



# Lews Castle College

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

9 March 2021



**EY**

Building a better  
working world

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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 Lews Castle College (the College) for financial years 2016/17 to 2021/22. 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 Hywel Ball, 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.

# Executive Summary: Key Conclusions from our 2019/20 audit

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We have issued an unqualified audit opinion on the College's 2019/20 financial statements.

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We updated our risk assessment in response to the global pandemic, and as a result placed additional focus on:

- the adequacy of the College's disclosures in relation to the pandemic; and
- management's assessment of going concern and the related financial impact of Covid-19 on the College in the year and going forward.

## Financial Statements

We have completed our audit of the College's financial statements for the year ended 31 July 2020. Four audit adjustments were required which are reflected in the most up to date financial statements.

The draft financial statements and supporting working papers were provided significantly later than the normal agreed timetable, reflecting the pressures on management and the finance team during the Covid-19 pandemic. Given the minimal time available, we worked with the finance team to update and make improvements to the financial statements to ensure basic material compliance with accounting disclosure requirements, in particular around Covid-19 and going concern disclosures.

We concluded that the other information subject to audit, including the applicable parts of the Remuneration Report and the Annual Governance Statement were appropriate. We were satisfied that the disclosures reflect the College's compliance with the Code of Good Governance for Scotland's Colleges, and the key changes in governance arrangements that were required as a result of changes to working practices due to Covid-19.

## Going Concern

Management is required to conclude on the going concern basis of preparation in the financial statements. As a result of the unprecedented financial and operational pressures faced by the College to respond to Covid-19, we placed additional emphasis on management's assessment of going concern and the related need to report on the impact of financial pressures on the College and its financial sustainability. We were satisfied that the College remains a going concern and worked with management to ensure appropriate disclosures in the financial statements in relation to the College's financial position. We have considered the related risks to the financial sustainability of the College and its longer term delivery of strategic objectives in our wider scope reporting.

## Wider Scope and Best Value

We summarise the conclusions we reached in response to our work on the wider scope dimensions below.

### Financial Sustainability

The financial environment in which the College operates was already challenging, and the Covid-19 pandemic has resulted in further, significant financial pressures, and creates a risk that the College will not be able to develop viable and sustainable financial plans due to external factors.

The College prepared a financial forecast return in August 2020 which forecast a small underlying operating surplus position through 2022/23. This requires the realisation of a number of significant assumptions, including management of vacant positions, recovery of activities after Covid-19 and future cost savings and support from external bodies.

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### Governance and Transparency

A number of features of good governance have remained in place at the College and have been operating effectively throughout the Covid-19 lockdown. The College responded quickly to ensure that governance arrangements were appropriate and operating effectively during the lockdown period caused by the global pandemic.

However, a number of actions continue to remain unimplemented from previous audits, and a number of areas for improvement in the governance process therefore remain outstanding.

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### Financial Management

We are satisfied that the College's financial monitoring and reporting was clear and consistent throughout the year, considering the impact of Covid-19 on the financial performance in 2019/20. We are satisfied that the core financial management arrangements were not materially impacted as a result of Covid-19 and the subsequent lockdown.

However, the significance of the delay in the production of the financial statements indicates the extent of additional capacity pressures on the College finance team during this time. Working from home has clearly had a significant impact on the capacity of the finance team with minimal resilience or contingent capacity within such a small team. This will continue to be a significant risk on the financial management arrangements until working arrangements return to normal.

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# Introduction

## Purpose of this report

As a result of the impact of Covid-19, Audit Scotland agreed to extend our appointment as external auditor of the College by at least 12 months, to 2021/22.

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 Lews Castle College (“the College”) for the five year period 2016/17 to 2020/21. Our appointment term has recently been extended by a further 12 months, to financial year 2021/22. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

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 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 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. Where we identify areas for improvement, we will highlight these throughout this report together with our judgements and conclusions regarding arrangements, and where relevant recommendations and actions agreed with management.

## Our independence

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as your 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 committee on in June 2020.

## The impact of the Covid-19 Pandemic

We conducted our planning in accordance with Audit Scotland's Code of Audit Practice in April and May 2020, and presented our Annual Audit Plan to the College's audit committee in June 2020. While the declaration of the global Covid-19 pandemic and the resulting lockdown arrangements were in place, we noted at the time that there remained a significant number of uncertainties over how the pandemic could impact the College's financial statements preparation and arrangements around the areas of wider scope subject to audit. As a result, we revisited our planning assessments for the 2019/20 audit and presented an updated Annual Audit Plan Addendum to College management and chair of the Audit and Risk Committee in September 2020.

As a result of our assessment we have not identified any new financial statement risks. There are, however, a number of areas of audit where we identified increased risks or new areas of focus within existing risks. The financial statement disclosures were also expected to have been impacted by Covid-19, including:

- **Governance Statement:** The governance statement is required to capture how the governance arrangements changed during the lockdown period and what steps were taken to maintain a robust control environment during the disruption.
- **Disclosures and estimates:** Additional disclosures were required throughout the financial statements, including the performance and accountability report, to reflect the additional risks facing the College and how these have impacted the key judgements and estimates made in preparation of the financial statements. These include disclosures on significant events after the balance sheet date.
- **Going concern:** In accordance with the Government Financial Reporting Manual ('the FReM'), the College should prepare its financial statements on a going concern basis unless informed by the relevant national body of the intention for dissolution without transfer of services or function to another entity. Covid-19 has created increased financial pressures throughout the public sector. Uncertainty remains about the level of financial support that may become available from the Scottish Government to reflect the financial consequences. In light of this, the audit placed increased focus on management's disclosures regarding the going concern basis of preparation in the financial statements, in particular the financial impact of Covid-19 and the future financial sustainability of the College. The results of this assessment are reported in Section 2 on page 16.

