Circular **03/08**

For Action: Responses to Annex A are requested by 31 January 2004

Finance

Further Education Colleges: Accounting Policies and Return of Audited Financial Statements

Summary

The purpose of this circular is to provide guidance to colleges and financial statement auditors on the preparation of colleges' annual financial statements. The Learning and Skills Council (LSC) has consulted college financial statements auditors and sector representatives on this guidance. This guidance supplements that in the Statement of Recommended Practice: Accounting for Further and Higher Education Institutions, and consolidates all previous accounting policies guidance issued by either the Further Education Funding Council (FEFC) or the LSC. This circular is applicable for the year ending 31 July 2003, and highlights issues for future years. It is principally of interest to college finance directors and financial statements auditors. While fairly technical in its content, it will be relevant to principals in their capacity as accounting officers of FE colleges and audit committees.

Supplements A-F

(available on the LSC's website: http://www.lsc.gov.uk). Please refer to the contents page of this document for supplement titles.

Supersedes

Circulars 01/04 and 02/07.

April 2003

Learning+Skills Council

Contents

Paragraph numbers

Annexes:

Supplements (available on the LSC's website: http://www.lsc.gov.uk)

Further information

For further information, please contact the appropriate local Learning and Skills Council office, or write to:

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Provider Financial Support
The Learning and Skills Council
Cheylesmore House
Quinton Road
Coventry CV1 2WT.

Responses to this document

Responses to Annex A are requested by 31 January 2004.

Enquiries

Provider Financial Support

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Executive Summary

Date: April 2003

Subject: Further education colleges: accounting policies and return of audited financial statements for the year ending 31 July 2003

Intended recipients: Principals and chief executives of further education colleges; finance directors at further education colleges; financial statements auditors; executive directors of local Learning and Skills Councils (LSCs) and other key organisations

Status: For information and response

This circular is a response to the outcomes of the consultation in Circular 02/07: *Further Education Colleges: Accounting Policies and Return of Audited Financial Statements*, where 97% of the 103 respondents requested that the LSC should continue to issue detailed guidance on accounting policies. After consultation with the College Finance Directors Group, it was felt that it would be useful if the LSC could consolidate all previous guidance on accounting policies into one document.

Therefore, this circular consolidates all previous accounting policies guidance issued by either the FEFC or the LSC, and supplements the Statement of Recommended Practice: Accounting for Further and Higher Education Institutions.

The circular consists of:

a main circular – This details the changes in accounting policies guidance from Circular 02/07; and

b six supplements:

- Supplement A: Draft Statement of Recommended Practice: Accounting for Further and Higher Education: March 2003;
- Supplement B: Spreadsheet to Calculate Provisions for Enhanced Pensions;
- Supplement C: Revised Model Report and Financial Statements for Casterbridge College for the Year Ended 31 July 2003;
- Supplement D: Guidance to the Preparation of the Notes to the Financial Statements;
- Supplement E: Finance Record 2002/03 Proforma; and
- Supplement F: Notes and Guidance on the Finance Record 2002/03.

Date of response: The following should be submitted to the local LSC no later than 31 January 2004:

- audited financial statements of the college and its subsidiaries (where applicable) for the year ending 31 July 2003;
- a hardcopy of the finance record for the year ending 31 July 2003, which has been signed by the principal/chief executive of the college; and
- financial statements auditor's management letter, including the college's response.

The following should be submitted via the LSC web portal no later than 31 January 2004:

- college's finance record for the year ending 31 July 2003.

Further Education Colleges: Accounting Policies and Return of Audited Financial Statements

Section 1: Introduction

Introduction

1 The purpose of this circular is to provide guidance on the preparation of colleges' financial statements for the year ending 31 July 2003, and to identify issues that will require consideration for future years. This guidance supplements that to be found in the Statement of Recommended Practice: Accounting for Further and Higher Education Institutions, and consolidates all previous accounting policies guidance issued by either the Further Education Funding Council (FEFC) or the Learning and Skills Council (LSC).

2 In publishing this guidance, the LSC has consulted college financial statements auditors and sector representatives (please see paragraphs 31 to 36 below). The issue of this circular is welcomed by the chair of the College Finance Directors Group and representatives of the Association of Colleges (AoC).

3 The LSC's accounting policies for the sector are applicable to all colleges, regardless of their size, constitution or complexity. They are not currently applicable to external institutions, private training providers or other public bodies in receipt of LSC funding.

4 The accounting policies need not be applied to immaterial items. Guidance on the determination of what is material may be found in statement 2.401: *The Interpretation of 'Materiality' in Financial Reporting*, issued by the Council of the Institute of Chartered Accountants in England and Wales.

5 Following changes in the arrangements for the audit of the Individualised Learner Record (ILR), and the requirement to comply with risk management best practice (Turnbull Committee), the LSC has published Circular 03/04 *Interim Audit Code of Practice March 2003*. The duty of care owed by financial statements auditors is not yet resolved. The model engagement letter and model auditor's report which must be followed by the financial statements auditors will be issued separately.

Consultation on Accounting Policies and Return of Financial Statements

6 In Circular 02/07: *Further Education Colleges: Accounting Policies and Return of Financial Statements*, the LSC sought views from further education (FE) colleges in respect of:

- the production of an annual circular for FE colleges to follow in preparing their financial statements; and
- revised enhanced pension tables.

7 The LSC received 103 responses to the consultation, with:

- 97% of respondents agreeing that the LSC should continue to issue detailed guidance on accounting standards; and
- 72% of respondents agreeing that the instructions on using the enhanced pensions tables are easy to follow.

8 Therefore, the LSC has agreed to continue to produce detailed supporting guidance on reporting standards in the form of a circular and associated supplements. However, it will continue to work with colleges and sector representatives to simplify guidance where possible.

9 Following the consultation in Circular 02/07, the LSC was asked to produce a spreadsheet in order to enable calculation of the enhanced pension provision. The LSC has now designed one which can be downloaded from its website (http://www.lsc.gov.uk/documents_detail.cfm?categoryID=15&articleID=1239). Further guidance on the spreadsheet and enhanced pensions provisions is provided at paragraphs 85 to 94 of this circular.

10 The LSC also received a number of requests for guidance on specific accounting issues, in particular:

- FRS 17 *Retirement Benefits;*
- treatment of capital grants and reserves;
- depreciation policy in respect of land and buildings;
- revaluation policy on fixed assets; and
- treatment of joint ventures and partnerships and the application of standards to less formal arrangements.

11 As guidance on the above issues has been provided in previous accounting policies circulars published by either the LSC or FEFC, we felt that FE colleges might find it beneficial if the LSC were to produce a consolidated guide. This circular, therefore, provides this consolidated guidance.

Revisions to Accounting/Auditing Guidance

12 Circular 02/07 took account of Financial Reporting Standards (FRSs) up to FRS 19 *Deferred Tax* and various exposure drafts. This circular considers:

- FRS 17 *Retirement Benefits;*
- Financial Reporting Exposure Draft (FRED) 22 *Revision of FRS 3 Reporting Financial Performance;*
- FRED 23 *Hedge Accounting;*
- FRED 25 *Related Party Disclosures;*
- FRED 27 *Events after the Balance Sheet Date;*
- FRED 28 *Inventories; Construction and Service Contracts;*
- FRED 29 *Property, Plant and Equipment; Borrowing Costs;*
- FRED 30 *Financial Instruments: Disclosure and Presentation and Recognition and Measurement;*
- international accounting standards;
- clarification on the rules governing capital funding from main allocation;
- commutation of loan support;
- exceptional support funding;
- disposal proceeds held for reinvestment;
- enhanced pensions provisions;
- corporate governance and risk management;
- Derek Higgs' review on the role and effectiveness of non-executive directors;
- Sir Robert Smith's report on audit committees;
- going concern and impairment reviews;
- accounting for recovery of funds (tolerance account);
- accounting for college-administered funds, including University for Industry (UfI) funding;
- payment performance;

- audit opinion 2002/03;
- revised model report and financial statements for Casterbridge College;
- guidance on preparing the notes to the financial statements; and
- finance record 2002/3.

