



# Lews Castle College

*Creating the University of the Highlands and Islands*

**ANNUAL REPORT  
TO THE BOARD OF MANAGEMENT AND THE  
AUDITOR GENERAL FOR SCOTLAND  
ON THE EXTERNAL AUDIT FOR THE  
YEAR ENDED 31 JULY 2010**

**NOVEMBER 2010**

**Wylie<sup>+</sup>Bisset, LLP**

Chartered Accountants  
Business & Tax Advisers

**168 Bath Street  
Glasgow**

Date of commencement of Final Visit	25/10/2010
Date of Draft Report to College	23/11/2010
Date of Meeting re Draft Report	By Tel
Date of College Responses	30/11/2010
Date of Presentation of Report	30/11/2010

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## **GLOSSARY OF TERMS**

<b>“Report”</b>	Annual report to the Board of Governors and the Auditor General for Scotland
<b>“The College”</b>	Lews Castle College
<b>“The Code”</b>	Code of Audit Practice
<b>“The SORP”</b>	Statement of recommended practice: accounting for further and higher education
<b>“SFC”</b>	Scottish Funding Council
<b>“VFM”</b>	Value for Money

## 1. INTRODUCTION

- 1.1. Wylie & Bisset were appointed as the External Auditors of Lews Castle College with effect from 1 August 2006 for a period of 5 years until 31 July 2011. Wylie & Bisset LLP succeeded Wylie & Bisset during 2008 and will undertake the remainder of the appointment.
- 1.2. The Annual Report has been prepared following the conclusion of our audit of the financial statements of Lews Castle College for the year ended 31 July 2010.
- 1.3. Our audit was carried out in accordance with our statutory responsibilities, statements of auditing standards and wider responsibilities contained in the Code of Audit Practice ('the Code') issued by Audit Scotland in March 2007.
- 1.4. Paragraph 24 of the 'Code' states that the auditor's objectives are to:
  - Provide an opinion whether the College's financial statements present a true and fair view of the financial position of the College and the regularity of transactions in accordance with standards and guidance issued by the Auditing Practices Board;
  - Review and report on the College's corporate governance arrangements as they relate to:
    - The College's review of its systems of internal control;
    - The prevention and detection of fraud and irregularity;
    - Standards of conduct, and the prevention and detection of corruption;
    - Its financial position; and,
  - Review aspects of the College's arrangements to manage its performance.
- 1.5. The responsibilities of the Board of Management with regard to the financial statements are set out in the "Statement of Responsibilities of the Board of Management" included in Appendix A and in the "Independent Auditors' Report" in Appendix B.
- 1.6. The responsibilities of Wylie & Bisset LLP with regard to the financial statements and our audit opinion on the financial statements are included in the "Independent Auditors' Report" included in Appendix B.
- 1.7. Our audit report on the financial statements for the year ended 31 July 2010 is unqualified.

- 1.8. The Annual Report covers the following areas as set out in the Code:
  2. Internal Controls and audit approach
  3. Financial Statements
  4. Internal Audit
  5. Corporate Governance
  6. Value for Money
  7. Prevention and detection of fraud and irregularities
  8. Management letter – 2009
  9. Management letter – 2010
  10. Current Issues
  
- 1.9. Our audit findings in each of the above areas are set out in the relevant sections of the report.
  
- 1.10. Our audit work is designed to enable us to form an audit opinion on the financial statements of the College and should not be relied upon to disclose all weaknesses in internal controls in relation to the Colleges systems and financial statements.
  
- 1.11. This report has been prepared for the purposes of the Board of Management and the Auditor General for Scotland and should not be issued to third parties without our prior written consent.
  
- 1.12. We would emphasise that our comments in this report are not intended to be any reflection on the integrity of the College staff whom we would like to thank for their help and assistance throughout our audit visits.
  
- 1.13. Should you have any queries on the contents of the Annual Report please do not hesitate to contact us.

Yours faithfully

Wylie & Bisset LLP

## **2. INTERNAL CONTROLS AND AUDIT APPROACH**

- 2.1. We have reviewed in the course of our audit the key elements of the College's systems of internal financial controls in the main operating cycles.
- 2.2. In carrying out our audit work we have taken into account the following:
  - a) The Code of Audit Practice issued by Audit Scotland;
  - b) The Code of Audit Practice issued by SFC;
  - c) Guidance issued by Audit Scotland;
  - d) Guidance issued by SFC;
  - e) The College's internal control procedures;
  - f) The College's Corporate Governance procedures;
  - g) The College's approach to Value for Money;
  - h) The financial memorandum between SFC and the College.
- 2.3. In reaching our audit opinion we carried out our audit work based on the audit plan with evidence obtained by:
  - a) Reviewing previous financial statements;
  - b) Reviewing internal audit plans and reports;
  - c) Discussions with senior management and staff at the College;
  - d) Completing appropriate audit programmes;
  - e) Carrying out analytical review procedures;
  - f) Carrying out substantive and compliance audit tests on a judgemental basis;
  - g) Reviewing the minutes of the principal College committees.
- 2.4. Based on our review the College appears to operate appropriate internal financial controls, subject to the management letter points and audit recommendations raised in Sections 8 & 9.
- 2.5. The recommendations have been graded as either High, Medium or Low priority depending upon the degree of risk assessment for each recommendation. Each recommendation has a target date for remedial action and the person responsible for each recommendation has been nominated in the relevant Section.

