

Testing on national insurance contributions examined payments over the three preceding financial years highlighted an underpayment of contributions. A voluntary disclosure has subsequently been made to HMRC and provision has been made within the financial statements for management's estimate of the financial impact.

Internal audit also noted that the College has made limited progress in implementing internal audit recommendations. Internal audit noted that only four of the 19 recommendations that were due to be implemented have been assessed as fully complete.

## Risk management

The College has an established Strategic Risk Management process. The College's approach to risk management is set out within the risk management policy, which is available on the College website. This was formally approved by the Board in 2016 and most recently reviewed in 2018. The Senior Management Team regularly considers and updates the College's risk register.

Throughout 2018/19, the key strategic risks were reported to and monitored by the Audit Committee at each of their meetings. We do, however, consider that the Board should formally review the risk register as part of its overall assessment of progress against the Strategic Plan and that further work is required to embed risk management across the College.

While risks remain for all public sector bodies, we are satisfied that the College's arrangements to prepare for EU withdrawal are appropriate and informed by wider sector involvement.

### EU withdrawal

As in 2017/18, Audit Scotland has maintained an interest in public bodies' preparedness for EU withdrawal. We assessed the College's arrangements against three key factors, relating to the workforce, funding and regulations.

The College's response and preparations for Brexit have been led by the SMT. Brexit is a key risk within the College's risk register and has been subject to regular updates throughout the year. The Plan draws on external guidance including publications from the Scottish Funding Council. The College has undertaken a range of actions, including:

- identifying individuals that may be directly impacted, including staff and students both currently enrolled in courses and applicants for next year;
- evaluation of the expected financial impact, including European Social Funding and tuition fees; and
- development of the Business Development Strategy and International Strategy to diversify income in the future.

### Correspondence received from Audit Scotland

During the course of the audit, we were advised of correspondence that Audit Scotland had received as part of their arrangements to allow members of the public to raise issues of concern. The correspondence was highlighted a number of areas of concern in relation to financial management and governance weaknesses. The Scottish Funding Council was also made aware of the allegations, and requested that the UHI Head of Internal Audit lead an investigation of the allegations. While not formally relying on the work of internal audit, we have liaised to ensure that we have not unnecessarily duplicated findings and recommendations.

We considered the implications of the UHI Head of Internal Audit report. We will follow up the status of improvement actions along with the recommendations outlined in Appendix D as part of our 2019/20 audit. We have agreed with the College that a formal follow up will be undertaken in May 2020 to inform reporting on progress to the Board and committees.

### National Reports

It is important that the College has embedded arrangements to ensure that consideration is appropriately given to national reports published by Audit Scotland. At present, national reports are reviewed by management and the impact on the College is considered. These will be presented to the Board or relevant committee where necessary. The Board should consider ensuring that key national reports are shared with Board members as a matter of course.

# Value for Money

The College has reviewed the effectiveness of balanced scorecard reporting during 2018/19, but the current scorecard does not provide metrics for key indicators. The Board received only an interim performance report for 2018/19; 40% of targets that can be measured have not been achieved.

Significant procurement weaknesses were identified and disclosed within the College's governance statement.

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## Strategic Plan 2019-21

The College's Strategic Plan 2019-21 was published in June 2016. Performance has been reviewed against the four strategic objectives within a balanced scorecard covering:

- Students and staff achieving their potential;
- Sustainability;
- Student activity measures; and
- Student Satisfaction

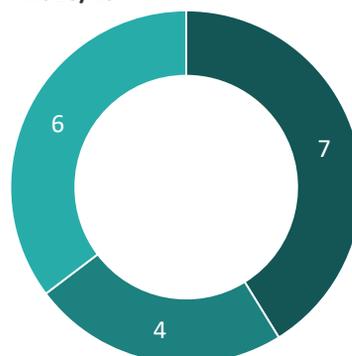
**Recommendation 13:** Performance reporting should be reviewed to ensure that it is timely and provides sufficient information to allow robust scrutiny.

Throughout 2018/19, the College reviewed the format of the Balanced Scorecard, which included consultation with relevant committees. However, the College has not yet fully reported on performance for 2018/19 against priorities. An interim progress report was presented to the Board in December 2019. This included information gaps, particularly against Student Activity Measures.

Exhibit 8 highlights that the College missed the target for over 40% of the measures for which data is available.

### Exhibit 8: College missed the target set for over 40% of the key performance indicators reported to date in 2018/19

- Missed target
- Progress maintained
- Target achieved



Source: Perth College Balanced Scorecard Interim Report, December 2019

**Recommendation 14:**  
The College must ensure that procurement weaknesses are addressed as a matter of urgency.

### **KPI reporting**

We reviewed the College's approach to public reporting and note that the College has a dedicated area of the website for Performance Indicators and External Review. The College has published the results for 2018/19, with its commentary in January 2020. However, we noted that reporting was limited to the indicators adopted and published by the SFC, rather than the wider performance measures that the College has assessed as key to delivering the Strategic Plan.