The ongoing disruption to the delivery of further education as a result of Covid-19 has a pervasive impact upon the financial statements.

The financial statements have been updated to reflect the impact of Covid-19 on the College's financial position and performance.

### Adaption to remote working

Our audit fieldwork was completed remotely as a result of the Scottish Government's lockdown restrictions. There were two key impacts:

- Additional work was required to assess the format of evidence provided and where necessary, procedures were performed to validate the authenticity of evidence; and
- All contact with senior management and the finance team was conducted via virtual meetings. We would take this opportunity to thank the full team for their co-operation and support throughout this period.

### Our review and reassessment of materiality

Our Annual Audit Plan explained that our audit procedures would be performed using a materiality based on 1% of operating expenditure. We considered whether any change to our materiality was required in light of Covid-19 and we remain satisfied that the materiality values reported within our Annual Audit Plan remain appropriate. As we reported in our Annual Audit Plan Addendum we audit a number of areas of additional focus to lower materiality levels.

Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations. Factors which we consider include the perspectives and expectations of users of the financial statements as well as our risk assessment as to the likelihood of material misstatements arising in the financial statements.

We remain satisfied that the values reported to you in our Annual Audit Report for planning materiality, performance materiality and our audit threshold for reporting differences remain appropriate.

Overall Materiality

£135,000

1% of the College's operating expenditure

Tolerable Error

£65,000

Materiality at an individual account level

Nominal amount

£5,000

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 lower materiality levels to the audit of the Remuneration Report and Related Party Transactions.

### 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.

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 Group as at 31 July 2020 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).

Our findings are summarised in Section 2 of this report.

### Wider Scope audit

Our responsibilities extend beyond the audit of the financial statements. Together the Accounts Commission and the Auditor General for Scotland agreed the two dimensions set out in the Code which comprise the wider scope audit for small public sector bodies in Scotland. These are financial sustainability and governance and transparency. We outlined in our Annual Audit Plan Addendum that, given the impact of Covid-19 and associated risks around robust financial management, we would consider this dimension as part of our work in 2019/20.

Our findings are summarised in Section 3 of this report.



## Financial Statements audit

### Introduction

The financial statements provide the College with an opportunity to demonstrate accountability for the resources that it controls, and report on its overall performance in the application of those resources during the year.

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.

The plan highlighted one area that we identified as a fraud risk relating to the risk of fraud in revenue and expenditure recognition, including through management override of controls.

### 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 were 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).

Management provided draft financial statements in February 2021, approximately 3 months after the planned timeframe for the audit. The financial statements included a number of sections which were incomplete and were completed subsequent to the conclusion of the main audit work, including disclosures around going concern and the impact of Covid-19, pensions and fixed asset valuations. The financial statements also needed to be updated for the new requirements as outlined in the SFC's 2019/20 Accounts Direction for colleges and the new FE SORP which was applicable this year.

### Audit Outcomes

We identified four audit differences arising from the audit which have been reflected within the updated financial statements. We have outlined all audit adjustments at Appendix D. Our overall audit opinion is summarised on the following page.

The FE/HE SORP 2019 edition became effective for the year ended 31 July 2020. We considered any required changes in conjunction with management and concluded none were required. Management should ensure a detailed review of future accounting standard and disclosure requirements is undertaken on a timely basis.

#### Recommendation 1

# 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 at 31 July 2020 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 have issued an unqualified audit opinion on the 2019/20 financial statements for the College and 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. Our work is outlined in more detail on page 15.</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 are satisfied that in all material respects income and expenditure are regular.</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 matters to report.</p>   |

# Significant and fraud audit risks

## 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.

As also outlined in our Annual Audit Plan, we rebut 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 rebut the risk of improper recognition of payroll expenditure.

## 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 and 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 across all balances;
- Review and test income and expenditure around the financial yearend to ensure it is accounted for in the correct financial period;
- Perform an additional search for material payments and receipts received after year end and ensured these had been accounted for in the correct period; and
- Review both income and expenditure for additional revenue streams and related to the Covid-19 outbreak, such as additional grant income or additional health and safety costs.

## Our conclusions

- Our testing identified one misstatement relating to revenue and expenditure recognition, as outlined in Appendix D to this report. The impact of the misstatement was nil on the overall financial position of the College, with a corresponding impact on income and expenditure.
- There were no new material income or expenditure streams as a result of Covid-19. The College disclosed the additional income received in the year from the Government job retention scheme in line with the requirements of the Accounts Direction. We agreed the impact of Covid-19 on tuition fees with management and concurred with the treatment in the financial statements.

### Risk of management override

Our Annual Audit Plan recognises that under ISA (UK) 240, management is considered to be in a unique position to perpetrate fraud in financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively. We respond to this risk on every engagement.

### Risk of Fraud

- We considered the risk of fraud, enquired with management about their assessment of the risks of fraud and the controls to address those risks. We also updated and developed our understanding of the oversight of those charged with governance over management's processes over fraud.

### Testing of Journal Entries

- We tested the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. We obtained all journals posted in the financial year and used our data analysers to identify those requiring further investigation and corroboration, such as those posted by management to key accounts around the financial yearend.

