

Audit Committee Item 5.2 4/09/17

Purpose

The purpose of this paper is to update the Audit Committee on the Accounts Direction received for The Lanarkshire Board (TLB) for 2016-17, sets out the basis of a review of the specific arrangements that have been in place during the financial year, and proposes options available to TLB for the 2016-17 annual report and accounts.

The Audit Committee are requested to review the options available and agree a proposal for approval by the Board.

Background

TLB was not fully operational during financial year 2015-16 and fully fundable status was not awarded to New College Lanarkshire (NCL) as the Regional Strategic Body (RSB) until August 2016. The prior auditors of NCL determined that TLB did not exercise sufficient decision making and control over the Board of South Lanarkshire College (SLC) to require consolidated accounts to be prepared as at 31 July 2016.

Both colleges have received an Accounts Direction from the Scottish Funding Council that requires the preparation of an annual report and accounts that comply with the 2015 SORP: Accounting for Further and Higher Education (HE/FE SORP) and are in accordance with their Financial Memorandum with the SFC.

The Lanarkshire Board received a separate 2016-17 Accounts Direction from the Scottish Funding Council on 26 July 2017 stating that:

'Under the relevant accounting standards, and given the wide ranging powers enshrined in the legislation that RSBs have over assigned colleges, it would appear likely that consolidated financial statements may require to be prepared by New College Lanarkshire. However, we fully recognise that the decision on whether consolidated financial statements will need to be prepared, based on a review of the specific arrangements which have been in place during the year, rests with the RSB and its auditors.'

The 2015 SORP: Accounting for Further and Higher Education requirements for consolidation mirror those of FRS 102.

FRS 102 states: *A subsidiary is an entity that is controlled by the parent. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. And 'Control can also exist when the parent has the power to exercise, or actually exercises, dominant influence or control over the undertaking or it and the undertaking are managed on a unified basis.'*

The Post-16 Education (Scotland) Act 2013 gives RSBs significant powers over the colleges, which, if exercised, demonstrate that the requirements of the SORP and FRS 102 are met. The external auditors have considered the RSBs powers through the Act, whether they have occurred during the 2016-17 financial year and whether they are an indication of control (see Appendix 1). Their conclusion is that there is the 'power to control' and as such, consolidated financial statements are required.

Options available to The Lanarkshire Board

Option	Implication
<p>Do nothing Prepare NCL and SLC accounts only. NCL Annual report does not contain information pertaining to governance as an RSB</p>	<p>Opinion on NCL financial statements will be qualified on the basis that they are materially misstated from the non-inclusion of SLC. Opinion on the 'other information in the annual report and accounts' would be qualified as RSB governance not fully explained. Qualification of financial statements is likely to lead to the Auditor General for Scotland issuing a s22 report on the College.</p>
<p>Three sets of accounts – NCL, SLC and TLB NCL and SLC accounts prepared, audited and authorised as in prior years. Subsequently an annual report and accounts will be prepared, audited and authorised for TLB.</p>	<p>Additional resource costs for NCL to produce the TLB annual report and accounts. Additional fee implications for the audit of the consolidation process and subsequent group accounts and audit of the TLB annual report.</p>
<p>NCL prepares TLB accounts only SLC accounts would be prepared, audited and authorised as in prior years. NCL would then produce a consolidated annual report and accounts, using the notes to the accounts to extract sufficient information on NCL to meet their Accounts Direction.</p>	<p>Additional resource costs for NCL to produce the TLB annual report and accounts. Additional fee implications for the audit of the consolidation process.</p>

If the second option of preparing three sets of accounts is taken, the submission deadline of 31 December is unlikely to be met given the short amount of time NCL have to prepare for the change. The Scottish Funding Council have indicated that they would make an extension of the deadline to 31 January, which has also been offered to the Glasgow Colleges Regional Body who are preparing consolidated accounts for the first time in 2016-17.

Appendix 1 – Consideration of powers available and exercised

Power	Occurred during 2016-17 year	Indication of control
To fund the assigned colleges, the RSB can also impose conditions upon that funding (s9(2)).	Grant income from Funding Council for SLC has been routed through NCL, thus, NCL has funded SLC. This has been in place since August 2016 (i.e. full academic year).	✓
To monitor the colleges, being mindful of work undertaken by Scottish Ministers or the SFC. RSBs have the right to address meetings of the assigned college board (s10(23G))	Monitoring of SLC has taken place through attendance of SLC at TLB meetings and notification of SLC board decisions.	✓
Power of direction over assigned incorporated colleges but must consult with the college, trade unions and the students associations of the college (s10(23M))	No direction used during 2016-17 year that we are aware of.	N/A
Power to appoint independent board members of the assigned college board including the Chair of the Board. Assigned college boards must comprise between 13 and 18 members, the majority being independent (s6(3A))	There have been no changes to the SLC board during 2016-17 to date. Note from TLB meetings in 2016, new SLC board members were approved by TLB.	✓
Assigned colleges cannot appoint a Principal without approval of the RSB, this represents an effective power of veto	There has been no change in Principal during the 2016-17 year.	N/A
The RSB must put in place a financial memorandum with its assigned colleges that follows the requirements of the SPFM, except where agreed by the Scottish Ministers	Financial Memorandum (FM) is in place – agreed and operating since January 2016. Contents of FM make clear that TLB has the power to control SLC and sets out particular instances of this. There is an overriding clause that TLB’s interpretation of the FM ‘shall be final’.	✓

Note: The funding mechanism is as follows – NCL do not review or amend the SLC drawdown request prior to submission to the SFC, but are merely copied in. The NCL review takes place prior to receiving Regional funds from the SFC and prior to disbursement of funding to SLC. The FM sets out that TLB can ‘suspend the payment of any or all grants to SLC’. In addition, TLB can claw-back funding from SLC where conditionality of funding (adhering to the FM) has not been met. Therefore, in terms of the accounting standards, TLB has the power to control the funding received by SLC.

The Financial Memorandum sets out other instances which indicate that there is power to exercise control. Contingent commitments entered into by SLC must be approved by TLB, there are financial delegations in the FM that SLC cannot exceed without TLB authority.

(Paper prepared by VP:Resources – August 2017)