### **Procurement arrangements**

During 2018/19, College management identified a number of areas of potential procurement weaknesses. To allow the College to understand the issues, the Head of Supply Chain for the UHI Partnership completed an audit of the College's systems, processes and procedures and found areas of non-compliance for improvement.

The College has seconded a Procurement Manager from APUC to support improvements, but during the audit we identified a number of areas of weaknesses including:

- The catering contract has significantly evolved since the last formal tendering exercise in 2004. The College has worked in collaboration with the contractor to enhance the student experience, attainment and achievement rates by providing a real-life training environment for hospitality students. The project is unique in the sector and has been extended year on year to allow the collaborative model to develop and mature. The College has now taken steps to define the critical requirements within the partnership and the full catering contract, including the aspects associated with the student experience project, will be subject to public tender in March 2020.
- A non-competitive quote was used to procure building works with a value of £98,265 without justification or approval of the Regional Strategic Body. We do, however, understand that College management had earmarked this project to be funded through the use of a capital receipt that had not drawn upon public funds.
- For the vast majority of purchases subject to audit (over 80%), no purchase orders were completed.

The College has identified a number of improvement actions, including the development of a contracts register to identify contracts that are due for retender and the revision and update of the Procurement Strategy.

As part of the improvements made to the financial statements, the College also disclosed the weaknesses within the 2018/19 Governance Statement.



# Appendices

A – Code of Audit Practice: responsibilities

B – Independence and audit quality

C – Required communications with the Audit and Risk Committee

D – Action plan

E – Follow up of prior year recommendations

F – Adjusted errors identified during the audit

G – Timing and deliverables of the audit

# Appendix A: Code of Audit Practice Responsibilities

## Audited Body's Responsibilities

### Corporate Governance

Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.

### Financial Statements and related reports

Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:

- preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation.
- maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.
- ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.
- maintaining proper accounting records.
- preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body.

Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.

Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.

### Standards of conduct / prevention and detection of fraud and error

Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.

### Standards of conduct / prevention and detection of fraud and error

Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- such financial monitoring and reporting arrangements as may be specified
- compliance with any statutory financial requirements and achievement of financial targets
- balances and reserves, including strategies about levels and their future use
- how they plan to deal with uncertainty in the medium and longer term
- the impact of planned future policies and foreseeable developments on their financial position.

### Best Value

The Scottish Public Finance Manual sets out that accountable officers appointed by the Principal Accountable Officer for the Scottish Administration have a specific responsibility to ensure that arrangements have been made to secure best value.

# Appendix B: Independence and audit quality

Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the College.

## Matters that we are required to communicate

The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY), its directors and senior management and affiliates, and you, including all services provided by us and our network to you, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 August 2018 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

## Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan, dated 14 May 2019.

We complied with the Financial Reporting Council's Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that management and members of the Board consider the facts known collectively to you and come to a view.

## Audit Fees

As we outline within Exhibit 1 to this report, the scope and level of testing required to finalise our opinion on the financial statements has been substantially increased. We have signalled to management that there will be a significant level of fee variation to reflect the scale of work required.

We will discuss the level of fee variation with Audit Scotland, along with the Principal and Vice Principal – External Engagement and report our final fee to a future meeting of the Audit Committee.

	2018/19	2017/18
<b>Component of fee:</b>		
<b>Total agreed auditor remuneration</b>	<b>£18,280</b>	£14,930
Fee variation	<b>£TBD</b>	-
Audit Scotland fixed charges:		
Pooled costs	<b>£880</b>	£960
Audit support costs	<b>£930</b>	£830
<b>Total fee</b>	<b>£TBD</b>	£16,720

Matters that we are required to communicate

International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

The EY 2019 UK Transparency Report, can be accessed on our website at [https://www.ey.com/Publication/vwLUAssets/ey-uk-2019-transparency-report/\\$FILE/ey-uk-2019-transparency-report.pdf](https://www.ey.com/Publication/vwLUAssets/ey-uk-2019-transparency-report/$FILE/ey-uk-2019-transparency-report.pdf). The report explains our outlook and how we are structured and governed, including the role of our Independent Non-Executives and how we apply the requirements of the UK's Audit Firm Governance Code. We refer to the quality of our audits and our commitment to recruiting, developing and diversifying our people and talent pool. We also explain how we manage our risks and remain innovative and technologically advanced in what we do and how we do it.

Maintaining high audit quality across all of our engagements is of paramount importance to us. Our transformational Audit Quality Programme continues and is a part of the global EY Sustainable Audit Quality Programme (SAQ).