### Judgements and Estimates

- We reviewed each significant accounting estimate for evidence of management bias, including retrospective consideration of management's prior year estimates.

### Significant unusual transactions

- We evaluated the business rationale for any significant unusual transactions appearing in the financial statements in the year.

### Accounting Policies

- We considered the consistency and application of accounting policies, and the overall presentation of financial information.

### Our conclusions

- We have not identified any additional risks in respect of potential frauds in the financial year.
- We have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls. We have outlined our consideration of this further in the financial management section of our wider scope audit work.
- There was no disagreement during the course of the audit over any accounting treatment or disclosure.

# Other Inherent Risk Area

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.

## Inherent Risk – Valuation of Property, Plant & Equipment

Given the value of the College estate, and the number of assumptions that are made in its valuation, we traditionally have assigned a higher inherent risk to the valuation property, plant and equipment. During the year, the Royal Institute of Chartered Surveyors (RICS) issued guidance highlighting that the uncertain impact of Covid-19 on markets may cause valuers to conclude that there is a material uncertainty at 31 March 2020. While this guidance was subsequently removed by 31 July 2020, there was a materially increased uncertainty around the valuation of assets in the current environment. In 2018/19 the College obtained a full valuation for its report which was reflected in the prior year financial statements.

Our approach focused on:

- Analysis of the College's estate, including consideration of the impact of Covid-19, any material changes from the prior year in its condition or planned future use, and assessment of the ongoing reasonableness of the assumptions and methods used in the valuation.
- Assessment of the potential for impairment across the College estate that has not been reflected in the financial statements or most recent formal valuation.

### Our conclusions

- We concluded that there were no material audit differences in the approach and conclusions around management's valuation of the College's estate at 31 July 2020.
- We recognise the short term impact that Covid-19 has had on the utilisation of the College estate, however given the long term useful lives of the assets and the plans to return to normal teaching arrangements in future we consider the carrying value to remain appropriate. This is something which should be kept under consideration by management going forward should teaching arrangements change on a more permanent basis in the future.

## Valuation of net pension liabilities

The College participates in two pension schemes: the Local Government Pension Scheme (Highland Council Pension Fund) and the Scottish Teachers Superannuation Scheme (STSS). At 31 July 2020, the College's share of the pension scheme net liability totalled £4.4 million (2018/19: £2.3 million) and the present value of the unfunded obligation in relation to early retirements agreed in previous years is £0.9 million (2018/19: £0.9 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.

Our approach included:

- obtaining an actuarial report at the year end date for the scheme and considering the reasonableness and consistency of actuarial assumptions underpinning such reports in conjunction with our internal specialists;
- performing substantive testing on the verification of the pension assets. Specifically, we engage with the auditor of Highland Council Pension Fund in line with the assurance protocols laid out by Audit Scotland for IAS 19 and FRS 102, including consideration of possible valuation uncertainties driven by the impact of Covid-19. We also analyse the fund's estimated asset position at 31 July 2020 from its financial yearend position at 31 March 2020 against expectations based on equity and other market movements in that time period;
- assessing the work of the actuaries in considering the impact of new and changing legal rulings impacting the liabilities in the fund, in particular in relation to the impact of updated guidance on the impact of the McCloud ruling and the new Goodwin judgement; and
- reviewing the calculation of the College's valuation of future early retirement liabilities at 31 July 2020, including the integrity of the underlying pensioner data used by the actuary and College.

### Our conclusions

- We have outlined in Appendix D an audit adjustment in relation to valuation of the College's share of the Highland Pension Fund liability related to the McCloud judgement. This relates to where the Fund's actuaries use high level estimates for the yearend liabilities, however more detailed analysis concludes a different estimate position.
- 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.

# Going concern

In accordance with the FReM, the College shall prepare its financial statements on a going concern basis unless informed by the relevant national body of the intention for dissolution without transfer of services or function to another entity. However, International Auditing Standard 570 Going Concern, as applied by Practice Note 10: Audit of financial statements of public sector bodies in the United Kingdom, still require auditors to undertake sufficient and appropriate audit procedures to consider whether there is a material uncertainty on going concern that requires reporting by management within the financial statements, and within the auditor's report.

The rationale for going concern remains the same, but we placed increased focus on management's assertion of going concern and disclosures relating to financial sustainability as a result of the uncertainty and unprecedented budget pressures caused by Covid-19.

Covid-19 has created a number of financial pressures throughout the public sector, including further education. Uncertainty remains about the level of financial support that may become available from the Scottish Funding Council (SFC) to reflect the financial consequences of Covid-19. As a result, the SFC's 2019/20 Accounts Direction requires an explanation of the adoption of the going concern basis and mitigating actions taken as a result of Covid-19 to be included as part of the going concern commentary within the College's financial statements, both in the Performance Overview and Annual Governance Statement.

Management's going concern assessment and associated disclosures cover at least the 12 month period from the date of approval of the financial statements, but may be expected to include future performance through the medium term.

The College has concluded that there are no material uncertainties around its going concern status. We have outlined our consideration of the College's financial position in the financial sustainability section of this report. Management has provided a cash flow forecast for the College through the going concern assessment period to supplement its formal assessment paper.