### **3. FINANCIAL STATEMENTS**

- 3.1. The financial statements of the College are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of these resources. In accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts direction issued by the SFC, it is the responsibility of the College to prepare financial statements, which give a true and fair view of the College's financial position and the income and expenditure for the year.
- 3.2. The Public Finance and Accountability (Scotland) Act 2000 requires that the auditor shall place on the abstract of accounts an audit report, which contains an opinion as to whether the College has fulfilled this responsibility. The format of the audit report directed by the Auditor General for Scotland clarifies the respective responsibilities of management and auditors in relation to the accounts and requires auditors to set out the basis on which they have formed their opinion.

#### **AUDIT REPORT**

- 3.3. We are pleased to record that there are no qualifications in our audit report on the College's 2009/10 accounts, as, in our opinion, the financial statements give a true and fair view of the College's financial position and the income and expenditure for the year; and funds received have been applied for their intended purpose.

#### **FINANCIAL PERFORMANCE**

- 3.4. The income and expenditure account shows an operating surplus for the year of £109k (2009 – restated deficit £421k). This is stated after a credit arising in relation to the pension scheme past services gain of £166k. Excluding the movements in relation to the pension liability under FRS17 the income and expenditure account would show an operating surplus of £7k (2009 – restated deficit £385k).
- 3.5. The pension scheme past service gain arises mainly in relation to the impact of the change in pension scheme valuation to take account of CPI rather than RPI and is determined by Barnett Waddingham, the scheme's actuaries. Note that this is considered further within section 10.
- 3.6. In 2009/10 the College forecast for an operating surplus of £4k through the College Financial Return. The actual surplus for the year pre FRS17 adjustments was £7k. The College has currently budgeted for a £2k operating surplus in 2010/11.
- 3.7. The balance brought forward on the consolidated income and expenditure reserve as at 1 August 2009 was a restated deficit of £1,587k. The balance on the income and expenditure reserve at 31 July 2010 is £1,580k in deficit.



### 3.8 PERFORMANCE INDICATORS

	<b>2008/09 Lews Castle College</b>	<b>2008/09 Sector Average</b>
Operating Surplus as a % of income	0.2%	(0.2%)
The Reserves (designated reserves plus Income & Expenditure reserves) as a % total of income	(10.9%)	25%
Historical cost surplus as a % of income	0.2%	2.4%
The liquidity ratio (current assets: current liabilities)	1.4%	1.87
Interest cover	3.1	0.59
The days cash to total expenditure ratio	9	81
Unit cost of WSUM	361	237
WSUM's per FTE teaching staff	296	374
Staff costs as % of total expenditure	66%	65%
Premises cost as % of total expenditure	7%	9.7%
Total funding grant as a % of total income	64%	73%
Recurrent grant as a % of total income	55%	65%
Total Education Contracts and Tuition Fees as a % of total income	10%	15.7%
Total other income as a % of total income	25%	10.0%
European Income as a % of total income	0.0%	1.7%

## SUBMISSION OF ACCOUNTS

- 3.9 The financial information was submitted for audit on 25th October 2010. The financial pages of the accounts submitted for audit at this date were not complete but a draft, incorporating the OFR and revision to financial information was available soon after. Working papers provided have generally been of a good standard and queries arising from the audit have all been resolved. Key staff members were readily available for consultation throughout the audit process.

## ISSUES ARISING

- 3.10 During the course of the audit a number of issues arose which were resolved in discussion with, or formally reported to the Director of Finance & Corporate Services and the Management Accountant. This practice is an established part of the audit process. The remainder of this report draws to the attention of the Board of Management and the Auditor General any matters of particular significance or interest, which arose from the audit.
- 3.11 **Accounting Policies:** In accordance with FRS18 the Audit Committee have formally reviewed the accounting policies included in the Annual Accounts.
- 3.12 **Capital expenditure:** During the year ended 31 July 2010, the College expended £367k on capital expenditure.
- 3.13 **Basis of Preparation – Going Concern:** The College makes reference to the accumulated deficit within its accounting policies. This area is reviewed on an annual basis to ensure the accounting policy note is still relevant. Given the College's financial situation and current economic climate, we have given particular regard to this area during our audit testing, however we have not considered an emphasis of matter with regard to this situation to be necessary.
- 3.14 Appendix C includes a copy of the letter of representation which we have sought from the College in support of the matters reported to us during our audit procedures. This also includes reference to the summary of unadjusted errors and deviations.
- 3.15 **SFC Clawback:** In August 2010 the SFC carried out a review of the college's ELS SUMs for AY 2007-08 and AY 2008-09. This review resulted in certain of the SUMs being deemed to be ineligible for ELS support funding. This will result in the repayment of the overclaimed SUMs of £842,000 to the SFC. This has been treated as a prior year adjustment with £438k being adjusted in 2008/09 and £404k in 2007/08.

## **4 INTERNAL AUDIT**

### **Objective and Approach**

- 4.1. Internal audit is a key element of the internal control system set up by management. A strong internal audit function is necessary to ensure the continuing effectiveness of the internal control system established. The College, therefore, needs to have in place a properly resourced internal audit service of good quality. To maximise the reliance that may be placed on internal audit and to avoid duplication of effort, the adequacy of internal audit is assessed each year.
- 4.2. The College's internal auditors for 2009 /10 were CIB Services.
- 4.3. The College's internal audit strategic and operational plans are set out for the year ending 31 July 2010 in the Audit Needs Assessment.
- 4.4. In the course of the year ended 31 July 2010 the following internal audit reports were issued:
  - a) Cash & Banking (October 10)
  - b) Financial Accounting Systems (October 10)
  - c) Income and Debtors (October 10)
  - d) Payroll (October 10)
  - e) Purchases and Creditors (October 10)
  - f) SUMs Report (October 2010)
- 4.5. The Internal Audit Annual Report was outstanding at the time of our audit visit.