Our Audit Quality Board (AQB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AQB meets monthly and also holds an annual strategy session. The AQB reports to the EY UK Board. The AQB receives regular updates on regulatory matters, results of internal and external reviews, results of root cause analysis, resourcing, the SAQ programme and pursuit approvals, as well as a comprehensive dashboard on quality measures.

Our Audit Quality Support Team (AQST), which started within the SAQ programme, reviews 40 to 50 audits each audit cycle providing challenge and guidance to the engagement teams. These are in-depth reviews carried out by experienced auditors independent of the audit team. AQST reviews enhance the quality of both the audit under review and other audits on which team members apply the lessons learned. The AQST has now become a business-as-usual function.

Audit Quality Framework / Annual Audit Quality Report

Audit Scotland's Appointments and Assurance Team are responsible for applying the new Audit Quality Framework across all financial audits and performance and Best Value audits. This covers the quality of audit work undertaken by Audit Scotland staff and appointed firms. The team are independent of audit delivery and provide assurance on audit quality to the Auditor General and the Accounts Commission.

We support Audit Scotland in their commitment to reporting on audit quality through responding to requests for information and providing the results of internal quality reviews undertaken in respect of relevant public sector audits in Scotland.

The most recent audit quality report which covers our work since appointment can be found at: [www.audit-scotland.gov.uk/uploads/docs/report/2018/as\\_audit\\_quality\\_1718.pdf](http://www.audit-scotland.gov.uk/uploads/docs/report/2018/as_audit_quality_1718.pdf).

# Appendix C: Required Communications

Required communication	Our reporting to you
<p><b>Terms of engagement / Our responsibilities</b></p> <p>Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.</p> <p>Our responsibilities are as set out in our engagement letter.</p>	<p>Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice</p>
<p><b>Planning and audit approach</b></p> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>	<p>Annual Audit Plan</p>
<p><b>Significant findings from the audit</b></p> <ul style="list-style-type: none"> <li>• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>• Significant difficulties, if any, encountered during the audit</li> <li>• Significant matters, if any, arising from the audit that were discussed with management</li> <li>• Written representations that we are seeking</li> <li>• Expected modifications to the audit report</li> <li>• Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	<p>Annual Audit Plan</p> <p>Annual Audit Report</p>
<p><b>Going concern</b></p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>• Whether the events or conditions constitute a material uncertainty</li> <li>• Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>• The adequacy of related disclosures in the financial statements</li> </ul>	<p>Annual Audit Report</p>
<p><b>Misstatements</b></p> <ul style="list-style-type: none"> <li>• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation</li> <li>• The effect of uncorrected misstatements related to prior periods</li> <li>• A request that any uncorrected misstatement be corrected</li> <li>• Corrected misstatements that are significant</li> <li>• Material misstatements corrected by management</li> </ul>	<p>Annual Audit Report</p>
<p><b>Fraud</b></p> <ul style="list-style-type: none"> <li>• Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>• Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>• A discussion of any other matters related to fraud</li> </ul>	<p>Annual Audit Report</p>
<p><b>Consideration of laws and regulations</b></p> <ul style="list-style-type: none"> <li>• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>• Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of</li> </ul>	<p>Annual Audit Report (to be issued on completion of audit work) or as occurring if material.</p>

Required communication	Our reporting to you
<p><b>Related parties</b></p> <p>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</p> <ul style="list-style-type: none"> <li>• Non-disclosure by management</li> <li>• Inappropriate authorisation and approval of transactions</li> <li>• Disagreement over disclosures</li> <li>• Non-compliance with laws and regulations</li> <li>• Difficulty in identifying the party that ultimately controls the entity</li> </ul>	<p>No significant matters have been identified.</p>
<p><b>Independence</b></p> <p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>• The principal threats</li> <li>• Safeguards adopted and their effectiveness</li> <li>• An overall assessment of threats and safeguards</li> <li>• Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	<p>Annual Audit Plan</p> <p>This Annual Audit Report – Appendix B</p>
<p><b>Internal controls</b></p> <p>Significant deficiencies in internal controls identified during the audit</p>	<p>This Annual Audit Report – no significant deficiencies reported</p>
<p><b>Group audits</b></p> <ul style="list-style-type: none"> <li>• An overview of the type of work to be performed on the financial information of the components</li> <li>• An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components</li> <li>• Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work</li> <li>• Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted</li> <li>• Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements</li> </ul>	<p>Annual Audit Plan</p> <p>This Annual Audit Report</p>
<p><b>Subsequent events</b></p> <p>Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.</p>	<p>We have asked management and those charged with governance. We have no matters to report.</p>
<p><b>Material inconsistencies</b></p> <p>Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</p>	<p>This Annual Audit Report</p>

# Appendix D: Action Plan

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the College or management to action.