We considered:

- the completeness of factors considered in management's going concern assessment;
- the integrity and robustness of the underlying cash flow forecasts supporting future financial projections, in particular if the College projects to require financial support during the going concern assessment period and the risk of it breaching loan covenants at 31 July 2021; and
- the appropriateness of disclosures in the financial statements in relation to going concern and future financial performance in line with the requirements of the SFC 2019/20 Accounts Direction.]

## Our conclusions

- We are satisfied that it remains appropriate for the College and Group financial statements to be prepared on a going concern basis, in particular recognising the SFC's confirmation it would provide support in cash flow management should it be required through the going concern period.
- We worked with management to improve the adequacy of some of the disclosures in relation to going concern and the expected medium term financial impact of Covid-19 on the College. We are satisfied with the updated disclosures.



## 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 each of the wider scope audit dimensions applicable to smaller bodies. The application of the smaller body status for the College is in line with the guidance set out by Audit Scotland in its planning guidance. We apply our professional judgement to risk assess and focus our work on each of the dimensions.

### The Wider Scope dimensions

#### Financial Management:

- Considers the effectiveness of financial management arrangements, including whether there is sufficient financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively. This dimension of wider scope work is not usually applicable to smaller bodies, however due to the increased risk around financial management at the College in the circumstances this year we have made the judgement to consider as part of our audit process.

#### Financial Sustainability:

- Considers the medium and longer term outlook to determine if planning is effective to support service delivery. This will focus on the arrangements to develop viable and sustainable financial plans.

#### Governance and Transparency:

- Is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

We outlined in our Annual Audit Plan Addendum, presented to management and the chair of the Audit Committee in September 2020, how our consideration and audit work in respect of the wider scope dimensions would be impacted by Covid-19. Our areas of audit focus in these areas have therefore been undertaken through the lens of Covid-19.

# Financial Sustainability

The financial environment in which the College operates was already challenging, and the Covid-19 pandemic has resulted in further, significant financial pressures, and creates a risk that the College will not be able to develop viable and sustainable financial plans due to external factors.

The College prepared a financial forecast return in August 2020 which forecast a small underlying operating surplus position through 2022/23. This requires the realisation of a number of significant assumptions, including management of vacant positions, recovery of activities after Covid-19 and future cost savings and support from external bodies.

## The context for financial sustainability in the FE sector

During 2020, the Scottish Funding Council released three reports considering the future of colleges and universities. Most recently in October 2020 the SFC published their review of coherent provision and sustainability which considered how best the SFC can fulfil its mission of securing coherent provision by post-16 education bodies, and the undertaking of research in these changing times. The review covered future provision, delivery, outcomes and targets, funding models and support for research activity across the college and university sector in Scotland.

Specifically, as part of this review, the SFC published their updated analysis of the sector within their report, The Financial Sustainability of Colleges and Universities in Scotland. This reflects on the specific financial challenges the sector was facing prior to the impact of Covid-19, including cost pressures from cost of living pay awards, employers' pension contributions, maintaining the college estate and the UK's exit from the European Union, and notes that colleges were already implementing transformation plans to address those challenges. Covid-19 has, in some cases, resulted in the delay of these transformation plans, particularly where they relate to severance and commercial income growth. The main impact of Covid-19 is considered to be felt most by the sector during the 2020/21 financial and academic year.

Recognising the financial challenges facing colleges in the upcoming period, the SFC identified a number of actions to further support colleges including:

- Targets – SFC will not recover funds for shortfalls against outcome agreement targets where these are related to Covid-19.
- Capital Funding – £2.3 million of additional funding for colleges has been awarded to support the provision of ICT equipment to help tackle digital poverty. In addition, the SFC announced £6.5 million of additional capital funding to support the economic recovery in 2020/21.
- Cash advances – SFC has provided flexibility in grant drawdowns to several colleges encountering liquidity challenges.
- Flexibilities in relation to Flexible Workforce Development Fund, Student Support funds and credits.

Work is underway to consider the full impact of the financial saving requirements outlined in the FFR against the College's strategic objectives.

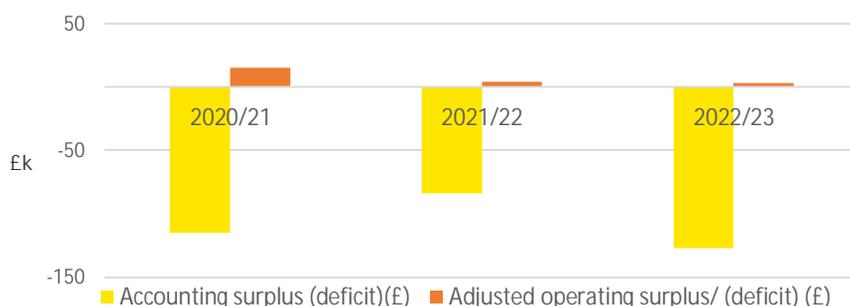
Additional funding is also expected to become available in relation to the Youth Guarantee Scheme (£10 million direct funding for colleges), the transitional training fund and use of the Coronavirus Job Retention Scheme.

In addition to these steps, the SFC is working with the Scottish Government and other stakeholders on a possible Transformation Investment Fund to support colleges to make specific one-off investments to achieve lasting improvement in their financial health.

### Medium term financial forecasting

The College prepared a three-year financial forecast for the period 2020 to 2023 and submitted this to the SFC in the form of the template Financial Forecast Return ('FFR'). The forecast is based on assumptions provided by the SFC in addition to College specific assumptions for areas such as other income and staff numbers. The assumptions have been subject to scrutiny by the College's senior management team and Finance Committee. As Exhibit 1 demonstrates, the College forecasts recurring underlying operating surpluses for the three years of the plan, but with minimal headroom.