### **Opinion**

- 4.6. Our audit procedures included an assessment of the adequacy of the Internal Audit function using a bespoke checklist and review of the reports issued by the Internal Audit function. Minutes of the audit committee were also reviewed. Our findings in this area identified a number of factors primarily in relation to the timing of internal audit procedures and reporting which have led us to conclude that we could not place formal reliance on work of Internal Audit.
- 4.7. Recommendations in this area are included within section 8.

## 5 CORPORATE GOVERNANCE

### **Objective and Approach**

- 5.1. A review and assessment of the College's Corporate Governance systems relating to standards of conduct, openness and integrity was performed as part of our audit, using a bespoke checklist. We also reviewed the following:
- a) The College's Corporate Governance Statement included in the financial statements for the year ended 31 July 2010;
  - b) The College's Corporate Governance strategy;
  - c) The minutes of meetings of key College committees issued during the year.

### **Opinion**

- 5.2. Based on our review the College appears to operate appropriate Corporate Governance procedures and management have adequate arrangements in place covering standards of conduct etc. These include, for example, Codes of Conduct for both Board Members and Staff. However, a specific weakness was noted with regard to attendance at committee meetings.

### **Recommendations**

- 5.3. A recommendation has been made in this area in relation to committee meeting attendance. This is detailed within section 8.

## **6 VALUE FOR MONEY**

### **Objective and Approach**

- 6.1. We have considered the College's strategy regarding value for money as part of our standard audit procedures. It is noted, that whilst there have been no specific VFM studies carried out by the College's internal auditor during the year, implicit assurance over this area is obtained via all the internal audit reviews.

### **Opinion**

- 6.2. Based on our review, we are satisfied that the College has established adequate arrangements to secure economy, efficiency and effectiveness in the use of its resources.

### **Recommendations**

- 6.3. There were no recommendations in this area in 2009. Similarly, no recommendations pertaining specifically to Value for Money have been made during the current year.

## **7 PREVENTION AND DETECTION OF FRAUD AND IRREGULARITIES**

### **Objective and Approach**

- 7.1 The Code sets out that the College should establish arrangements for the prevention and detection of fraud and other irregularities as part of its Corporate Governance procedures
- 7.2 An assessment was made of the adequacy of the systems and controls for the prevention and detection of fraud and irregularities using a bespoke checklist.
- 7.3 In the course of the audit we have reviewed the following areas with regard to the prevention and detection of fraud and irregularities:
- a) The monitoring and compliance with financial procedures;
  - b) The College's strategy to prevent and detect fraud and other irregularities;
  - c) The internal controls operated for segregation of duties, authorisation and approval processes and reconciliation procedures.
- 7.4 No areas of significant concern were found during normal audit procedures.
- 7.5 We emphasise that our audit of the financial statements is planned to ensure there is a reasonable expectation of detecting misstatements arising from fraud or other irregularity that are material in relation to those financial statements, but cannot be relied upon to detect all frauds and irregularities.

### **Opinion**

- 7.6 Overall we concluded that management takes its responsibilities toward fraud prevention and detection seriously and has reasonable controls in place to ensure that potential areas for fraud are detected and dealt with in an appropriate manner.

### **Recommendations**

- 7.7 There are no recommendations made specifically in relation to in this area, however it should be noted that all recommendations have an implicit impact on the prevention and detection of fraud and irregularities.

## 8 MANAGEMENT LETTER – 2009

- 8.1 A management letter was prepared by Wylie & Bisset in relation to the accounts of Lews Castle College for the year ended 31 July 2009.
- 8.2 This included ten observations along with our recommendations to management. As part of our audit procedures during the current year we have followed up the areas highlighted and include below our conclusions from the current year.

### PRIORITISATION

- 8.3 The points within the report have been assigned a propriety level based on the urgency required in addressing the matters highlighted. An explanation of the priority levels is as follows:

<b>High Priority</b>	Recommendations addressing significant control weaknesses which should be implemented immediately.
<b>Medium Priority</b>	Recommendations addressing significant control weaknesses which should be addressed in the medium term.
<b>Low Priority</b>	Recommendations which, although not addressing significant weaknesses, would either improve efficiency or ensure that the College matches current good practice.

### 31 JULY 2009 RECOMMENDATIONS

#### 8.4 ESF Projects

- 8.4.1 **2009 Observation:** It was noted that there are several ESF projects in which Lews Castle College are part of, although, they are not the lead partner. The finance department and the Head of Finance and Estates were not aware that the college had agreed to take part in these projects. It was also not able to quantify the amount that was due to the college for these projects at the year end audit.
- 8.4.2 **2009 Recommendation:** We recommend that the college put a system in place where all ESF projects which the college agrees to take part in must be approved by the Head of Finance and Estates.
- 8.4.3 **2010 Update:** The College have been in contact with UHI to try to quantify the amount that is due to the college for these projects but has so far been unsuccessful. We understand that the issue arises from UHI contacting college staff directly to carry out pieces of work with finance staff not being made aware of this commitment until the staff member makes a claim for the costs which then results in the finance department having to chase UHI for the income resulting in a negative cashflow for the college.