## Classification of recommendations

**Grade 1:** Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.

**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.

**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
1	The College was unable to produce compliant financial statements within the deadline agreed as part of the planning process, or within the SFC's 2018/19 Account Direction requirements. The draft financial statements were subject to a significant level of error and omission.	Significant improvements are required to the financial closedown procedures and preparation of the financial statements to ensure timely and accurate completion of financial statements.  <i>Grade 1</i>	The SMT acknowledges delays with compliant financial statements due to staff changes resulting in insufficient capacity and capability within the Finance Team together with the use of manual procedures.  <b>Actions</b> 1. Review Structure of Finance Team including the appointment of a Financial Director on SMT: <b>Complete</b> 2. Transition existing manual financial processes to electronic, Stage 1 complete use of POs: <b>July 2020</b> 3. Improve the efficiency of year end workings to allow quicker production of primary statement and notes: <b>August 2020</b> 4. Develop a revised approach and timetable for the production of financial statements and year end processes: <b>July 2020</b>  <b>Responsible officer: VP/ HoF</b> <b>Implementation date: August 2020</b>

### Key:

**SMT – Senior Management Team**

**VP – Vice Principal**

**HoF – Head of Finance**

**HoHR&OD – Head of Human Resources and Organisational Development**

**HoEst – Head of Estates**

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
2	<p>Audit testing identified a significant level of error, particularly within accruals testing. We would not normally expect to find the level of error where effective management review processes are in place.</p>	<p>The finance team must ensure that quality assurance and review processes are in place throughout the year to reduce the risk of fraud or error.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>A significant level of staff turnover within the Finance team has resulted in loss of institutional knowledge and continuity and consistency of service.</p> <p>Many of these errors related to previous financial years resulting in increased delays in the completion of the 2018/19 audit and impacted the final Adjusted Operating Position.</p> <p>SMT, the College Chair and subsequently the wider Board were aware of ongoing capacity issues within the Finance Team and all had expressed frustrations at the impact this had on late papers and the availability of information on which to base decisions. This continues to be addressed by SMT.</p> <p>Permanent appointments of vacant roles were made to ensure temporary appointments and staff turnover was no longer an issue. With the resignation of the previous Head of Finance, an interim appointment has been made pending the appointment of a Financial Director. The team is now more stable and will continue to be supported and developed to ensure outstanding issues are addressed effectively.</p> <p><b>Action</b> Implement quality control and review processes across all transactions.</p> <p><b>Responsible officer: VP/HoF</b> <b>Implementation date: September 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
3	<p>As part of the additional work we were asked to perform on deferred income, we noted that management records and communication across College departments were ineffective. There is therefore a risk that income is not reflected accurately within financial statements.</p>	<p>The Finance Team should review the processes in place to record and track all sources of income.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>The deferred income issue was raised with our External Auditors in March 2019 and was reported to Audit, FGPC, Chairs Committees and the Board, as well as to SFC in February 2019. Regular updates were provided as the situation developed.</p> <p>Discussions concluded with External Audit in August 2019 when it was confirmed that income could be appropriately released into 2018/19 with a non-material amount of deferred income relating to previous financial years.</p> <p><b>Actions</b></p> <p>An improved budgeting and contract management process to record and monitor performance milestones is underway.</p> <p>Improved communication between Finance and College teams to plan and monitor income and expenditure.</p> <p><b>Responsible officer: VP/ HoF</b>  <b>Implementation date: June 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
4	<p>The revised SORP will be effective for financial periods beginning on or after 1 January 2019 and therefore will be applied by the College within their 2019/20 financial statements.</p>	<p>The College should conduct an impact assessment on the implementation of the revised SORP.</p> <p style="text-align: right;"><i>Grade 3</i></p>	<p>Complete impact assessment on implementation of revised SORP</p> <p><b>Responsible officer: HoF</b></p> <p><b>Implementation date: July 2020</b></p>
5	<p>We consider that the Finance Team overall has had insufficient knowledge and experience, particularly in financial accounting, since December 2018.</p> <p>We also note that there were a number of historical issues with financial systems and approaches that College appointments within Finance were unable to address.</p>	<p>The College must review the capacity and capability within the finance team to ensure that skills gaps are addressed.</p> <p>The Board needs to urgently ensure that there are appropriate arrangements established to provide strategic financial leadership.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>The structure and resourcing of the Finance Team has been a ongoing focus of SMT with additional resources being invested during 2018/19 provided to increase the capacity and broaden the experience in the department. All positions are now filled permanently with the exception of the Interim Head of Finance who was appointed on a fixed term contract to May 2020, pending a revised structure.</p> <p><b>Actions</b></p> <p>Structure review of Finance: <b>Complete</b></p> <p>SMT recommendation for the appointment of a Director of Finance considered by the Remuneration Committee: <b>Complete and approved</b></p> <p>Implement a CPD plan across the Finance Team: <b>December 2020</b></p> <p><b>Responsible officer: Principal/ HoF</b></p> <p><b>Implementation date: December 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