Exhibit 1: The College's FFR highlights that the College is forecasting a small adjusted operating surplus for the three years of the FFR period through to 2022/23.



Source: Lews Castle College Financial Forecast Return, September 2020

The College's forecasts recognise significant uncertainty in the current environment. The main risks associated with the forecast income and expenditure in the financial forecast return are:

- Continued uncertainty around the future impact of Covid-19 on the College's operations, with all income generating operations expected to be back to normal operations from 2021/22.
- The ongoing delivery of target student numbers going forward is noted as an ongoing risk for the College.
- Ongoing uncertainty around staff costs as pay increases and other equalisation of benefits are subject to national bargaining outwith the College's control.
- The 2020/21 financial position is balanced by the planned delay in recruiting for vacant positions, saving up to £250,000.

## Medium term financial strategy and plan

Financial forecasting, and the impact of required financial decisions, should be formally aligned to the College's strategic planning.

Recommendation 2

We outlined in previous years that while the FFR submission process itself is robust, the College does not explicitly align its financial forecasts to its overall strategic or operational objectives. The College's forecast financial position over the medium term, outlined on the previous page, outlines a number of areas of significant risk to the financial position which, if realised, may require significant savings or increased support to allow the College to obtain a breakeven operating position in the future. The uncertainty of the future impact of Covid-19, combined with the potential significance of savings requirements and other future required financial decisions continues to increase the risk that financial savings requirements materially impact the College's ability to meet its strategic objectives.

## Going concern cash flow forecasting

We have outlined our work in respect of going concern on page 15 of this report. While the College has prepared its financial statements on a going concern basis as required by the FReM for a public body, it is required to consider its ability to meet liabilities as they fall due over the going concern assessment period, being 12 months from the approval of the financial statements.

Management should ensure that its cash flow position and forecast for at least the next 12 months is subject to rigorous review on a routine basis. Any uncertainty around the College being able to support itself should be reported to the Regional Strategic Body and SFC to discuss support options.

Recommendation 2

As part of its financial forecasting arrangements the College has forecast its cash flow at a summary level for the three years of the FFR and at a detailed level through to July 2021, and is updating this to cover the going concern period to December 2021. The College forecasts holding cash of at least £155,000 during the 2020/21 financial year, however this is subject to significant volatility risk depending on the future impact of Covid-19 on the College's operations.

# Financial Management

We are satisfied that the College's financial monitoring and reporting was clear and consistent throughout the year, considering the impact of Covid-19 on the financial performance in 2019/20. The College has an established budget setting and monitoring framework. We are satisfied that the core financial management arrangements were not materially impacted as a result of Covid-19 and the subsequent lockdown, and have not identified any weaknesses in the design and implementation of key controls through the year either before or after the Covid-19 lockdown and resulting working from home.

However, the significance of the delay in the production of the financial statements indicates the extent of additional capacity pressures on the College finance team during this time. Working from home has clearly had a significant impact on the capacity of the finance team with minimal resilience or contingent capacity within such a small team. This will continue to be a significant risk on the financial management arrangements until working arrangements return to normal.

## Financial performance and monitoring

The College reported a deficit of £487,000 for the year (2018/19: £470,000). Following an actuarial loss of £1.6 million, the College reported total comprehensive expenditure of £2.1 million (2018/19: £2.5 million). The College had an operating surplus after removal of non-cash accounting adjustments (relating to pension and capital accounting) of £174,000 (2018/19: £23,000 deficit).

The financial performance in 2019/20 was significantly impacted by Covid-19. In particular, tuition fee and other non-SFC income reduced significantly following the College closure in March 2020. This reduction in income was offset by staff savings through the furlough scheme and other savings related to delayed expenditure.

In line with previous years, the College's financial performance was monitored throughout the year by management and the Finance Committee. This process was not impacted by Covid-19, and there is evidence of financial monitoring, reporting and planning by the Board and relevant committees through the financial year, up to the approval of the 2020/21 budget and its submission to the SFC in June 2020. Throughout 2019/20 management reported budget pressures and variances through its management accounting. These were significant in the year, however we are satisfied these related to the unforeseen impact of Covid-19 on College operations on the last four months of the financial year.

## Impact of Covid-19 on systems of internal control and financial statements preparation

Within the Annual Governance Statement, the College has concluded that they have obtained assurance that the system of internal control was operating effectively during the year with no exceptions or issues identified. Through our audit of the financial statements, we consider 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 implemented as designed.

We undertook an initial assessment of the financial control environment as part of our planning work in June 2020, and updated our understanding as part of the yearend audit, in particular to consider the impact of Covid-19 on the financial management environment. Our work has not identified any significant weaknesses in the College's systems of internal control. In particular, we have not identified any significant changes to the design and implementation of controls as a result of the impact of Covid-19 on working arrangements.

The head of finance, college management and the Finance Committee, should keep the financial management resilience of the College under close scrutiny through the remainder of the working from home period.

### Recommendation 3

We noted through this report that the timeframe for the preparation of the financial statements, and the underlying supporting schedules, has been significantly delayed this year compared to previous years. These delays have been necessary to ensure that management and the finance team had the time to address all requirements of the financial statements preparation process, and ensure that all audit queries are responded to sufficiently to allow our audit opinion to be signed off as well. However, the additional time required this year clearly reflects the extent of additional pressures on the finance team, and the impact of working from home on a small team with limited contingency and less sophisticated online systems compared to some institutions. The longer working from home arrangements continue under Covid-19, the greater the risk that financial management arrangements, including key controls, start to be impacted.