8.4.4 **Further action required:** The college should continue to correspond with UHI to quantify the amount due to the college and the College's obligations in relation to these projects and implement a procedure to prevent the college being involved with ESF projects prior to the authorisation by the Head of Finance and Estates.

8.4.5 **Priority: High**

8.4.6 **Management Response:** A procedure has already been established and all staff are to be reminded of the importance of compliance. Discussions with UHI are continuing.

8.4.7 **Timescale:** Immediate.

## 8.5 Accounting for Projects

8.5.1 **2009 Observation:** There is one project run by the college for which the income and expenditure is recorded through balance sheet codes resulting in the income and expenditure not being recorded through the statement of income and expenditure.

8.5.2 **2009 Recommendation:** We recommend that income and expenditure is recognised separately in the profit and loss statement and not netted off in balance sheet codes.

8.5.3 **2010 Update:** The project in question ended in November 2009, and to this time, the College continued to record the income and expenditure through the balance sheet codes. This has resulted in the income and expenditure being understated by £5k and £10k respectively (£5k deficit). Whilst this is not material, this has been recorded on the schedule of unadjusted misstatements.

8.5.4 **Further action required:** We recommend that should the college be involved in any such future projects they recognise the income and expenditure in the profit and loss statement.

8.5.5 **Priority - High**

8.5.6 **Management Response:** Agreed.

8.5.7 **Timescale:** Immediate.

## 8.6 Fixed Asset Register

8.6.1 **2009 Observation:** The College does not keep a register of fixed assets which reconciles to the financial statements.

8.6.2 **2009 Recommendation:** We recommend that the college maintains a fixed asset register for all assets held which should be reconciled to the financial statements.



8.6.3 **2010 Update:** The College has a fixed asset register which reconciles to the financial statements. However, it is noted that this does not include an inventory listing detailing the locations of the assets. We understand that the IT department have such a list for their equipment.

8.6.4 **Further action required:** We recommend that the register be updated to include an inventory listing showing the location of the assets held by the college.

8.6.5 **Priority - Medium**

8.6.6 **Management Response:** The location will be updated during the current session.

8.6.7 **Timescale:** July 2011.

## 8.7 Internal audit

8.7.1 **2009 Observation:** For the 12 areas that the 2008 programme of work had planned to review only 3 reports were available for us at the year end audit and they were still in draft format. Although a plan had been prepared for the 2009 programme of work an annual report had yet to be prepared during our visit.

8.7.2 **2009 Recommendation:** We recommend that management ensure the internal audit work planned is carried out and reports are prepared on a timely basis.

8.7.3 **2010 Update:** With regard to the 2009 planned internal audit work, 3 reports were never issued.

Of the 8 areas that the 2010 programme of work had planned to review, no reports were available at the interim visit: at our final visit, 5 reports were available (having been issued in October rather than July) while 3 reports were outstanding. The outstanding reports were due to be have been provided prior to our audit fieldwork in October.

In addition, the Internal Auditor only attended 2 of the 6 audit committee meetings.

8.7.4 **Further action required:** The internal audit work has covered the majority of reports which it planned to address, however, reports were generally supplied significantly later than planned, reducing their impact and effectiveness for the audit committee. This has also had an impact on our audit procedures as we were unable to place reliance on the work done.

Good governance requires the college to have an internal audit function which determines the audit needs of the college and performs reviews in line with this plan providing reports on a timely basis. It is not good practice for areas identified not to be reviewed. We recommend that management seek commitment to the agreed timetable from the internal auditor and chase reports on a timely basis in order to prevent undue delay.

8.7.5 **Priority - Medium**

8.7.6 **Management Response:** A letter was sent to the Internal Auditor by the Chair of the Audit Committee seeking confirmation to comply with the agreed timetable. A response by the Internal Auditor was provided verbally at the October meeting and by letter.

8.7.7 **Timescale:** Done.

## 8.8 Purchase invoices

8.8.1 **2009 Observation:** Purchase invoices under query are not posted to the purchase ledger since it was the Colleges' policy to only include items once they have been approved for payment.

8.8.2 **2009 Recommendation:** We recommend that purchase invoices are posted to the purchase ledger when received to ensure all invoices are logged onto the system and that recorded liabilities are complete.

8.8.3 **2010 Update:** The purchase invoice register is now electronic and is maintained on the access system. Purchase invoices are posted onto the system when they are received.

8.8.4 **Further action required:** No further action required.

## 8.9 Student Support Fund

8.9.1 **2009 Observation:** It was noted that Student Support Fund bank accounts are not held within the main ledger.

8.9.2 **2009 Recommendation:** We recommended that Student Support Funds bank accounts should be maintained within the main ledger.

8.9.3 **2010 Update:** The College are looking into a new system which will integrate with their current student records system and allow the college to record payments made to students. They feel that, currently, it is too difficult to record the student payments through the access system. This gives rise to the risk that assets and liabilities of the college are incorrectly stated within the accounts.

8.9.4 **Further action required:** The College should investigate the best way to bring all student support fund bank accounts onto the accounting system.

8.9.5 **Priority - Medium**

8.9.6 **Management Response:** SITS is being used in the current year. A journal will be produced for the year end transfer to the main accounting system.

8.9.7 **Timescale:** July 2011.

## 8.10 Accounting for Investments

8.10.1 **2009 Observation:** The college has an investment in both Lews Castle College Trading Company and Greenspace Research Limited and 2 sub-subsidiaries which are part of Greenspace Research Limited. However, the investments are not included in the college's trial balance or accounting system.

8.10.2 **2009 Recommendation:** We recommend that the shares are included in the colleges' accounting system to recognise these investments.