6	<p>We noted that key financial reports to the Board and committees were provided late, tabled on the day or replaced by verbal updates. In our view this is unacceptable and undermines the Board's ability to monitor financial performance.</p>	<p>Financial reporting must be significantly improved to support Board member scrutiny.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>The Finance Team capacity issues reflected above have been an ongoing focus by SMT with the support of the Board. Actions already taken have addressed the continuity issues within the team and to enable fully compliant Board financial monitoring.</p> <p><b>Action</b></p> <p>Ensure robust financial reports are provided ahead of Committee and Board meetings: <b>February 2020</b></p> <p>In consultation with the Board, Committees and budget holders work towards an information pack to manage the business: <b>December 2020</b></p> <p><b>Responsible officer: Principal/VP</b></p> <p><b>Implementation date: December 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
7	<p>Our work has identified ongoing weaknesses in internal controls, including:</p> <ul style="list-style-type: none"> <li>• Reliance on paper based systems, which led to problems in relation to the retention of financial records.</li> <li>• Lack of segregation of duties, including inadequate review of journal entries and lack of purchase orders.</li> <li>• Financial systems that have not been kept up to date, including the payroll system, or are not fit for purpose, such as the fixed asset register.</li> <li>• Significant delay in the transition to the Government Banking Service leading to the maintenance of unnecessary bank accounts.</li> </ul>	<p>The College must improve key financial controls to ensure that the weaknesses identified are addressed at pace.</p> <p style="text-align: center;"><i>Grade 1</i></p>	<p>The reliance on paper based systems is recognised as a key contributor to weaknesses in our internal controls. This has caused particular issues in relation to our payroll. This was identified by SMT who added this to the risk register and commissioned internal audit work to quantify the extent of the issue.</p> <p>Steps already taken include</p> <ul style="list-style-type: none"> <li>• Internal Audit Action Plan commissioned and partially actioned</li> <li>• Affected staff informed of issue and steps being taken to rectify and recompense</li> <li>• Amended the payroll system user access rights to ensure that that these are appropriate for user roles and remove all generic users from the payroll system</li> <li>• Strengthened controls around variations to staff salaries on the payroll system to reduce the opportunity for unauthorised entries to be added to the tracker and inadvertently processed</li> <li>• Introduced mechanisms to ensure that payroll checklists are always completed and held on file and that these checklists are always checked and signed off by someone independent of the payroll team prior to processing of the payroll.</li> <li>• Internal Audit commissioned to conduct evaluation of pensions and tax payments</li> <li>• Voluntary HMRC Disclosure made</li> </ul> <p><b>Future Actions</b></p> <ol style="list-style-type: none"> <li>1. Develop transition plan towards electronic systems. Work underway towards consistent use of Purchase Orders: <b>September 2020</b></li> <li>2. Introduce quality monitoring of journal entries: <b>February 2020</b></li> <li>3. Complete bank transition: <b>March 2020</b></li> <li>4. Investment in a managed service for Ciph: <b>Underway</b></li> <li>5. Implement Fixed Asset Register: <b>July 2020</b></li> </ol> <p><b>Responsible Officers: VP, HoF, HoHR&amp;OD, HoEst</b></p> <p><b>Implementation date: September 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
8	<p>The College did not participate with the NFI exercise until December 2019. We also note that the Fraud Response Plan does not refer to the exercise, or the need to resource or investigate the follow up of matches.</p>	<p>The College should ensure that the Fraud Response Plan is updated to reflect the investigation of matches identified through the NFI exercise.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>The previous Head of Finance had engaged with NFI but had not fully completed the testing of the matches within the specified deadlines.</p> <p>Once SMT became aware of this in December 2019, action was taken immediately to register key staff and to investigate the matches.</p> <p><b>Action</b> Update Fraud Response Plan to reflect the investigation of matches identified through NFI: <b>June 2020</b></p> <p>Self assessment form agreed and launched: <b>May 2020</b></p> <p><b>Responsible officer: HoF</b> <b>Implementation date: June 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
9	<p>The Board was given insufficient time and strategic financial support to allow effective scrutiny of the key assumptions underpinning the Financial Forecast Return.</p>	<p>The Financial Forecast Return should be presented in sufficient time to ensure that the Board has an opportunity to influence key assumptions prior to submission.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>The capacity within the Finance Team together with sources of income channelled through UHI not being fully confirmed resulted in delays in finalising the College budget for 2019/20.</p> <p>SMT worked hard to ensure the robustness of the budget and the savings required to be achieved during the year. The budget was ultimately approved at the October Board. This had a knock on effect to the development of the FFR.</p> <p>SMT and the Board expressed dissatisfaction that there was insufficient time to fully scrutinise the assumptions underpinning the FFR. As a result this is being reviewed to determine any revisions to be made.</p> <p><b>Actions</b></p> <p>Revise FFR for 2019/20 to ensure accuracy  Implement scenario planning exercise with College Board to inform 2020/21 FFR: <b>May – September 2020</b></p> <p>Increase engagement with UHI Finance to achieve early confirmation of income sources to inform 2020/21 budget: <b>May 2020</b></p> <p><b>Responsible officer: HoF</b></p> <p><b>Implementation date: September 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