13 The following FREDs and Urgent Issues Task Force (UITF) abstracts are not addressed on the grounds of their limited applicability to the sector:

- UITF Abstract 34 *Pre-contract Costs;*
- UITF Abstract 35: *Death in Service and Incapacity Benefits;*
- FRED 24 *The Effects of Changes in Foreign Exchange Rates; Financial Reporting in Hyperinflationary Economies;* and
- FRED 26 *Earnings per Share*.

14 If colleges consider the guidance referred to in paragraph 13 may be relevant to their particular circumstances, then they may discuss accounting treatments with their financial statement auditors.

Return of Audited Financial Statements for 2002/03

15 The financial relationship between the LSC and colleges is set out in its financial memorandum, as detailed in FEFC Circular 99/48 *Financial Memorandum*. The financial memorandum sets out the terms and conditions on which payments of grant will be made from the LSC to institutions. A specific responsibility of the college is to provide the LSC with audited financial statements for the financial year no later than five months after the year-end.

16 To take account of the new arrangements for auditing the Individualised Learner Record (ILR), the LSC temporarily amended this requirement in Circular 02/07, so that audited financial statements for the year ending 31 July 2002 were to be submitted no later than six months after the year-end.

17 Audit firms have raised the issue that they can only sign off the financial statements of a college following receipt of the institution's audited interim ILR statements. Experience during the 2001/02 audit process suggests that a proportion of audited interim ILR statements are likely to be received towards the end of December. In this context, the LSC believes that it would be unreasonable to reinstate the requirement for colleges' audited financial statements to be submitted by the end of December. Therefore, for 2002/03 colleges should continue to submit their financial statements to the LSC no later than six months after the year-end. The LSC will review this change for future years as part of the consultation process in the revision of the financial memorandum and in its implementation of *Success for All*.

18 Each college should send an original signed copy of its audited financial statements for 2002/03, together with its signed finance record and, where applicable, copies of the audited financial statements of its subsidiaries, to the relevant local LSC to arrive on or before 31 January 2004.

19 A cover sheet for the returns is attached at Annex A to this circular.

Audit Reports and Management Letters

20 Colleges should send a copy of the final version of the financial statements auditor's management letter, including the college response, to the head of the Provider Financial Assurance function at the relevant local LSC by 31 January 2004.

21 Financial statement auditors are reminded that where they are unable to express an unqualified opinion on the college's financial statements, they should immediately communicate this to the principal, the chair of the corporation and the chair of the audit committee. They should also inform the head of Provider Financial Assurance of the relevant local LSC.

Guidance

22 Colleges with queries about how to apply the LSC's guidance on accounting policies to the particular circumstances of their own college may wish to consult their financial statement auditors or the local LSC. Colleges wishing to make general points about the development of accounting guidance should contact Peter Darwen in the Provider Financial Support team at the LSC national office.

Approval of reports and financial statements

23 The reports and financial statements must be approved by the corporation. They should be signed and dated as follows:

- the members' report should be signed and dated by the chair of governors on behalf of the corporation;
- the balance sheet should be signed and dated by the principal and one other member of the corporation, usually the chair of governors; the director of finance is not required to sign it;
- the statement of the responsibilities of the corporation members should be signed and dated by the chair of governors;
- the corporate governance statement should be signed and dated by the chair of governors; and
- the internal financial controls statement should be signed and dated by the principal.

24 The above items should normally be signed on the same date. They must also be signed on, or very shortly before, the date on which the college's financial statements auditor signs and dates their audit report.

Section 2: The Development of Accounting Policies for the FE Sector

Statement of Recommended Practice: Accounting for Further and Higher Education Institutions

25 For all accounting periods commencing on or after 1 August 1999, all FE institutions have had to prepare their financial statements in accordance with the requirements of the Statement of Recommended Practice: Accounting for Further and Higher Education Institutions (F&HE SORP). In December 2002 the Higher Education/Further Education Board for the SORP (HE/FE SORP Board) issued a revised F&HE SORP for consultation with the sector. Although it is likely that the revised F&HE SORP will not be published until the end of May 2003, the LSC wishes to reiterate that the revised F&HE SORP will be the primary document to be followed by colleges and is effective for all accounting periods commencing on or after 1 August 2002. A copy of the draft F&HE SORP is provided at Supplement A to this circular.

26 The F&HE SORP is intended to apply to all colleges, including voluntary-aided sixth form colleges, voluntary-controlled sixth form colleges and specialist-designated institutions. Where these bodies are constituted as companies limited by guarantee, they should follow the F&HE SORP with any additional disclosures required to comply with the *Companies Act 1985*.

27 In the small number of cases where the institution is a separate registered charity and less than 50% of its income is from the LSC, it is likely that application of the charities SORP (*Accounting and Reporting by Charities: Statement of Recommended Practice* (Revised 2000)) will give a better representation of the institution's activities than the F&HE SORP. Where additional information is required under the F&HE SORP, that information should be given by way of note. Where a college considers that it may fall within this group, then it should discuss the position with its financial statement auditors and the local LSC.

Higher Education/Further Education Board for the SORP

28 The sponsoring body of the F&HE SORP is the HE/FE SORP Board. The HE/FE SORP Board is composed of senior representatives of the HE/FE funding councils of the UK, which are currently:

- Higher Education Funding Council for England (HEFCE);
- Education and Learning Wales (ELWa);
- Scottish Higher Education Funding Council (SHEFC);
- Department for Education and Learning Northern Ireland (DELNI); and
- the LSC.

together with the representative bodies (Universities UK, Standing Conference of Principals and the Association of Colleges), the accounting profession and the chair of the HE/FE SORP Board's Technical Advisory Committee.

29 While the funding councils and the institutions each retain their sovereignty, they do so in the expectation of full compliance with accounting standards and the advice of the HE/FE SORP Board. In this context, therefore, the HE/FE SORP Board will:

- approve, update, amend and issue the HE/FE SORP to reflect current accounting standards in a timely manner;
- respond to requests from the Accounting Standards Board (ASB) in respect of all matters relating to accounting standards;
- advise as to whether financial directives issued by the funding councils conform to the SORP

(although the funding councils are at liberty to require information and disclosures in excess of the SORP should they deem it necessary);

- consider any matters relating to accounting standards and financial reporting;
- issue guidance to institutions on the probable impact of exposure drafts;
- annually review institutions' compliance with the SORP;
- approve the composition and terms of reference of the Technical Advisory Committee; and
- report on its activities annually to its member bodies, and annually or as required by the ASB.

30 The ASB wishes to see the continuance of a high-quality SORP for the further and higher education sectors. To meet this objective, the LSC has agreed the following with the HE/FE SORP Board:

- the HE/FE SORP Board will issue accounts direction on any necessary amendments to the F&HE SORP. This accounts direction is published by the LSC through its Sector Accounting Policies circular. This ensures that all institutions in the further and higher education sectors prepare financial statements on a comparable and consistent basis;
- the issue of additional disclosure requirements, such as corporate governance statements, will be made by individual funding councils.