8.10.3 **2010 Update:** The investment in Lews Castle College Trading Company is now included in the trial balance, however, the investment in Greenspace Research Limited is not. We understand that this is due to the company being dormant and that the value of investment is not significant.

8.10.4 **Further action required:** We recommend that the investment in Greenspace Research Limited is included in the college's accounting system with an appropriate offsetting provision if necessary in order that this does not become neglected when preparing the accounts.

8.10.5 **Priority - Low**

8.10.6 **Management Response:** Agreed.

8.10.7 **Timescale:** July 2011.

## 8.11 Fixed assets – Disclosure of Scrapped Items

8.11.1 **2009 Observation:** When testing the existence of fixed assets we identified assets costing £162k which the college no longer own. Whilst we acknowledge that the net book value of these assets is nil, this has led to incorrect disclosure.

8.11.1 **2009 Recommendation:** We recommend that the college review the fixed asset register and identify which assets they no longer own and recognise the disposal of these assets within the accounts.

8.11.2 **2010 Update:** The client wrote off the £162k of scrapped assets after this was highlighted during the 2010 audit, however, further assets which had been scrapped were identified as part of our sample in our physical verification test.

8.11.3 **Further action required:** We recommend that the college carry out a review of the fixed asset register and identify which assets they no longer own and dispose of these assets from the accounts. This should be done in conjunction with the recommendation at 8.6.

8.11.4 **Priority: Medium**

8.11.5 **Management Response:** A review will take place during this academic session.

8.11.6 **Timescale:** July 2011.

## 8.12 Attendance at Committee Meetings

8.12.1 **2009 Observation:** We noted that one member of the finance committee had not attended any meetings during the year. We understand that this was due to other commitments.

8.12.2 **2009 Recommendation:** We recommend that the College remind committee members of their obligations to the College and monitor the attendance of committee members in order to identify any further instances on a timely basis. It is for the benefit of the college that committee members regularly attend meetings and in the instance that members are not able to provide the necessary commitment it may be more beneficial for the College to seek to appoint alternate members who may be more able to offer their experience and guidance to the Board.

8.12.3 **2010 Update:** We noted that one member of the audit committee had attended only one meeting during the year and that 3 members had attended only two meetings. We understand that this was due to work commitments and that the college was actively seeking new members with the appointment of 3 new members post year end.

8.12.4 **Further action required:** We recommend that the College continue to remind committee members of their obligations to the College and monitor the attendance of committee members in order to identify any further instances on a timely basis which can be followed up by the Board as appropriate.

8.12.5 **Priority** – Medium

8.12.6 **Management Response:** Agreed. Members will be reminded at the Board of Management meeting on 6<sup>th</sup> December 2010.

8.12.7 **Timescale:** 6<sup>th</sup> December 2010.

## 8.13 Operating and Financial Review

8.13.1 **2009 Observation:** We noted that the Operating and Financial Review is not fully compliant with the guidance issued by the Scottish Funding Council.

8.13.2 **2009 Recommendation:** We recommend that the College reviews and updates the financial statements in future years to ensure it is fully compliant with the guidance issued by the Scottish Funding Council.

8.13.3 **2010 Update:** The Operating and Financial Review is now compliant with the guidance issued by the Scottish Funding Council.

8.13.4 **Further action required:** No further action required.

## 9. MANAGEMENT LETTER – 2010

9.1 Those additional matters which were highlighted as a result of our 2010 audit procedures are detailed below along with our recommendations. This has been assigned a priority level in line with that explained in section 8.3.

### 9.2 Accounting for Petty Cash

9.2.1 **Observation:** During our testing of the petty cash balance we identified that the petty cash expenditure for Barra had only been posted up until the 6<sup>th</sup> July. We understand that this is due to a delay in the finance department receiving the receipts from the outreach centres. Whilst the amounts involved (£28) are negligible, non timeous updates can lead to erroneous reporting.

9.2.2 **Recommendation:** We recommend that petty cash receipts are provided on a timely basis from the outreach centres.

9.2.3 **Priority – Low**

9.2.4 **Management Response:** A reminder will be issued and this will be reviewed by the Management Accountant.

9.2.5 **Timescale:** March 2011.

### 9.3 Purchase cut-off

9.3.1 **Observation:** As part of our testing of purchase cut-off we sampled 6 purchase invoices post year end and found that 5 of these purchase invoices were recorded in the incorrect period. 3 of these items related to project costs and hence should also have been recorded with the associated accrued income. Thus, income and assets were also misstated as a result of this error.

9.3.2 **Recommendation:** We recommend that a careful review of post year end purchase invoices is carried out to ensure that expenditure is recorded in the year to which it relates.

9.3.3 **Priority – Medium**

9.3.4 **Management Response:** Agreed. Errors identified were largely due to funded projects where the decision to code to the new year was to save the creation of a creditor and debtor. The Management Accountant will ensure the policy is reviewed and adhered to.

9.3.5 **Timescale:** July 2011.

#### 9.4 Debtors Ledger

9.4.1 **Observation:** As part of our interim audit testing we reviewed the period 10 debtors ledger where we identified 2 large credit balances. We understand that these resulted from monies being received and invoices yet to be raised due to a member of the finance team having left and the guidance notes being mislaid.

9.4.2 **Recommendation:** We recommend that a procedures manual is created for the finance department where such guidance notes can be filed for reference should a member of staff absence.

9.4.3 **Priority – Low**

9.4.4 **Management Response:** The relevant income is contractual and does not require to go through the debtors ledger. Procedures will be updated by the Management Accountant.