10	<p>Staff costs within the Financial Forecast Return have been reduced to reflect the savings required to return a balanced position, rather than as a result of an effective workforce plan. In our view, the Financial Forecast Return does not provide a robust medium term financial plan.</p>	<p>The College urgently needs to develop effective medium term financial planning. This should be supported by scenario planning and ongoing monitoring.</p> <p style="text-align: center;"><i>Grade 1</i></p>	<p>Rationale included within Finding 9.</p> <p><b>Actions</b></p> <p>Develop alternative scenarios, modelling and fiscal/ budget assumptions to more accurately forecast and monitor future financial impacts</p> <p>Undertake CMT and Board Development sessions on the creation of the FFR for 2021-26</p> <p><b>Responsible officer: HoF</b></p> <p><b>Implementation date: May - September 2020</b></p>
11	<p>We noted a number of instances where reporting to the Board was ineffective and may not support Board members' specific responsibilities as charitable trustees. Examples include:</p> <ul style="list-style-type: none"> <li>• Key decisions on senior staffing structure</li> <li>• The Board did not consider the 2018/19 budget, but noted the minutes of the F&amp;GP committee.</li> <li>• The 2019/20 Budget was approved in October 2019, following the start of the financial year.</li> <li>• The Board does not receive the risk register or financial monitoring updates.</li> </ul>	<p>We understand that the College will receive an external evaluation of its governance arrangements by December 2020. This review should consider the quality of reporting, and be informed by the specific responsibilities of charitable trustees.</p> <p style="text-align: center;"><i>Grade 1</i></p>	<p>See Responses in 2, 5, 6 and 9</p> <p>The College risk register process has already been reviewed and updated with risks monitored at all committee and board meetings. This is managed by the Clerk to the Board with each SMT member owning specific risks and the relevant committees monitoring the progress against these risks. The full register has now been included within all Board meetings.</p> <p><b>Actions</b></p> <p>Review the College's Annual Governance plan to ensure approvals are obtained based on robust and timely information</p> <p>Board agendas to include Financial monitoring updates</p> <p>Review the process for reporting and approval of settlement agreements</p> <p><b>Responsible officer: Principal/ Board Clerk</b></p> <p><b>Implementation date: March – July 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
12	The College has not undertaken a review of the Governance Statement against the good practice guidance referred to within the Accounts Direction.	The College should review the quality of the Governance Statement against good practice guidance to ensure that it meets users needs.  <i>Grade 2</i>	The College has already created a document reflecting the evidence of its compliance against the Governance Statement. This will be further reviewed to ensure this data is fully and fairly reflected within the Governance Statement.  <b>Action</b>  Review and implement the good practice guidance to ensure the quality of the Governance Statement  <b>Responsible officer: VP/ Board Clerk</b>  <b>Implementation date: March- July 2020</b>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
13	<p>The Balanced Scorecard is under development but the most recent report to December 2019 provided only an interim report on 2018/19 performance. We also noted that a number of indicators were RAG rated only, but the actual metrics were not reported. This may be insufficient for effective scrutiny.</p>	<p>Performance reporting should be reviewed to ensure that it is timely and provides sufficient information to allow robust scrutiny.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>The College has undertaken a significant amount of work in reviewing the Balanced Scorecard. This has been consulted on across the College and at all Committees and at the Board.</p> <p>The revised Balanced Scorecard format is reported at all committee and board meetings.</p> <p>The timings of the completion of the full balanced scorecard has been delayed this year due to the delay in the production of the Financial Statements. The final 2 measures of AOP and % of non SFC turnover were unable to be included until the Financial Statements were completed.</p> <p>The College is always receptive to recommendations for improvements and will further review the current format to ensure that it provides the best possible monitoring information.</p> <p><b>Actions</b></p> <p>Implement further improvements to the Balanced Scorecard to include actual metrics and reporting timelines.</p> <p><b>Responsible officer: Principal/ Board Clerk</b></p> <p><b>Implementation date: March – July 2020</b></p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
14	The College has disclosed a number of significant weaknesses in procurement within its Governance Statement, including lack of competitive tenders for material contracts.	<p>The College must ensure that procurement weaknesses are addressed as a matter of urgency.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>SMT identified a weakness in this area and as a result took a number of corrective actions to ensure that appropriate systems and processes were addressed and that policies and procedures were up to date and communicated effectively to staff.</p> <p>SMT acknowledges the 2 areas of non compliance which were already in process of being addressed prior to the external audit being undertaken. These were a contract which is broader than a tendered service relationship and which had been in place since 2004 and which is subject to a current retender process. Secondly, a contract that required reporting to RSB which was undertaken retrospectively was non-compliant. This contract was funded through non-public funded sources</p> <p>SMT have already implemented a control system which includes:</p> <ul style="list-style-type: none"> <li>• APUC contract in place</li> <li>• Revision of Procurement Strategy and Procedures</li> <li>• Contracts register enabling forward planning of contract values, tenders and renewals</li> <li>• Greater use of APUC Frameworks</li> <li>• Implementing a consistent purchase order system</li> <li>• Retendering of non-compliant contracts</li> <li>• Discussions with RSB on rationales for exemptions to tender</li> </ul> <p><b>Responsible officer: VP</b> <b>Implementation date: March - July 2020</b></p>