### 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. We submitted an assessment of the College's participation in the exercise to Audit Scotland in 2019, along with a follow up in February 2020. As part of our yearend audit arrangements, we have seen evidence that the College continues to submit the required data and follow up on identified matches as appropriate.

# Governance and Transparency

A number of features of good governance have remained in place at the College and have been operating effectively throughout the Covid-19 lockdown. The College responded quickly to ensure that governance arrangements were appropriate and operating effectively during the lockdown period caused by the global pandemic.

However, a number of actions continue to remain unimplemented from previous audits, and a number of areas for improvement in the governance process therefore remain outstanding.

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## Annual Governance Statement

The College has demonstrated through the year that it has implemented a number of the key requirements for good governance. The key aspects of governance arrangements in the year are required to be disclosed in the College's Annual Governance Statement within the financial statements. We reviewed the governance statement within the financial statements against the requirements outlined in the SFC's 2019/20 Accounts Direction and our understanding of governance arrangements in place up to 31 July 2020.

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:

- Ensuring that the College has met all requirements of the SFC's 2019/20 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; and
- 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 in the statement.

We reviewed an initial draft by of the governance statement by management and provided comments on areas to be enhanced, in particular around disclosing the impact of Covid-19 on governance arrangements in the year and the status of planned actions from prior year. These were updated in the final version of the accounts.

Governance arrangements were quickly developed to ensure that the College was kept informed of the impact of Covid-19. We were therefore satisfied that Board members had sufficient information to continue to fulfil their role.

### Covid-19 Governance Arrangements

Like all other public bodies in Scotland, the College moved to revised governance arrangements at the beginning of the UK lockdown period. Board meetings and other committee meetings scheduled from April 2020 continued via remote working arrangements, and all relevant business continued to be considered as required, with the exception of the remuneration committee not being able to meet at the previously scheduled date, which is in the process of being mitigated.

Risks associated with the pandemic have also been considered by the Board through an updated risk register, which has been considered by the Audit Committee in the year. We are satisfied that key information continues to be disseminated to the Board and other committees on a timely basis.

### Enquiries of those charged with governance

In line with previous years, we formally wrote to the Chair of the Audit Committee to make inquiries around the College's governance arrangements, including consideration by those charged with governance in respect of compliance with laws and regulations; identification of fraud, error and breaches of internal control; and material litigation and claims. No matters of concern were raised in the response provided.

Internal audit's opinion for the year was based on its agreed audit plan as approved by the Audit and Risk Committee. For 2019/20, the internal auditor's opinion notes that it 'is satisfied that, for the areas reviewed during the year, Lews Castle College has reasonable and effective risk management, control and governance processes in place.' The internal auditors have noted that they were not able to complete all planned internal audit work in the year due to the Covid-19 pandemic, however this has not impacted their opinion.

### 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 most recent reports considered include the SFC's Review of Coherent Provision and Sustainability. Management has confirmed this will be issued to the Finance Committee and considered at a future meeting.

The areas for improvement in governance arrangements should be addressed as a priority in 2021 as soon as capacity allows. Capacity going forward should be kept under ongoing review.

#### Recommendation 4

### Progress around governance improvements

In our prior year Annual Audit Report, we noted that a number of areas of good governance had outstanding actions from various external reports and findings, and that progress in addressing these had been limited. These areas included addressing non-compliance areas with the Code of Good Governance, maintaining policies and procedures, and implementing governance improvements from external reviews. Our view was that the overall pace of improvement at the College around governance arrangements indicated insufficient management capacity to address the required improvements.

Progress around these areas has been limited in 2020, resulting from changes in key personnel and then the impact of the Covid-19 pandemic on the College Board's priorities. At the time of drafting this report the following matters remain outstanding:

- Completion of an externally facilitated review of governance arrangements in line with the three yearly requirement;
- Full assessment of compliance with the code of good governance, including assessment of prior identified non-compliance and action plan for addressing remaining areas;
- Up to date posting of key Board and Committee papers and minutes to demonstrate good practice transparency arrangements; and
- Maintaining of a full list of policies and procedures and ensuring appropriate timely review and updating by the relevant individuals.

### EU withdrawal

There continues to be a significant interest in public bodies' preparedness for EU withdrawal. We are aware that management has continued to consider and monitor the arrangements and risks around the UK's departure from the EU and the upcoming end of its transition period. The College is aware that there continues to be a potential for disruption to operations and costs arising from Brexit and continues to review any new information and guidance provided by bodies such as Scottish Government and the SFC as it is published. Management is confident at this stage that the College is mitigated from the immediate direct impacts of Brexit on its operations and funding.

### Compensation for loss of office

There were two posts made redundant in 2018/19, resulting in two individuals receiving compensation for the loss of office during 2019/20. The College accounted for payments of £23,100 for these redundancies, and both payments were calculated using statutory terms. We confirmed that the College had followed the procedures outlined within SFC's guidance for seeking approval for the redundancy payments.