9.4.5 **Timescale:** July 2011.

#### 9.5 Register of Interests

9.5.1 **Observation:** As part of our consideration of related party transactions we reviewed the Board of Management's register of interests. There were 4 Board members for which a register of interests had not been completed. 3 out of the 4 members were newly appointed and will be asked to complete a register of interest at the November board meeting. The other member was appointed in 2009.

9.5.2 **Recommendation:** We recommend that board members are asked to complete a register of interests on their appointment to ensure that any potential related parties are highlighted as soon as possible and that this be reviewed on an annual basis to identify any omissions or changes on a timely basis.

9.5.3 **Priority – Low**

9.5.4 **Management Response:** Board members are reminded at each Board meeting (Standing Agenda item in AOCB) of the need to keep the Register up to date.

9.5.5 **Timescale:** Ongoing.

#### 9.6 Non completion of bank reconciliations

9.6.1 **Observation:** At the time of the audit (October 2010) the bank reconciliations at 31<sup>st</sup> July 2010 were not available for those accounts held outwith the main ledger.

9.6.2 **Recommendation:** We recommend that bank accounts are reconciled on a monthly basis for all accounts as part of month end procedures.

9.6.3 **Priority – Low**

9.6.4 **Management Response:** Agreed – timescales to be adhered to.

9.6.5 **Timescale:** Immediate.

## 9.7 Accounting for Greenspace Capital Expenditure

9.7.1 **Observation:** From our review repairs and maintenance costs for potential capital items we identified costs for equipment purchases in relation to the Greenspace project which totalled £217k which had not been capitalised. We understand that the college matches these costs against grants received as they do not feel that the equipment is of significant value to the college.

9.7.2 **Recommendation:** We recommend that the college consider capitalising the costs in relation to the projects ran where the college will receive benefits which extend over a year.

9.7.3 **Priority – Low**

9.7.4 **Management Response:** Agreed.

9.7.5 **Timescale:** July 2011.

## **10. CURRENT ISSUES**

### **10.1 Changes to measurement of price inflation in public sector pensions**

On 22 June 2010, George Osborne, Chancellor of the Exchequer, announced a change of how price inflation will be measured for the purposes of annual increases in public sector pensions: from 2011, annual indexation will be accomplished by reference to the Consumer Price Index ("CPI") rather than the Retail Price Index ("RPI").

The impact of this has been accounted for by Barnett Waddingham determining the actuarial valuation for the pension scheme as at 31 July 2010. In doing this they have prepared their valuation on the basis that the change from RPI to CPI is a change in benefit. The gain arising from this valuation has therefore been taken directly to the Income and Expenditure account, in accordance with FRS 17. For Lews Castle College the past service gain for the current year has amounted to a credit of £166k to the income and expenditure account.

This accounting treatment is in line with others in the sector.

However, there is question as to whether the change from RPI to CPI should instead be treated as a change in assumption (rather than change in benefit). In this instance, the valuation would require to be reconsidered and any gain/ loss arising would be included within the balance sheet valuation rather than within the income and expenditure account.

The Accounting Standards Board ("ASB") is due to meet within the next few weeks to decide upon whether the change should be classified as a change in benefit or a change in assumption. Should they elect that this is a change in assumption, the valuation and accounts will require to be adjusted.

We will continue to review the situation and will keep the College apprised of the situation in order that any change can be acted upon accordingly. Note that should any change be made after the date of signing of the accounts, the current year results will be restated to reflect this within the financial statements for year ended 31 July 2011.

### **10.2 ASB 'Policy Proposal: the future of UK GAAP'**

The purpose of this consultation paper from the Accounting Standards Board (ASB) is to set out a proposed strategy for the future basis of UK GAAP and its convergence with International Financial Reporting Standards (IFRS).

The proposed approach is to work under the International Accounting Standards Board's (IASB) framework and to converge with IFRS to the fullest extent possible consistent with the needs of UK entities. The ASB's current intention is to issue an exposure draft withdrawing the separate body of literature currently referred to as UK GAAP and replacing it with new IFRS-based literature. Any modifications to the application in the UK of the underlying IFRS literature would be proposed at that stage.

The paper considers the future role of statements of recommended practice (SORPs) that are issued by industry or sectoral bodies that are recognised by the ASB. As a general principle, the ASB's view is that SORPs should only remain where there is a need arising from



sector specific issues not covered by guidance in accounting standards. The proposal is to restrict the number of SORPs to which the ASB provides any endorsement, however following consultation the ASB has reached the tentative decision (July 2010) that SORPs will be retained for certain Public Benefit Entities, including a SORP for Education.

The ASB intends issuing an exposure draft outlining its recommendations for the future of UK GAAP after considering the feedback on this paper.

It is noted that the SFC's expectation is that colleges will continue to converge with international financial reporting standards (IFRS) as UK GAAP converges over the next few years, and it appears likely that implementation will not take place before 2013. Consequently, it is highlighted that the transition timetables for IFRS that apply to the rest of the public sector do not therefore apply to colleges.

## STATEMENT OF THE BOARD OF MANAGEMENT RESPONSIBILITIES

The Board of Management is required to present audited financial statements for each financial year.

In accordance with the Further and Higher Education (Scotland) Act 1992, the Board of Management is responsible for the administration and management of the College's affairs, including ensuring an effective system of internal control, and is required to present audited financial statements for each financial year.