# Appendix E: Follow up of prior year recommendations

This section of our report summarises our assessment of the College's progress against the recommendations that we identified during our 2017/18 audit.

Prior year recommendations			
No.	Recommendation / grading	Management response/ Implementation timeframe	Our assessment of progress
1	<p>Management is sighted as to the requirement for savings to be delivered over the next five years and has begun reviewing possible avenues for delivery.</p> <p>As the College develops these plans it is important that these are quantified in a detailed medium term financial plan which aligns to FFRs and strategic and operational plans.</p> <p>The College's future financial forecast should be reviewed, not just annually with each submission, but as significant updates are required as saving programmes are identified or assumptions crystalize. Any significant changes should be communicated to UHI as the regional strategic body, and the SFC if appropriate. Should sufficient savings not be identified to address forecast deficits in the next financial period, management should consider alternate action with the regional strategic body.</p> <p><i>Grade 1</i></p>	<p>Agreed. To be completed through the 2018/19 financial year.</p> <p><b>Updated response – February 2020</b></p> <p>Changes in the Finance Team, including at Senior Management Team level resulted in this recommendation not being implemented fully.</p> <p>In line with the responses to the 2018/19 Audit Report, the SMT appointment of a Financial Director; increased Board financial reporting; early change notification to RSB will improve FFR's alignment with strategic and operational plans.</p>	<p>As we report within Financial Sustainability, we consider that strategic financial planning remains inadequate.</p> <p>Audit Assessment: Not yet complete.</p>

# Appendix F: Errors identified during the audit

This table sets out the adjustments processed in the financial statements finalisation above our reporting threshold

Adjusted differences				
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Adjusting accounting treatment of SITS debtor</i>	Cr Tuition Fee Income £57,970		Dr Debtors £57,970
2	<i>Capitalisation of assets and treatment of capital grant</i>	Cr Expenditure £345,629 Dr Income £345,629		Dr Debtors £345,629 Cr Deferred Capital grants £345,629
3	<i>Recognition of depreciation and deferred capital grant release on newly capitalised assets</i>	Dr Depreciation £48,603 Cr Income £48,603		Dr Deferred Capital grants £48,603 Cr Accumulated Depreciation £48,603
4	<i>Reallocation of expenditure incorrectly classified</i>	Dr Other Operating Expenditure £46,193 Cr Payroll Expenditure £46,193		
5	<i>Correct accounting for pension liability</i>		Dr Actuarial Loss £1,088,000	Cr Pension liability £1,088,000
6	<i>Being increase to national insurance liability</i>	Dr Payroll costs £141,533		Cr Accruals £141,533
7	<i>Removal of income for telephone masts which relates to previous financial years</i>	Dr Other income £42,229		Cr Accrued income £42,229
8	<i>Correction of sales invoice posted to 2018/19 in error</i>	Dr Residences Income £23,179		Cr Debtors £23,179

## Adjusted differences

No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
9	<i>Correction to accounting for 2019/20 NDR expenditure</i>			Dr Creditors £62,417 Cr Prepayments £62,417
10	<i>Reversal of capital additions which relate to 2019/20</i>	Dr Grant income £2,795 Dr Expenditure £27,951 Cr Depreciation Expense £2,795 Cr Capital Maintenance Grant £27,951		Dr Accumulated Depreciation £2,795 Dr Deferred Capital Grants £25,156 Cr Assets – Fixtures and Fittings £27,951
11	<i>Being reversal of depreciation charged not in line with policy</i>	Dr Grant income £35,129 Cr Depreciation Expense £35,129		Dr Accumulated Depreciation £35,129 Cr Deferred Capital Grants £35,129
12	<i>Correction of accrued research income</i>	Dr Research Income £49,457		Cr Accrued Income £49,457
13	<i>VAT adjustment</i>	Dr Expenditure £44,168		Dr VAT Debtor £587 Cr VAT Creditor £44,755