Sector Accounting Policies Group

31 The LSC wished to introduce both a proactive and interactive approach to the development of guidance on accounting policies to the sector. In January 2002 the Sector Accounting Policies Group was formed.

32 The membership of this group includes representatives from the following:

- college financial statements auditors;
- AoC;
- the College Finance Directors' Group;
- Department for Education and Skills (DfES);
- HEFCE;
- ELWa; and
- Scottish funding councils.

33 The Sector Accounting Policies Group's aims are to encourage colleges to consider new guidance on accounting policies as early as possible and provide a forum for the bringing together of any issues and/or problems over their implementation. The LSC wishes to inform the sector of the decisions of the Sector Accounting Policies Group on a timely basis. The group meets every two to three months with the publication of the minutes of the meetings and relevant papers through the LSC's website. For further information on published papers, please visit: http://www.lsc.gov.uk/documents_list.cfm?categoryId=42.

34 Since the publication of Circular 02/07, the following papers have been published:

- Clarification on FRS17 *Retirement Benefits;*
- *College Combinations;*
- *Enhanced Pensions Provisions Clarification;*
- *Risk Management Clarification;*
- *Disposal of Fixed Assets;*
- *Clarification on the Rules Regarding Spending Part of the College's Main Allocation for Capital Purposes;*
- draft F&HE SORP;
- *Revised Standard Unqualified Audit Opinion for Colleges' Financial Statements for the Year Ended 31 July 2002;*

- FREDs 23 to 30; and
- UITFs 34 and 35.

35 For ease of reference the above papers have been summarised in this circular.

36 It is expected that the Sector Accounting Policies Group will give feedback to the HE/FE SORP Board on issues regarding the implementation of accounting directives from the ASB.

Section 3: Update to the F&HE SORP

37 The accounting guidance on the following FRSs and FREDs has been issued after consultation with the HE/FE SORP Board.

Financial Reporting Standards

FRS 17 *Retirement Benefits*

38 Under the transitional arrangements of the FRS there is no requirement to fully implement the accounting standard until the year ended 31 July 2005. The LSC recommends that colleges do ***not*** adopt the Standard early and fully implement FRS 17 in the current year, in light of ongoing discussions and national debate in respect of this accounting standard. For their financial statements for the year ended 31 July 2003, colleges should ensure that they disclose, in a note to the accounts, the entries that would be made in the financial statements if the FRS was fully implemented. These are the same disclosure notes as those required for colleges' financial statements for the year ended 31 July 2002. It is expected that colleges should have the following disclosure notes in their financial statements for the year ended 31 July 2003:

- amount of net pension asset/(liability);
- analysis of the amount charged to the income and expenditure account;
- analysis of net return on pension scheme;
- amount recognised in the Statement of Total Recognised Gains and Losses (STRGL);
- movement in surplus/(deficit) in year; and
- history of experience gains and losses (from 2006, five years must be shown).

39 In addition, a number of college financial statements include Statement of Standard Accounting Practice (SSAP) 24 *Pension Costs* provisions in respect of underfunding of the Local Government Pension Scheme (LGPS). In producing the FRS 17 disclosure note, such provisions will need to be factored into the disclosure. (In particular, such provisions will need to be added back to the reported college net assets *per* the balance sheet at 31 July 2003, in order to give a revised net asset figure for FRS 17 disclosure purposes.)

FRED 22 revision of FRS 3 *Reporting Financial Performance*

40 In December 2000 the ASB issued FRED 22, seeking comments on the proposed revision of FRS 3 *Reporting Financial Performance*. Although the closing date for responses was 30 April 2001 no financial reporting standard has been issued. The ASB and the International Accounting Standards Board (IASB) are working in partnership to develop a standard that would require a new statement to replace the existing income and expenditure account and the STRGL. This builds on FRED 22.

41 For the time being, colleges should be aware that the ASB and IASB are considering fundamental changes to the format of the income and expenditure account, STRGL and note of historical gains and losses. However, it is not proposed that colleges seek to adopt the proposals in the FRED. It is anticipated that a revision to the F&HE SORP will be required to incorporate the proposals of any revised FRS.

42 The main proposals of the FRED are as follows:

a the income and expenditure account and the STRGL are combined to form a single statement of financial performance;

b the performance statement shows all gains and losses recognised during the period that relate to that period;

c the statement is divided into three sections:

- operating;
- financial and treasury;
- other gains and losses.

d recycling of gains and losses between different sections of the performance statement is not permitted;

e a memorandum note of the historical cost and losses for the period may be presented if it would help users to understand the entity's performance. This would be required for colleges to show the difference between historical cost depreciation charge (nil) for inherited assets and the actual depreciation charge, calculated on the revalued amount, included in the operating section; and

f a table of exceptional items reported over the last five years will be required.

FRED 23 *Hedge Accounting*

43 A hedge is a contract (the hedge instrument) that individually, or with other contracts, has a value or cash flow that is expected, wholly or partly, to move inversely with changes in the value of, or cash flows arising from, another contract or other exposure (the hedged item).

44 The LSC believes that a minority of colleges may have hedging arrangements in place for any capital borrowings or investments on the money market. Where this is the case, colleges should review the proposed accounting standard for the potential impact that it may have on their financial statements.

45 The ASB considers it highly likely that by 2005, listed companies will follow International Accounting Standard (IAS) 39 *Financial Instruments: Recognition and Measurement*. As a result, the ASB has decided to publish a FRED on hedge accounting.

46 A financial instrument would only qualify for hedge accounting if, and only if, it is held as a hedging instrument in a hedge that meets both:

- the hedging relationship criteria (including the pre-designation criterion) set out in paragraph 47 below; and
- the hedge effectiveness criteria set out in paragraph 48 below.

47 The hedging relationship criteria that need to be met are as follows.

- At the inception of the hedge, there is a formal documentation of the hedge relationship and the college's risk management objective and strategy for undertaking the hedge.
- The effectiveness of the hedge can be reliably measured.
- If a forecast transaction is being hedged, it must be highly probable and must present an exposure to variations in cash flows that could ultimately affect the reported operating surplus or deficit.

48 The hedge effectiveness criteria that need to be met are as follows.

- The hedge was expected at the outset to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged item, consistent with the originally-documented risk management strategy for that particular hedging relationship.
- The hedge has been assessed on an ongoing basis since its commencement, and actually determined to have been highly effective throughout the reporting period.

49 The hedge would be regarded as highly effective if the actual results are within a range of 80% to 125% of the hedging instrument.

50 The accounting treatment is that any ineffective portion of the loss or gain on the hedging instrument that would have been recognised had hedge accounting not been adopted, should be immediately recognised in the income and expenditure account.

FRED 25 *Related Party Disclosures*

51 FRED 25 proposes to replace FRS 8 *Related Party Transactions* with the

international standard IAS 24. However, the FRED proposes retaining, for the UK, the requirement that an entity's controlling party should be named. The main changes to FRS 8 are as follows:

- the names of transacting related parties should not be disclosed; and
- the proposed exemption for subsidiaries' disclosure extends only to wholly-owned subsidiaries.

FRED 27 *Events after the Balance Sheet Date*

52 The FRED proposes the replacement of SSAP 17 *Accounting for Post Balance Sheet Events* with IAS 10 *Events after the Balance Sheet Date*. The main change to SSAP 17 is a stricter definition of 'adjusting events'.