The Board of Management is responsible for keeping proper accounting records which disclose, with reasonable accuracy at any time, the financial position of the College and enable it to ensure that the financial statements are prepared in accordance with the Further and Higher Education (Scotland) Act 1992, the 2007 Statement of Recommended Practice – Accounting for Further and Higher Education Institutions and other relevant accounting standards. In addition, within the terms and conditions of a Financial Memorandum agreed between the Scottish Funding Council and the College's Board of Management, the Board of Management, through its designated office holder, is required to prepare financial statements for each financial year which give a true and fair view of the College's state of affairs and of the surplus or deficit and cash flows for that year.

In preparing the financial statements, the Board of Management is required to:

- Select suitable accounting policies and apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- Prepare financial statements on the going concern basis, unless it is inappropriate to presume that the College will continue in operation. The Board of Management is satisfied that it has adequate resources to continue in operation for the foreseeable future and for this reason the going concern basis continues to be adopted in the preparation of the financial statements.

The Board of Management has taken reasonable steps to:

- Ensure that funds from the Scottish Funding Council are used only for the purposes for which they have been given and in accordance with the Financial Memorandum with the Funding Council and any other conditions which the Funding Council may from time to time prescribe;
- Ensure that there are appropriate financial and management controls in place to safeguard public funds and funds from other sources;
- Secure the economical, efficient and effective management of the College's resources and expenditure.

The key elements of the College's system of internal financial control, which is designed to discharge the responsibilities set out above, include the following:

- Clear definitions of the responsibilities of, and the authority delegated to, Heads of academic and administrative departments;

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- A comprehensive medium and short-term planning process, supplemented by detailed annual income, expenditure, capital and cash flow budgets;
- Regular reviews of key performance indicators and business risks and quarterly reviews of financial results involving variance reporting and updates of forecast outturns;
- Clearly defined and formalised requirements for approval and control of expenditure, with investment decisions involving capital or revenue expenditure being subject to formal detailed appraisal and review according to approval levels set by the Board of Management;
- Comprehensive Financial Regulations, detailing financial controls and procedures, approved by the Audit Committee and the Finance and General Purposes Committee;
- Professional internal audit team whose annual programme is approved by the Audit Committee and endorsed by the Board of Management and whose Head provides the Board of Management with a report on internal audit activity within the College and an opinion on the adequacy and effectiveness of the College's system of internal control, including internal financial control.

Any system of internal financial control can only provide reasonable, but not absolute, assurance against material misstatement or loss.

## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE BOARD OF MANAGEMENT OF LEWS CASTLE COLLEGE, THE SCOTTISH PARLIAMENT AND THE AUDITOR GENERAL FOR SCOTLAND**

We have audited the financial statements of Lews Castle College for the year ended 31 July 2010 under the Further and Higher Education (Scotland) Act 1992. These comprise the Income and Expenditure Account, the Balance Sheet, the Cash Flow Statement and Statement of Total Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out within them.

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and for no other purpose. In accordance with paragraph 123 of the Code of Audit Practice approved by the Auditor General for Scotland, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

### **Respective responsibilities of the Board of Management, Accountable Officer and Auditor**

The Board of Management and Accountable Officer are responsible for preparing the Annual Report and the financial statements in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction issued thereunder by the Scottish Funding Council which requires compliance with the Statement of Recommended Practice on Accounting in Further and Higher Education Institutions. They are also responsible for ensuring the regularity of expenditure and income. These responsibilities are set out in the Statement of Board and Accountable Officer's Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and with International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland.

We report our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction. We also report if, in our opinion, the information which comprises the Operating and Financial Review, included in the Annual Report, is consistent with the financial statements. We also report whether in all material respects

- the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers;
- funds provided by the Scottish Funding Council have been applied in accordance with the Financial Memorandum dated 1<sup>st</sup> January 2006 and any other terms and conditions attached to them for the year ended 31 July 2010; and
- funds from whatever source administered by the college for specific purposes have been properly applied for the intended purposes.

In addition, we report to you if, in our opinion, the college has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE BOARD OF MANAGEMENT OF LEWS CASTLE COLLEGE, THE SCOTTISH PARLIAMENT AND THE AUDITOR GENERAL FOR SCOTLAND (CONTINUED)**

We review whether the Statement of Corporate Governance and Internal Control reflects the college's compliance with the requirements of the Scottish Funding Council and report if, in our opinion, it does not. We are not required to consider whether the statement covers all risks and controls, or form an opinion on the effectiveness of the college's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

**Basis of audit opinion**

We conducted our audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board as required by the Code of Audit Practice approved by the Auditor General for Scotland. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of expenditure and income included in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Board of Management and Accountable Officer in the preparation of the financial statements, and of whether the accounting policies are appropriate to the college's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE BOARD OF MANAGEMENT OF LEWS CASTLE COLLEGE, THE SCOTTISH PARLIAMENT AND THE AUDITOR GENERAL FOR SCOTLAND (CONTINUED)**

**Opinion**

**Financial statements**

In our opinion

- the financial statements give a true and fair view, in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction made thereunder by the Scottish Funding Council, of the state of affairs of the college as at 31 July 2010 and of its surplus, total recognised gains and losses and cash flows for the year then ended; and
- the financial statements have been properly prepared in accordance with the Further and Higher Education (Scotland) Act 1992 and the Accounts Direction made thereunder by the Scottish Funding Council; and
- information which comprises the Operating and Financial Review included with the Annual Report is consistent with the financial statements.