## Appendices

A – Code of Audit Practice: responsibilities

B – Independence and audit quality

C – Required communications with the audit and risk committee

D – Audit differences identified during the audit

E – Audit recommendations identified throughout the audit, including prior year recommendation status updates

F – Timing and deliverables of the audit

# Appendix A: Code of Audit Practice Responsibilities

## Audited Body's Responsibilities

|   |  |
|---|--|
| <p>Corporate Governance</p>   | <p>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, risk and governance committees or equivalent) in monitoring these arrangements.</p>   |
| <p>Financial Statements and related reports</p>                           | <p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> <li>• 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.</li> <li>• maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.</li> <li>• ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.</li> <li>• maintaining proper accounting records.</li> <li>• 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.</li> <li>• 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.</li> </ul> <p>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.</p> |
| <p>Standards of conduct / prevention and detection of fraud and error</p> | <p>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.</p>  |
| <p>Standards of conduct / prevention and detection of fraud and error</p> | <p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> <li>• such financial monitoring and reporting arrangements as may be specified</li> <li>• compliance with any statutory financial requirements and achievement of financial targets</li> <li>• balances and reserves, including strategies about levels and their future use</li> <li>• how they plan to deal with uncertainty in the medium and longer term</li> <li>• the impact of planned future policies and foreseeable developments on their financial position.</li> </ul>  |

# 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 2019 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 May 2020.

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 College consider the facts known collectively to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the audit committee in November 2020.

## Audit Fees

|   | 2019/20 | 2018/19 |
|---|---------|---------|
| Component of fee:                       |         |         |
| Auditor remuneration - expected fee     | £20,320 | £17,000 |
| Additional audit procedures (see below) | £13,400 | £3,250  |
| Audit Scotland fixed charges:           |         |         |
| Pooled costs                            | £1,160  | £980    |
| Contribution to Audit Scotland costs    | £1,110  | £1,030  |
| Total fee                               | £35,990 | £22,260 |

The expected fee for each body is set centrally by Audit Scotland, and assumes that it has sound governance arrangements in place and operating effectively throughout the year, prepares comprehensive and accurate draft financial statements and supporting schedules, and meets the agreed timetable for the audit. It also assumes there is no major change in respect of the scope of work in the year and an unqualified audit opinion resulting from the audit.

The 2019/20 audit has required significant additional audit input to address a number of matters, in particular; the need for a reassessment of all audit risks, the additional scrutiny around the College's response to and financial statement disclosures around the direct and indirect consequences of Covid-19, including going concern and financial sustainability consideration and the impact on financial management arrangements; additional audit specialist and manager work around the College's share in the Highland Council Pension fund, and reallocation of staff to address changes in timing to the delivery of audit work. This has resulted in the additional work resulting in the fee variation outlined above and agreed with management.

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 2020 UK Transparency Report can be accessed on our website at [https://www.ey.com/en\\_uk/who-we-are/transparency-report-2020](https://www.ey.com/en_uk/who-we-are/transparency-report-2020). This material is published to provide a timely and relevant source of information about EY in general, and our audit business in particular. This includes our inaugural Audit Quality Report.

The disclosures are extensive. For example, they explain 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 (AOB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AOB meets monthly and also holds an annual strategy session. The AOB reports to the EY UK Board. The AOB 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 at the IJB since appointment can be found at: <https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-201920>.

# Appendix C: Required communications

| Required communication   | Our reporting to you   |
|--|--|
| <p>Terms of engagement / Our responsibilities</p> <p>Confirmation by the audit, risk and governance 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>Planning and audit approach</p> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>  | <p>Annual Audit Plan<br/>Annual Audit Plan Addendum</p>  |
| <p>Significant findings from the audit</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<br/>Annual Audit Report</p>   |
| <p>Going concern</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>Misstatements</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>Fraud</p> <ul style="list-style-type: none"> <li>• Enquiries of the audit, risk and governance 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>Consideration of laws and regulations</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, risk and governance committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the 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>Related parties</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>Independence</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>Internal controls</p> <p>Significant deficiencies in internal controls identified during the audit</p>  | <p>This Annual Audit Report – no significant deficiencies reported</p>                           |
| <p>Subsequent events</p> <p>Where appropriate, asking the audit, risk and governance 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>Material inconsistencies</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: Errors identified during the audit - adjusted

This Appendix sets out the significant adjustments processed in the financial statements finalisation.

| Adjusted differences |  |   |   |  |
|----------------------|--|---|---|--|
| No.                  | Description  | Income and Expenditure Impact                           | Other Comprehensive Income and Expenditure Impact | Balance Sheet Impact                                     |
| 1                    | Adjustment relating to late SFC confirmation regarding 2019/20 job evaluation funding                          | DR Staff costs<br>£177,129<br>CR SFC Income<br>£177,129 |   | DR Accrued income<br>£177,129<br>CR Accruals<br>£177,129 |
| 2                    | Adjustment relating to the impact of the McCloud judgement – reversal of the past service gain from prior year | DR Past service gain<br>£61,000                         |   | CR Pension Liabilities<br>£61,000                        |
| 3                    | Adjustment to ensure that the impact of the McCloud judgement is recognised in the OCI                         |   | DR Actuarial loss<br>£21,000                      | CR Pension Liabilities<br>£21,000                        |
| 4                    | Being the increase in early retirement pension provision based on the updated discount rate being applied      | DR Pension Expense<br>£96,884                           |   | CR Pension Provision<br>£96,884                          |