FRED 28 *Inventories; Construction and Service Contracts*

53 The FRED proposes to replace SSAP 9 *Stocks and Long-term Contracts* with two international standards; one based on the revised IAS 2 *Inventories*, and another based on IAS 11 *Construction Contracts*, with limited text from IAS 18 *Revenue*. There are no major differences between the accounting requirements of FRED 28 and those in SSAP 9.

FRED 29 *Property, Plant and Equipment; Borrowing Costs*

54 The FRED proposes the replacement of FRS 15 *Tangible Fixed Assets* with a combination of IAS 16 *Property, Plant and Equipment* and IAS 23 *Borrowing Costs*. FRED 29 and FRS 15 have much in common in terms of principles for initial measurement and depreciation of fixed assets. Both approaches allow the same choice between depreciation and revaluation, but IAS 16 requires revalued assets to be accounted for under a 'fair value' approach rather than a 'value to the business'.

FRED 30 *Financial Instruments: Disclosure and Presentation and Recognition and Measurement*

55 FRED 30 proposes the implementation in the UK in 2004 of two further UK standards based on the following International Financial Reporting Standards (IFRSs):

- IAS 32 *Financial Instruments: Disclosure and Presentation;* and
- IAS 39 *Financial Instruments: Recognition and Measurement*.

56 In July 2001 the IASB carried out an IAS 39 amendments project to try to simplify implementation of the standard. The consequent amendments have been made to IAS 32. In June 2002, the IASB issued the result of its amendments project in the form of exposure drafts of revised versions of the two standards.

57 The FRED also contains proposals on the withdrawal of FRS 4 *Capital Instruments* and FRS 13 *Derivatives and Other Financial Instruments: Disclosures* and other related UITF abstracts.

IAS 32 *Financial Instruments: Disclosure and Presentation*

Disclosure

58 UK entities are currently required to produce a range of narrative and numerical risk disclosures about their financial instruments. FRED 30 proposes that these requirements are replaced by a UK standard based on IAS 32 disclosure requirements which broadly follow the existing requirements, but are less detailed. This will allow entities greater flexibility as to the form of the disclosures that they provide.

Presentation

59 The categories into which capital instruments will be classified will change from liabilities and shareholders' funds to liabilities and equities. Instruments, including shares, will be classified in accordance with the substance of the contractual arrangements involved. Only income payments on instruments classified as equity will be treated as dividends. Income payments on all other instruments will be treated as interest expense. For example, this will result in most preference shares being classified as liabilities, and most preference share dividends being classified as interest expense.

60 The standard also requires that the debt and equity elements of convertible debt and similar instruments are dealt with and presented separately in the accounts. At present, FRS 4 requires convertible debt to be classified wholly as a liability.

61 There is one further change to the existing requirements on the presentation of financial instruments. FRS 5 *Reporting the Substance of Transactions* contains provisions specifying when balance sheet debits and credits should be shown together as a single asset or liability. The standard proposes that these provisions are replaced by offset provisions. This will allow balance sheet debit and credits to be offset more often than they are at present.

IAS 39 *Financial Instruments: Recognition and Measurement*

Fair value measurement

62 The ASB understands that by 1 January 2004, the *Companies Act 1985* will be amended in order to permit companies to adopt fair value accounting rules. These rules will allow companies to measure certain financial assets and financial liabilities at fair value, and to recognise changes in those fair values immediately in the profit and loss account. FRED 30 sets out the way in which fair value accounting rules should be applied, if an entity chooses to adopt them.

63 In particular, such companies will be required to:

a measure at fair value all derivatives, all financial assets and liabilities that are held for trading, and all financial assets 'available for sale';

b measure at a cost-based amount all financial assets (other than derivatives) that are 'held to maturity' or 'loans or receivables originated by the reporting entity', and all financial liabilities that are neither derivatives nor being held for trading; except that an entity can elect to measure any of these assets at fair value and recognise changes in those fair values immediately in the profit and loss account (so long as an election is made on initial recognition); and

c recognise in the profit and loss account immediately all changes in the fair value of instruments, except that changes in the fair value of 'available for sale' financial assets are required to be recognised immediately in the STRGL.

Hedging

64 IAS 39 includes a number of requirements on the use of hedge accounting in addition to those incorporated in FRED 23 *Financial Instruments: Hedge Accounting*. This will further limit the availability of hedge accounting to account for financial instruments. The standard prescribes exactly how hedge accounting should be done, should an entity choose to do it. From 2005, the expectation is that listed entities will be required to adopt the hedge accounting requirements of IAS 39 in their consolidated accounts. Unlisted entities and individual financial statements of listed companies will only be required to comply with hedge accounting rules if the fair value accounting rules are adopted in the financial statements involved.

Recycling

65 IAS 39 currently requires certain gains and losses to be recognised initially outside the profit and loss account, and then at a later date, recognised in the profit and loss account (that is, recycling). The ASB does not support the use of recycling and hopes that the practice will be prohibited internationally.

Recognition and de-recognition of financial instruments

66 The IASB is proposing to replace the existing material in IAS 39 on the recognition and de-recognition of financial instruments with material based on a new approach to the subject. The new basis of accounting, called the 'Continuing Involvement Approach', involves a different philosophy from that underlying FRS 5 *Reporting the Substance of Transactions*.

Implementation of FRED 30

67 FRED 30 also proposes how IAS 32 and IAS 39 should be implemented in the UK prior to 2005. It proposes in particular that UK standards based on IAS 32 and IAS 39 should be implemented for all types of entities with effect from 1 January 2004, except that:

- amendments would be made to the requirements of IAS 39 in order to eliminate the need to recycle certain gains and losses;
- the disclosure requirements in the new standard would apply only to listed entities and unlisted banks;
- the requirements based on the measurement and hedge accounting requirements of IAS 39 would be mandatory from that date only for entities listed or unlisted that chose to adopt fair value accounting; and
- the requirements of IAS 39 on recognition and de-recognition would not be implemented in the UK at the present time.

68 From 2005 all listed entities will have to comply with IASs 32 and 39 in full. The proposal in the FRED is that the position described above would continue to apply for unlisted entities.

Action by Colleges

69 Although FREDs 22 to 30 do not apply to colleges' financial statements for the year ending 31 July 2003, colleges need to be aware of the FREDs and should consider their impact on college financial statements. If in doubt, colleges should contact their financial statements auditors.

International Accounting Standards

70 For accounting periods beginning on or after 1 January 2005, the UK's listed companies must use European Union (EU) adopted international accounting standards in their group financial statements. Although it is not known at this stage whether FE colleges will have to follow the same rules, it would appear to be inevitable as the ASB is reviewing all of its existing accounting standards to ensure compliance. Colleges need not take any further action for now, but should consider the potential impact on their financial statements.

Section 4: Other Guidance

Clarification on the Rules Governing Capital Funding from Main Allocation

71 Up to 31 July 2001, colleges were required to spend at least 2% of their funding allocation for capital purposes. This element of the funding would be matched against the related purchase. Thus, if the grant was spent on an asset which was capitalised, the grant would be treated as a deferred capital grant and be released to the income and expenditure account over the life of the relevant asset. If the grant was spent for capital purposes but not on an item that would normally be capitalised (for example, on an item costing less than the institution's capitalisation limit or certain minor works), it would be released to the income and expenditure (I&E) account from the deferred capital grant immediately.