## Adjusted differences

No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
14	<i>Correction of accruals which do not relate to 2018/19</i>	Cr Expenditure £240,999		Dr Accruals £240,999
15	<i>Correction of tuition fee income for 2019/20 not received in advance</i>			Dr Deferred income £38,480 Cr Debtors £38,480
16	<i>Accrual of gift aid income from subsidiary</i>	Cr Gift aid income £225,435		Dr Accrued Income £225,435
17	<i>Being AFS adjustment</i>	Dr Grant income £4,000 Cr Depreciation Expense £5,744	Cr Revaluation Gain £54,641	Dr Assets Held for Sale £230,000 Dr Accumulated Depreciation £37,585 Cr Assets – Cost £207,200 Cr Deferred Capital Grants £4,000
18	<i>Correction of annual leave accrual</i>	Dr Payroll expenditure £44,999		Cr Accruals £44,999

### Adjusted differences

No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
19	<i>Correction of National insurance liability</i>			Dr Accruals £250,000 Cr Provisions £250,000
20	<i>Increase in relation to accrual of ESIF income</i>	Cr Grant Income £120,382		Dr Accrued Income £120,382
21	<i>Release of Foundation Apprenticeship income relating to 2017/18</i>	Cr Income £223,398		Dr Deferred Income £223,398
22	<i>Release of LUPS income relating to 2016/17</i>	Cr Income £118,977		Dr Deferred Income £118,977
23	<i>Accrual for the income and expenditure in relation to job evaluation which relates to 2018/19</i>	Dr Staff costs £384,947 Cr Income £384,947		

This table sets out the unadjusted differences above our reporting threshold in relation to the College.

### Unadjusted differences

No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Recognition of Development Trust</i>			Dr Net Assets    £54,487 Cr I & E Reserve   £54,487

This table sets out the adjustments processed in the financial statements finalisation above our reporting threshold in relation to AST (Engineering) Limited.

Adjusted differences				
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Correction of accounting for NDR liability</i>			Dr Trade creditors £31,925 Cr Prepayments £31,925
2	<i>Recognition of tuition fee income</i>	Cr Tuition Fee Income £17,022		Dr Accrued Income £17,022
3	<i>Correction of expenditure accruals</i>	Dr Expenditure £5,034		Cr Accruals £5,034
4	<i>Correction to tuition fee income</i>	Dr Tuition Fee Income £4,659		Cr Accrued Income £4,659
5	<i>Tuition fee income not recognised</i>	Cr Tuition Fee Income £33,365		Dr Accrued Income £33,365
6	<i>Correction of prepaid fees</i>	Dr Tuition Fee Income £3,571		Dr Deferred income £119,884 Cr Debtors £123,455
7	<i>Accrual of gift aid income from to parent</i>	Dr Gift aid distribution £225,435		Cr Accruals £225,435
8	<i>Recognition of annual leave accrual</i>	Dr Payroll Expenditure £4,765		Cr Accruals £4,765

This table sets out the unadjusted differences above our reporting threshold in relation to AST (Engineering) Limited.

Unadjusted differences				
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Correction of accrual</i>	Cr Expenditure £2,439		Dr Accruals £2,439

# Appendix G: Timing and deliverables of the audit

We deliver our audit in accordance with the timeline set by the College, in accordance with guidance from Audit Scotland. Below is a timetable showing the key stages of the audit and the deliverables through the 2018/19 audit cycle.

	Audit Activity	Deliverable	Timing
MAR			
APR	<ul style="list-style-type: none"> <li>Review of current issues impacting the College throughout the audit process</li> </ul>	Periodic current issues return submission	22 March 2019 8 November 2019
MAY	<ul style="list-style-type: none"> <li>Audit planning and setting scope and strategy for the 2018/19 audit</li> </ul>	Annual audit plan	6 June 2019
JUNE	<ul style="list-style-type: none"> <li>Walkthrough visit</li> </ul>	Completion of internal documentation	24 June 2019
AUG	<ul style="list-style-type: none"> <li>Review progress of the NFI exercise</li> </ul>	Submit NFI questionnaire	30 June 2019
SEPT			
OCT	<ul style="list-style-type: none"> <li>Year-end substantive audit fieldwork on unaudited financial statements</li> </ul>	Audited financial statements	October 2019
NOV	<ul style="list-style-type: none"> <li>Conclude on results of audit procedures and finalise Annual Audit Report</li> </ul>	Issue Annual Audit Report	20 February 2020
DEC	<ul style="list-style-type: none"> <li>Issue opinion on the College's financial statements</li> </ul>	Submit Audit Scotland Minimum dataset request	

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