# Appendix E: Audit recommendations, including prior year recommendations

This action plan summarises specific recommendations included within the 2020 Lews Castle College 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  | Recommendation  | Management response / Implementation timeframe  |
|-----|---|---|---|
| 1   | The FE/HE SORP 2019 edition became effective for the year ended 31 July 2020. We considered any required changes in conjunction our review of the financial statements and concluded none were required. As part of our review of the accounts we noted areas of disclosure which needed updated to reflect the requirements of the SFC accounts direction.   | Management should ensure a detailed review of future accounting standard and disclosure requirements is undertaken on a timely basis.<br><br>Grade 2  | Response: Agreed. Management will review any planned changes to financial reporting requirements in advance of preparing the annual financial statements.<br><br>Responsible officer: Head of Finance.<br><br>Implementation timeframe: Ongoing.  |
| 2   | While the College has prepared its financial statements on a going concern basis as required by the FReM for a public body, it is required to consider its ability to meet liabilities as they fall due over the going concern assessment period, being 12 months from the approval of the financial statements.<br><br>We outlined in previous years that while the FFR submission process itself is robust, the College does not explicitly align its financial forecasts to its overall strategic or operational objectives. | Financial forecasting, and the impact of required financial decisions, should be formally aligned to the College's strategic planning going forward.<br><br>Management should ensure that its cash flow position and forecast for at least the next 12 months is subject to rigorous review on a routine basis.<br><br>Any uncertainty around the College being able to support itself should be reported to the Regional Strategic Board and Scottish Funding Council to discuss support options.<br><br>Grade 1 | Response: Agreed. The College will align financial forecasts to the wider strategic planning in the future. A 12 month cashflow forecast was prepared with the financial statements and there was no indication that there would be a shortage of cash in the upcoming financial year.<br><br>Responsible officer: College Board of Management, coordinated by Principal.<br><br>Implementation timeframe: Through to October 2021. |

### Classification of recommendations

| No. | Findings  | Recommendation  | Management response / Implementation timeframe   |
|-----|---|---|--|
| 3   | <p>We have noted through this report that the timeframe for the preparation of the financial statements, and the underlying supporting schedules, has been significantly delayed this year compared to previous years.</p> <p>The additional time required this year clearly reflects the extent of additional pressures on the finance team, and the impact of working from home on a small team with limited contingency and less sophisticated online systems compared to some institutions.</p> | <p>The longer working from home arrangements continue under Covid-19, the greater the risk that financial management arrangements, including key controls, start to be impacted.</p> <p>The head of finance, college management and the Finance Committee, should keep the financial management resilience of the College under close scrutiny through the remainder of working from home period.</p> <p style="text-align: right;">Grade 1</p> | <p>Response: Agreed. Management will keep the financial management arrangements and in particular progress against key deliverables under scrutiny through the rest of 2021. The College have seconded a Finance Director on a part time basis from another UHI partner and intend to appoint a permanent director in the 2021/22 academic year.</p> <p>Responsible officer: College Board of Management, coordinated by Principal.</p> <p>Implementation timeframe: Throughout 2021 ongoing.</p>  |
| 4   | <p>Progress around improving governance arrangements has been limited in 2020, resulting from changes in key personnel and then the impact of the Covid-19 pandemic on the College Board's priorities. At the time of drafting this report a number of significant matters remain outstanding.</p>  | <p>The areas for improvement in governance arrangements should be addressed as a priority in 2021 as soon as capacity allows. Capacity going forward should be kept under ongoing review.</p> <p style="text-align: right;">Grade 1</p>   | <p>Response: Agreed. The Board Secretary will establish a baseline setting out areas for improvement in consultation with the External Auditors. A Development Plan - Governance - 2021/22 with timelines, proposed actions and setting out ownership to address matters outstanding, including those set out on page 24 of the Report, together with any associated findings from the 2021 External Review (which is currently underway) will be submitted to the Board in June 2021.</p> <p>Responsibility: Board of Management.<br/>Responsible Officer: Board Secretary</p> <p>Implementation timeframe: Report to Board - 22 June 2021. Capacity will be kept under review to enable the actions set out in the approved Development Plan - Governance to be implemented by 31 July 2022.</p> |

# Appendix F: 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 2019/20 audit cycle.

|     | Audit Activity   | Deliverable                                   | Timing                 |
|-----|--|---|------------------------|
| FEB | <ul style="list-style-type: none"> <li>Review progress of NFI exercise</li> </ul>  | Submit NFI Questionnaire                      | 28 February 2020       |
| MAR |  |   |                        |
| APR | <ul style="list-style-type: none"> <li>Audit planning and setting scope and strategy for the 2019/20 audit</li> </ul>    | Annual Audit Plan                             | April/May 2020         |
| MAY |  |   |                        |
| JUN | <ul style="list-style-type: none"> <li>Walkthrough Visit</li> </ul>  | Completion of internal documentation          | June 2020              |
| JUL |  |   |                        |
| SEP | <ul style="list-style-type: none"> <li>Year-end substantive audit fieldwork on unaudited financial statements</li> </ul> | Audited Financial Statements                  | September/October 2020 |
| OCT |  |   |                        |
| NOV | <ul style="list-style-type: none"> <li>Conclude on results of audit procedures</li> </ul>                                | Issue Annual Audit Report                     | 31 December 2020       |
| DEC |  |   |                        |
| JAN |  |   |                        |
| MAR | <ul style="list-style-type: none"> <li>Issue opinion on the College's financial statements</li> </ul>                    | Submit Audit Scotland minimum dataset request | 8 March 2021           |

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