Accounting Policy Post-31 July 2001

72 With effect from 1 August 2001, the LSC no longer requires institutions to apply a percentage of their main funding allocation for capital purposes. Therefore, the full funding allocation for 2001/02 onwards should be credited to the income and expenditure account. No amount should be accounted for as a deferred capital grant as the grant is no longer given for capital purposes. Colleges are free to determine their own capital budgeting processes, and will need to budget for future depreciation charges when deciding whether to make capital purchases.

Commutation of LSC Loan Support

73 Prior to the current capital grant arrangements operated by the LSC, colleges were offered support for capital projects through a system based on a notional loan. The first year of grant support was calculated as the repayment of principal and interest of a 15-year loan for an agreed percentage of the project value. Subsequent years' grant support was calculated as 90% of the previous year; therefore, grant support in year 2 was 90% of year 1, and in year 3 it was 81% of year 1.

74 In March 2003, the LSC offered each college that received capital support a single lump sum, payable in the March payment run, to replace the future capital grant support payments calculated on the notional loan basis. For those colleges who accepted the LSC's offer, the treatment of the computation should be the same as if it were a capital grant. Accordingly, the payment should be credited to deferred capital grants and released to the income and expenditure account over the remaining life of the related asset.

Exceptional Support Funding

75 Some colleges may receive exceptional support funding from the LSC to assist them in implementing either a college combination or the delivery of a strategic recovery plan. This funding is provided as a grant outside the mechanisms of the funding methodology. As with any grant, the accounting treatment should be determined in light of any terms and conditions agreed between the LSC and the college.

76 In most cases (unless terms and conditions indicate otherwise), exceptional support funding should be recognised as income in the college financial year in which it is received and disclosed separately in note 2 *Funding Council Grants* to the financial statements. If the amount is material to a college's financial statements then it should be shown separately instead on the face of the income and expenditure account in accordance with FRS 3 *Reporting Financial Performance*. Colleges will need to discuss the disclosure of such grants with their financial statements auditors.

Disposal Proceeds Held for Reinvestment

77 The financial memorandum (FEFC Circular 99/48) states that:

- where the college is proposing to dispose of ______ land and buildings which have been acquired by exchequer funds* the LSC may require the college to surrender some or all of the proceeds; and
- the LSC would normally expect colleges to apply the proceeds of asset sales to investment in fixed assets.

(*Exchequer funds include grants from the LSC (including Hunter funds) and other government bodies. They do not include funds from local education authorities. Inherited assets are regarded therefore as partly exchequer-funded assets, due to the investment of Hunter and other LSC funds in them following incorporation.)

78 In practice, this means that colleges need the LSC's consent to retain and apply disposal proceeds. These consents are usually given as part of the overall consent to a college capital proposal.

79 In the past, colleges were required to earmark disposal proceeds in a restricted or designated reserve, and to hold the cash funds in a separate bank account depending on the circumstances (FEFC Circular 00/22 *Sector Accounting Policies*). Circular 00/22 also required colleges to provide a note in their accounts in order to identify any material sums which were being held for reinvestment, for example, as an extension to the note on changes in net funds.

80 Following the introduction of the F&HE SORP, the FEFC moved away from the concept of restricted reserves in order to bring the FE sector in line with the HE sector. On 30 October 2000 the FEFC's director of finance wrote a letter to principals and finance directors of colleges titled *Sector Accounting Policies: Clarification*. This letter indicated that:

> *The Council would now only expect to see a restricted reserve in extremely limited circumstances, for example, in respect of a prize fund.*

81 The LSC has become aware that colleges do not generally appear to be disclosing the material cash sums that they hold at the balance sheet date for reinvestment in fixed assets (or exceptionally for another purpose agreed by the LSC). In fairness, this requirement has not been carried forward into the current accounting policies guidance issued to the sector (Circulars 01/04 and 02/07).

82 The LSC would not wish to reintroduce any requirements to show restricted reserves. However, we consider that any material sum held for reinvestment should be brought to the attention to the reader of a college's accounts, in order to aid understanding of a college's underlying financial position.

Accounting Policy for Financial Statements on or after 1 August 2002

83 Colleges must disclose, by way of a note, the amount of disposal proceeds that they hold and for what purpose (almost without exception, this will be for reinvestment in land and buildings). The note should form an extension to the existing note on changes in net funds, and might be worded as follows:

> *£1.5 million of the funds in current asset investments is derived from the sale of the Westwick site and is held (in a separate ring-fenced bank account*) for reinvestment in the main site.*

(*where required/applicable)

84 If the planned reinvestment of proceeds is part of a complex funding package including, for example, loan finance, future disposal proceeds, etc, it is recommended that the above disclosure is expanded as necessary to ensure that users of the financial statements have a clear view of the underlying funds of the institution.

Enhanced Pension Provisions

85 In Supplement B of Circular 02/07 *Revised Enhanced Pensions Tables*, the LSC provided a revised set of enhanced pensions tables which should have been used in colleges' annual financial statements for the year ended 31 July 2002. Supplement B included:

- full instructions on use of the tables in calculation of the provisions;
- the charge to the income and expenditure account in the year of early retirement;
- the interest charge in current and subsequent years; and
- a summary of the conversion issues from SSAP24 to allow provisions to be calculated on the net interest basis method as required by FRS17.

86 In May 2002, the LSC was approached by a number of colleges to design a spreadsheet which would make the enhanced pension provision calculation simpler. Therefore, a spreadsheet was put on the LSC's website, accompanied by a worked example (please see http://www.lsc.gov.uk/documents_detail.cfm?categoryID=15&articleID=1239).

87 This spreadsheet, with the worked example, has been revised to make it easier for colleges to calculate the provision. It is provided in Supplement B to this circular.

88 The following changes have been made to the spreadsheet:

a the notes and instructions for use have now been incorporated into the spreadsheet;

b the net interest rate (NIR) is now automatically restated to the nearest 0.5%;

c the factor from the NIR table is automatically picked up from the relevant table; and

d additional rows can now be displayed or hidden in the provision sheet by clicking on the plus (+) or minus (-) sign at the bottom of the page.

89 It is necessary for the user to ensure that the Excel Add-In programs have been activated in order for certain new functions within the calculations to work (see note 1 in the spreadsheet).

90 The following yield indices from the UK Bonds – FTSE Actuaries Government Securities as at 31 July (for both the current year and the previous year), will be published in the first week of August 2003 within the Sector Accounting Policies Group heading at the LSC's website (http://www.lsc.gov.uk/documents_list.cfm?categoryId=42):

- fixed interest 10-year yield indices; and
- index-linked over five years (5% inflation yield).

91 As noted in paragraph 38, the LSC recommends that colleges do not fully implement FRS 17 in the current year. As a result, enhanced pension provisions should continue to be updated by the college and accounted for within the financial statements on the existing SSAP 24 basis.

92 Under FRS 17, further information will need to be included within the FRS 17 disclosure note detailing the impact on reported results of treating the enhanced pension provisions on a SSAP 24 basis rather than a FRS 17 basis. These disclosures are in the same format as those disclosed for the LGPS set out above. Colleges should consider combining the disclosures into one note which sets out, in overall terms, the differences between accounting for pension costs on a SSAP 24 basis versus FRS 17 basis.

93 For clarity, the revisions to the enhanced pension provisions apply to all enhancements (Teachers' Pension Scheme (TPS) or LGPS), and compiling information for the FRS 17 disclosure note will need to be carried out by the college. Where provisions are material, the college may wish to consider obtaining advice from their financial statement auditors or an actuary.