**Regularity**

In our opinion in all material respects

- the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers
- funds provided by the Scottish Funding Council have been applied in accordance with the Financial Memorandum dated 1<sup>st</sup> January 2006 and any other terms and conditions attached to them for the year ended 31 July 2010; and
- funds from whatever source administered by the college for specific purposes have been properly applied for the intended purposes.

Wylie & Bisset LLP  
Chartered Accountants and Registered Auditors  
168 Bath Street  
GLASGOW G2 4TP

**LEWS CASTLE COLLEGE**

Lews Castle College  
Stornoway  
Isle of Lewis  
HS2 0XR

20 December 2010

Messrs Wylie & Bisset  
Chartered Accountants  
168 Bath Street  
Glasgow  
G2 4TP

Dear Sirs

**LETTER OF REPRESENTATION**

We confirm to the best of our knowledge and belief the following representations given to you in connection with your audit of the charity's accounts for the year ended 31<sup>st</sup> July 2010.

1. We acknowledge as members of the Board of Management our responsibility for ensuring:
  - a) the financial statements are free of material misstatements including omissions.
  - b) that the financial statements give a true and fair view of the state of affairs of the College as at 31<sup>st</sup> July 2010.
  - c) all the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the College have been properly reflected and recorded in the accounting records.
  - d) all other records and related information, including minutes of all management meetings, have been made available to you.
  - e) the accounting policies used are detailed in the financial statements and are consistent with those adopted in the previous financial statements and are in accordance with the Accounts Direction issued by SFC under the terms of the Further and Higher Education (Scotland) Act 1992, and
  - f) compliance with the terms and conditions of the Financial Memorandum issued to the Board of Management by the SFC.
2. We have appointed CIB Services as Internal Auditors to the College as required by SFC. All reports issued to the College and our responses to them have been made available to you.
3. We acknowledge our responsibility for the design and implementation of internal control systems to prevent and detect fraud. We have disclosed to you the results of our risk assessment that the financial statements may be misstated as a result of fraud. There have been no irregularities (or allegations of irregularities) involving management,

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employees who have a significant role in internal control or others that could have a material effect on the financial statements.

4. The College has no liabilities or contingent liabilities other than those disclosed in the accounts.
5. All claims in connection with litigation that have been, or are expected to be, received have been properly accrued for in the financial statements.
6. There have been no events since the balance sheet date that require disclosure or which would materially affect the amounts in the accounts, other than those already disclosed or included in the accounts. Should further material events occur, which may necessitate revision of the figures included in the financial statements or inclusion of a note thereto, we will advise you accordingly.
7. The College has had at no time during the year any arrangement, transaction or agreement to provide credit facilities (including loans, quasi-loans or credit transactions) for the Board of Management nor to guarantee or provide security for such matters.
8. We confirm that we have disclosed to you all related party transactions relevant to the College and that we are not aware of any further related party matters that require disclosure in order to comply with the requirements of charities legislation, the Statement of Recommended Practice for Further and Higher Education accounts or accounting standards.
9. The College has not contracted for any capital expenditure other than as disclosed in the accounts.
10. The College has satisfactory title to all assets and there are no liens or encumbrances on the College's assets, except for those that are disclosed in the financial statements.
11. We are not aware of any irregularities, including fraud, involving management or employees of the College, nor are we aware of any breaches or possible breaches of statute, regulations, contracts, agreements or College's Constitution and Articles of Government which might result in the College suffering significant penalties or other loss. No allegations of such irregularities, including fraud, or such breaches have come to our attention.
12. We confirm that we are not aware of any possible or actual instance of non-compliance with those laws and regulations which provide a legal framework within which the College conducts its business.
13. We confirm that, in our opinion, the College is a going concern on the grounds that current and future sources of funding or support will be more than adequate for the College's needs. We have considered a period of twelve months from the date of approval of the financial statements. We believe that no further disclosures relating to the College's ability to continue as a going concern need to be made in the financial statements.
14. We confirm that although the SFC have indicated that they will be clawing back £842,000 of ELS SUMs our understanding is that this will be done in a way which will not



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significantly impact the college's short term cashflows including the period of 12 months from the date of signing the accounts.

15. We confirm that we have considered the attached unadjusted deviations. It is our view that the cost of making these adjustments to the financial statements outweighs any benefits that will be gained by users of the accounts. The combined effect of the deviations is not material and we do not consider that their absence from the financial statements affects the true and fair view given.
16. So far as the Board of Management is aware, there is no relevant audit information of which the College's auditors are unaware, and it has taken all the steps that it ought to have taken as a Board of Management to make itself aware of any relevant audit information and to establish that the college's auditors are aware of that information.

We confirm that the above representations are made on the basis of enquiries of management and staff with relevant knowledge and experience (and, where appropriate, of supporting documentation) sufficient to satisfy ourselves that we can properly make each of the above representations to you.

Yours faithfully

..... Chairman

..... Principal

**LEWS CASTLE COLLEGE  
SUMMARY OF DEVIATIONS**

Nature of Deviation & Reason for it	Actual Deviation £	Unadjusted I&E Effect £	Unadjusted B/S Effect £
Underaccrued SUSPLAN income	16,000	16,000	(16,000)
Reallocation of OFFTI balance	10,698	- -	10,698 (10,698)
OFFTI income recorded in the balance sheet	4,878	4,878	(4,878)
OFFTI expenditure recorded in the balance sheet	10,001	(10,001)	10,001
Potential accrual Strathclyde University	10,465	(10,465)	10,465

All of the above unadjusted amounts are immaterial in nature and have no effect on the audit opinion.