94 *Where a college has a provision for enhanced pensions, the use of the tables in this circular are mandatory.*

Corporate Governance and Risk Management

95 The Turnbull Committee published its guidance on internal control in September 1999. Although this guidance was written for companies, it has been adapted for the further education sector as set out in the following paragraphs.

96 The Turnbull Committee has sought to reflect some of the best practices in designing and operating systems of internal control, and in embedding a risk-based approach. The aim is to move corporate governance towards integration with management processes. More corporation involvement is now implied, with the process being explicitly risk-based and subject to both review and assessment by the corporation.

97 In outlining broad principles, the guidance suggests that the corporation should use its judgement to assess whether or not it has complied. The expectation is that the corporation will implement the spirit of the guidance in a way that helps it to achieve its own institutional objectives, and that will build on practices already in place.

98 It is important to understand that the Turnbull guidance is broader than that of the previous Cadbury guidance in that the review must cover business, operational and compliance as well as financial control.

99 Colleges need to ensure that they become fully compliant with Turnbull before 31 July 2003. Non-compliance by that date is likely to result in qualification of their financial statements, if the LSC makes full compliance with Turnbull a requirement in its revised financial memorandum with colleges. Colleges that comply during the financial year ending 31 July 2003 should avoid qualification of their financial statements.

Financial statements disclosure

100 Annex B sets out illustrative corporate governance disclosures to be included within financial statements for the year ended 31 July 2003. For 2003, colleges are required to include the following statements:

- corporate governance statement setting out the institution's position in respect of complying with the Turnbull Combined Code; and
- principal's statement, as accounting officer, on the system of internal financial control at the college (as in prior years).

101 Two corporate governance statements are included: one is to be used where the college has fully complied with Turnbull during the year ended 31 July 2003; the other for partial compliance is to be used where the college intends to fully comply from 1 August 2003.

102 Changes to the wording of the examples should be kept to a minimum. However, the key areas outlined in Annex B are the minimum disclosures expected and the corporation is encouraged to describe any additional features of their policies in complying with Turnbull recommendations.

Derek Higgs' Review on the Role and Effectiveness of Non-executive Directors

103 In January 2003, the Department of Trade and Industry (DTI) published Derek Higgs' review on the role and effectiveness of non-executive directors. The review seeks to advance and reflect best practice through revisions to Turnbull's Combined Code of Practice. While the recommendations are for listed companies, some of these principles are applicable to FE colleges. The review recommends that the changes to the Combined Code be implemented for accounting periods commencing on or after 1 July 2003. As the LSC anticipates that the Treasury will endorse this report, it is likely that many of the recommendations will have to be implemented by public sector bodies.

The LSC will issue further guidance to colleges on the implementation of the Higgs proposals, once advice has been received from the Treasury. A copy of the report is available at the DTI website (http://www.dti.gov.uk/cld/non_exec_review).

Sir Robert Smith's Report on Audit Committees

104 In January 2003 the Financial Reporting Council published Sir Robert Smith's report on audit committees. The LSC's requirements in respect of audit committees are set out in Circular 03/04. As the audit code of practice is kept under review, any explanatory guidance on the principles in the report will be developed in the future. A copy of the report is available at http://www.frc.org.uk/publications.

Going Concern and Impairment Reviews

105 Where colleges and/or their financial statement auditors have concerns about the appropriateness of the value of assets, or the use of the going concern basis for the preparation of accounts, they should contact the LSC's director of finance and the executive director at the relevant local LSC.

Arrangements for the Recovery of Funding for Underachievement against Funding Agreement

106 The arrangements for the recovery of funding for underachievement against funding agreements will be published later in 2003. For the time being, colleges should plan that any underachievement will be recovered by the LSC.

Accounting for College-administered Funds, Including University for Industry Funding

107 Over recent years, colleges have increasingly acted as conduits for funding which has passed to other organisations, for example, University for Industry (UfI) funding. The LSC has previously indicated that such funding should be accounted for in accordance with the principles of FRS 9 for joint ventures and partnerships. Following queries from a number of audit firms and sector representatives, the LSC has sought clarification on the policy to be adopted for its funds from the DfES. The DfES has confirmed that for LSC funding, it should be accounted 'net' where LSC funds are passed to other FE sector bodies (who in turn will recognise the income in their financial statements). This will ensure that the financial statements for the sector as a whole do not double count LSC funding. Where LSC funding passes to organisations outside the sector, the college should account for the income and expenditure gross to ensure that all funding is captured within the sector's accounts. For example, where a college is a recipient for UfI, funding passed to other colleges should be excluded from the recipient college's income and expenditure account. Funding which is passed to other UfI partners (for example, under franchising arrangements) should be included within the college's income and expenditure.

108 Where institutions have adopted a different approach in the previous year's financial statements, and the revision would have a material effect on comparatives, they should be restated and disclosure made within the notes to the financial statements in a similar way to the restatement of access funds in earlier years.

Payment Performance

109 The *Late Payment of Commercial Debts (Interest) Act 1998* provides small businesses with a statutory right to claim interest on late payment of commercial debts. In November 1998, small firms were first given the right to charge interest to large companies and public sector organisations. The *Late Payment of Commercial Debts (Interest) Act 1998* was extended to cover large companies in November 2002.

110 A late payment is defined as being late when it is received after the expiry of the contractually-agreed credit period; or the credit period in accordance with trade custom and practice or in the course of dealing between parties; or the default credit period defined in the legislation. Where no credit period is defined in a contract, or no contract exists, the Act sets a default credit period of 30 days from the delivery of the invoice for payment or of the goods and services, whichever is the later.

111 The legislation seeks to recompense the creditor for the cost of the delay of payment. It provides a power for the secretary of state to set the rate of statutory interest. The rate of interest is currently set at 8% above the 'official dealing' rate. This rate is published by the Bank of England's Monetary Policy Committee, and is a rate at which the smallest and most vulnerable businesses are generally able to borrow from banks. It will be possible to amend the interest rate.

112 The Treasury has stated that the target for payment to suppliers within 30 days is 95%.

113 The members' report of the financial statements has been amended to include a statement on the payment performance of the college as stated below:

Payment Performance

The Late Payment of Commercial Debts (Interest) Act 1998, which came into force on 1 November 1998, requires colleges, in the absence of agreement to the contrary, to make payments to suppliers within 30 days of either the provision of goods or services or the date on which the invoice was received. The target set by the Treasury for payment to suppliers within 30 days is 95%. During the accounting period 1 August 2002 to 31 July 2003, the college paid (XX)% of its invoices within 30 days. The college incurred no interest charges in respect of late payment for this period.

114 The above statement should be amended to reflect the college's circumstances. The provision of a statement is optional for colleges' 2002/03 financial statements, but *mandatory for accounting periods commencing on or after 1 August 2003*.

Audit Opinion 2002/03

115 A revised audit opinion for 2002/03 has not been provided with this circular as it will be issued with the Audit Code of Practice later in the year. However, it is anticipated that a supplementary standard opinion will be required in colleges' financial statements for the year ended 31 July 2003, which will be either where:

a the institution is fully compliant with the requirements of Turnbull for the year ended 31 July 2003. This will require additional disclosure within the audit opinion and set out clearly the scope of the auditor's work in this area; or

b the institution is partially compliant with the requirement of Turnbull for the year ended 31 July 2003.

Revised Model Report and Financial Statements for Casterbridge College

116 In Circular 02/07 the LSC provided model financial statements for Casterbridge College for the year ended 31 July 2002. These model statements have been updated to reflect new accounting reporting requirements. A revised model annual report for Casterbridge College for the year ending 31 July 2003 has been provided in Supplement C of this circular. The changes to the financial statements from those provided in Circular 02/07 have been highlighted in the model. The model report is available for download in the following formats:

- members' report, auditor's report and accounting policies disclosure note in Word 97/Word 2000 on Windows '95; and
- income and expenditure account, STRGL, balance sheet, cash flow statement and disclosure notes in Excel 97/Excel 2000 on Windows '95.

117 Previous LSC guidance set out specific disclosure requirements relating to colleges only. These are incorporated within the model Casterbridge College report and are summarised below.

- In the members' report, colleges must include the following:
  - disability statement;
  - note on expenditure against the planned maintenance plan;
  - note on payment performance;
  - list of the governors who served on the board during the year; and
  - statement of the responsibilities of the members of the corporation.
- statement on the system of internal financial control signed by the principal;
- corporate governance statement signed by the chair of governors;
- detailed analysis of funding council grants;
- detailed analysis of tuition fees and education contracts;
- additional disclosures in respect of the remuneration of senior postholders and other higher paid staff (including details of pay awards for specific individuals/groups, etc);
- analysis of costs associated with overseas activities; and
- analysis of deferred capital grants received in the year.

118 If colleges wish to download the model report, they should use it only as a basis for completion of their own accounts. The LSC accepts no responsibility for any errors that may result from using the downloaded Excel spreadsheet or Word file.

Guidance to the Notes of the Revised Model Report and Financial Statements for Casterbridge College

119 The F&HE SORP provides guidance on accounting policies and the primary statements of colleges' financial statements, namely:

- the income and expenditure account;
- balance sheet;
- STRGL;
- statement of historical cost surpluses and deficits; and
- cash flow statement.

120 However, the presentation of the notes to the financial statements is left to the individual funding councils. Supplement D to this circular provides guidance to the completion of these notes, and where necessary provides further clarification to the guidance in the F&HE SORP.

Finance Record 2002/03

121 The finance record was designed to be an electronic version of the audited financial statements. When the LSC wishes to refer to the financial performance of the sector or of individual colleges (for example, when making submissions to ministers or publishing benchmarking information), it uses the finance record as its source.

122 In previous years colleges would submit the finance record on a floppy disc to the local LSC, for input onto the LSC's database. However, as a web portal has been developed for the submission of colleges' individualised learner records, it is now appropriate to make use of this technology. The use of such a web portal would have the following advantages:

- the college would receive a receipt to indicate a successful download;
- any input errors would be rejected and so these would have to be corrected

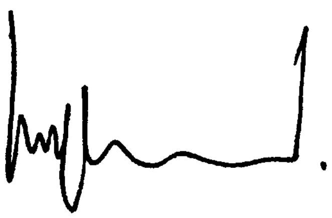
before the finance record could be successfully transferred; and

- as the timing of the annual accounts publication is dependent upon the receipt of accurate finance records, it is expected that this document could be published in a more timely manner.

123 The instructions on transferring the finance record via the web portal will be published at a later date on the Sector Accounting Policies Group page of the LSC's website at: http://www.lsc.gov.uk/documents_list.cfm?categoryId=42.

124 Where a provider does not have an Internet connection with sufficient capacity to return data in this way, they may arrange with their local LSC to use their connection. A designated computer will be set aside to enable them to transfer the data to the LSC database via the secure portal.

125 A signed paper copy of the finance record should be submitted, with the audited financial statements, to the local LSC by 31 January 2004. Supplement E of this circular provides a copy of the finance record, and Supplement F provides notes and guidance on the completion of the finance record. Colleges should download the finance record worksheet from the LSC's website and return the worksheet via the web portal by 31 January 2004.



John Harwood, Chief Executive

Annex A: Cover Sheet for the Return of Audited Financial Statements and Finance Record for the Year Ended 31 July 2003

Area Finance Director
Cheylesmore House
Quinton Road
Coventry
CV1 2WT
T 024 7682 3758
F 024 7682 3590

www.lsc.gov.uk

(Reference Circular 03/08)

This cover sheet must be completed by all colleges. Please photocopy, complete and return to the relevant local Learning and Skills Council office by **31 January 2004**.

Learning+Skills Council

Name of college *(please print)*
Code
Contact for queries *(please print)*
Telephone number

Returns enclosed (please tick)

1	one signed copy of the college's audited financial statements for 2002/03;	☐
2	one signed paper copy of the college's finance record for 2002/03;	☐
3	one copy of each of the college's subsidiary undertakings audited financial statements for 2002/03.*	☐

*If these accounts have not yet been signed please return an unsigned copy indicating when you expect to be able to forward a signed copy.

Annex B: Illustrative Corporate Governance Statements Partial Turnbull Implementation

1 The college is committed to exhibiting best practice in all aspects of corporate governance. This summary describes the manner in which the College has applied the principles set out in section 1 of the *Combined Code on Corporate Governance*, which was issued by the London Stock Exchange in June 1998. Its purpose is to help the reader of the accounts to understand how the principles have been applied.

2 With the exception of the full implementation of the Turnbull guidance as noted below under 'internal control', in the opinion of the Corporation the college complies with all the provisions of the Combined Code in so far as they apply to the further education sector, and it has complied throughout the year ended 31 July 2003.

The Corporation

3 The composition of the Corporation is set out on page ______. It is the Corporation's responsibility to bring independent judgement to bear on issues of strategy, performance, resources and standards of conduct.

4 The Corporation is provided with regular and timely information on the overall financial performance of the College together with other information such as performance against funding targets, proposed capital expenditure, quality matters and personnel-related matters such as health and safety and environmental issues. The Corporation meets each term.

5 The Corporation conducts its business through a number of committees. Each committee has terms of reference, which have been approved by the Corporation. These committees are: finance and general purposes, remuneration, search and audit.

6 All governors are able to obtain independent professional advice in furtherance of their duties at the College's expense and have access to the Clerk to the Corporation, who is responsible to the Board for ensuring compliance with all applicable procedures and regulations. The appointment, evaluation and removal of the Clerk are matters for the Corporation as a whole.

7 Formal agendas, papers and reports are supplied to governors in a timely manner, prior to Board meetings. Briefings are also provided on an ad hoc basis.

8 The Corporation has a strong and independent non-executive element and no individual or group dominates its decision-making process. The Corporation considers that each of its non-executive members is independent of management, and free from any business or other relationship which could materially interfere with the exercise of their independent judgement.

9 There is a clear division of responsibility in that the roles of the Chairman and Principal are separate.

Appointments to the Corporation

10 Any new appointments to the Corporation are a matter for consideration of the Corporation as a whole. The Corporation

has a search committee comprised of ______, which is responsible for the selection and nomination of any new member for the Corporation's consideration. The Corporation is responsible for ensuring that appropriate training is provided as required.

11 Members of the Corporation are appointed for a term of office not exceeding four years.

Remuneration Committee

12 Throughout the year ending 31 July 2003, the College's remuneration committee comprised ______. The committee's responsibilities are to make recommendations to the Board on the remuneration and benefits of the Principal and other senior postholders.

13 Details of remuneration for the year ended 31 July 2003 are set out in note ______ to the financial statements.

Audit Committee

14 The Audit Committee comprises of three members of the Corporation (excluding the Principal and Chair). The Committee operates in accordance with written terms of reference approved by the Corporation.

15 The Audit Committee meets on a termly basis and provides a forum for reporting by the College's internal and financial statement auditors, who have access to the Committee for independent discussion, without the presence of College management. The Committee also receives and considers reports from the LSC as they affect the College's business.

16 The College's internal auditors monitor the systems of internal control, risk management controls and governance processes in accordance with an agreed plan of input and report their findings to management and the Audit Committee.

17 Management is responsible for the implementation of agreed audit recommendations and that internal audit undertake periodic follow-up reviews to ensure such recommendations have been implemented.

18 The Audit Committee also advises the Corporation on the appointment of internal and financial statement auditors and their remuneration for both audit and non-audit work.

Internal Control

19 The Corporation is ultimately responsible for the College's system of internal control and for reviewing its effectiveness. However, such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable, not absolute, assurance against material mis-statement or loss.

20 The Corporation has delegated to the Principal, as Accounting Officer, the day-to-day responsibility for reviewing the adequacy of the system of internal financial control and making any appropriate amendments. He/she is also responsible for reporting to the Corporation any material weaknesses or breakdowns in internal financial control.

21 (The Corporation is of the view that there is a formal ongoing process for identifying, evaluating and managing the College's significant risks that has been in place and operational for the period from the beginning of January 2003 up to the date of approval of the annual report and accounts. This process is regularly reviewed by the Corporation. The governors are unable to state that a formalised process has been in place for the first five months of the year, as this period was needed to put in place the procedures which the Corporation agreed should be established.)

or

(The Corporation is unable to state that a formalised process for identifying, evaluating and managing the College's significant risks has been in place and operational during the year ended 31 July 2003. In the period up to 31 July 2003, the College has put in place the procedures that the Corporation agreed should be established, and the Corporation is of the view that they have been operational from 1 August 2003).

22 The Corporation expects to be able to make a full statement on their corporate governance policy and their review of risks and the systems put in place to mitigate those risks in their report for the year to 31 July 2003.

Going Concern

23 After making appropriate enquiries, the Corporation considers that the College has adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.

(Signed) ______________________________

(Date) ______________________________

(Chair) ______________________________

Full Turnbull Implementation

24 The College is committed to exhibiting best practice in all aspects of corporate governance. This summary describes the manner in which the College has applied the principles set out in section 1 of the *Combined Code on Corporate Governance*, which was issued by the London Stock Exchange in June 1998. Its purpose is to help the reader of the accounts to understand how the principles have been applied.

25 In the opinion of the governors, the College complies with all the provisions of the Combined Code in so far as they apply to the further education sector, and it has complied throughout the year ended 31 July 2003.

The Corporation

26 The composition of the Corporation is set out on page ______. It is the Corporation's responsibility to bring independent judgement to bear on issues of strategy, performance, resources and standards of conduct.

27 The Corporation is provided with regular and timely information on the overall financial performance of the College, together with other information such as performance against funding targets, proposed capital expenditure, quality matters and personnel-related matters such as health and safety and environmental issues. The Corporation meets each term.

28 The Corporation conducts its business through a number of committees. Each committee has terms of reference which have been approved by the Corporation. These committees are: finance and general purposes, remuneration, search and audit.

29 All governors are able to obtain independent professional advice in furtherance of their duties at the College's expense and have access to the Clerk to the Corporation, who is responsible to the Board for ensuring compliance with all applicable procedures and regulations. The appointment, evaluation and removal of the Clerk are matters for the Corporation as a whole.

30 Formal agendas, papers and reports are supplied to governors in a timely manner, prior to Board meetings. Briefings are also provided on an *ad hoc* basis.

31 The Corporation has a strong and independent non-executive element and no individual or group dominates its decision-making process. The Corporation considers that each of its non-executive members is independent of management, and free from any business or other relationship which could materially interfere with the exercise of their independent judgement.

32 There is a clear division of responsibility in that the roles of the Chairman and Principal are separate.

Appointments to the Corporation

33 Any new appointments to the Corporation are a matter for consideration of the Corporation as a whole. The Corporation has a nominations committee comprised of ______, which is responsible for the selection and nomination of any new member for the Corporation's consideration. The Corporation is responsible for ensuring that appropriate training is provided as required.

34 Members of the Corporation are appointed for a term of office not exceeding four years.

Remuneration Committee

35 Throughout the year ending 31 July 2003, the College's remuneration committee comprised ______. The committee's responsibilities are to make recommendations to the Board on the remuneration and benefits of the Principal and other senior postholders.

36 Details of remuneration for the year ended 31 July 2003 are set out in note ______ to the financial statements.

Audit Committee

37 The audit committee comprises of three members of the Corporation (excluding the Principal and Chair). The committee operates in accordance with written terms of reference approved by the Corporation.

38 The Audit Committee meets on a termly basis and provides a forum for reporting by the College's internal and financial statement auditors, who have access to the Committee for independent discussion, without the presence of College management. The Committee also receives and considers reports from the LSC as they affect the College's business.

39 The College's internal auditors monitor the systems of internal control, risk management controls and governance processes in accordance with an agreed plan of input, reporting their findings to management and the Audit Committee.

40 Management is responsible for the implementation of agreed audit recommendations and that internal audit undertake periodic follow-up reviews to ensure such recommendations have been implemented.

41 The Audit Committee also advises the Corporation on the appointment of internal and financial statement auditors and their remuneration for both audit and non-audit work.

Internal Control

42 The Principal, as Accounting Officer, is responsible for ensuring that an effective system of internal control is maintained and operated by the College.

43 The Corporation is ultimately responsible for the College's system of internal control and for reviewing its effectiveness. However, such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable, not absolute, assurance against material mis-statement or loss.

44 The Corporation has delegated to the Principal, as Accounting Officer, the day-to-day responsibility for reviewing the adequacy of the system of internal financial control and making any appropriate amendments. He/she is also responsible for reporting to the Corporation any material weaknesses or breakdowns in internal financial control.

45 The Corporation has reviewed the key risks to which the College is exposed together with the operating, financial and compliance controls that have been implemented to mitigate those risks. The Corporation is of the view that there is a formal ongoing process for identifying, evaluating and managing the College's significant risks that has been in place for the period ending 31 July 2003 and up to the date of approval of the annual report and accounts. This process is regularly reviewed by the Corporation.

46 The senior management team receives reports setting out key performance and risk indicators, and considers possible control

issues brought to their attention by early warning mechanisms which are embedded within the departments and reinforced by risk awareness training. The senior management team and the Audit Committee also receive regular reports from internal audit, which include recommendations for improvement. The Audit Committee's role in this area is confined to a high-level review of the arrangements for internal control. The Corporation's agenda includes a regular item for consideration of risk and control and receives reports therein from the senior management team and Audit Committee. The emphasis is on obtaining the relevant degree of assurance, not merely reporting by exception. At its October 2003 meeting, the Corporation carried out the annual assessment for the year ended 31 July 2003 by considering documentation from the senior management team and internal audit, and taking account of events since 31 July 2003.

Going Concern

47 After making appropriate enquiries, the Corporation considers that the College has adequate resources to continue in operational existence for the foreseeable future. For this reason it continues to adopt the going concern basis in preparing the financial statements.

(Signed) ______________________________

(Date) ______________________________

(Chair) ______________________________

Notes

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