Llywodraeth Cymru
Welsh Government

www.cymru.gov.uk

Accounts direction to further education institutions for 2012/13

PHOTO REDACTED DUE TO THIRD PARTY RIGHTS OR OTHER LEGAL ISSUES

Guidance

Welsh Government circular no: 009/2013
Date of issue: September 2013
Replaces circular no: 012/2012

Accounts direction to further education institutions for 2012/13

Audience	Senior finance managers of further education institutions in Wales.
Overview	This accounts direction advises institutions of the Welsh Government's requirements of their audited financial statements in accordance with paragraph 54 of the Financial Memorandum issued on 1 January 2007 (reference 026-06).
Action required	None – for information only.
Further information	Enquiries about this document should be directed to: Natalie James Finance and Corporate Services Division Department for Education and Skills Welsh Government Cathays Park CF10 3NQ Tel: 029 2082 5842
Additional copies	This document can be accessed from the Welsh Government's website at www.wales.gov.uk/educationandskills
Related documents	Financial Memorandum between Welsh Government, Further Education Institutions and Higher Education Institutions providing further education in Wales (2007)

Digital ISBN 978 1 4734 0168 6

WG19665

Contents

Introduction

1 This Accounts Direction advises institutions of the Welsh Government's requirements of their audited financial statements in accordance with paragraph 54 of the Financial Memorandum.

Background

2 Paragraph 54 of the Financial Memorandum between the Welsh Government and institutions requires institutions to comply with the Accounts Direction issued periodically by the Welsh Government. The direction will cover information to be contained in the financial statements, the manner in which they are to be presented and the methods and principles according to which they are prepared and will be in accordance with Generally Accepted Accounting Principles.

3 In issuing this direction the Welsh Government wishes to ensure the form, content and disclosures within institution's financial statements follow good practice, are consistent across the sector and meet any specific requirements of the Welsh Government.

Accounts direction for 2012/13

4 In preparing their financial statements, the Welsh Government requires all institutions to comply with the **Statement of Recommended Practice: Accounting for Further and Higher Education (SORP),** or any successor to the SORP.

5 In July 2007 the FE/HE SORP Board issued a Statement of Recommended Practice (SORP), effective from 1 August 2007. This SORP is applicable for the 2012/13 financial year. Copies of the SORP can be downloaded from the Universities UK website at:

http://www.universitiesuk.ac.uk/highereducation/Pages/SORP.aspx

6 Institutions should note that paragraph 15 of the SORP requires that the four primary accounting statements (an income and expenditure account, a balance sheet, a cash flow statement and a statement of total recognised gains and losses) must be presented in the formats set out in Appendix 2 to the SORP.

7 Appendix 3 of the SORP provides a list of notes which may be required to accompany the primary statements. The 'Casterbridge College Model Financial Statements', (chapter 4 of the Association of Colleges Accounts Direction Handbook 2012/13) give illustrative examples of these and institutions are encouraged to disclose as much of this information as possible. The latest version of the Handbook is available at the AoC website at:

http://www.aoc.co.uk/en/policy-and-advice/funding-and-finance-pensions/finance-directors/finance-guidance.cfm

8 In addition to the requirements of the SORP, the Welsh Government requires that institutions' audited financial statements be prepared in accordance with current Accounting Standards, FRS's and Urgent Issues Task Force (UITF) Abstracts issued or adopted by the Accounting Standards Board.

9 In the case of an institution that is also a company limited by guarantee, this direction is subject to the additional requirements of the Companies Act 2006.

10 Where an institution has subsidiaries that are limited companies they will be subject to the requirements of the Companies Act 2006.

11 Where an institution is a registered charity they will be subject to the additional requirements of the 'Accounting and Reporting by Charities' Statement of Recommended Practice (revised 2005) and the Charities Act 2011. In order for Welsh Further Education Institutions to remain as exempt charities the Welsh Government will become the principal regulator of the sector from 1 September 2013.

12 Institutions are also required to include in their financial statements the following:

i a statement covering the responsibilities of their governing body in relation to corporate governance. This statement, that incorporates a statement on internal control, is required to indicate how the institution has complied with current best practice in this area. Guidance on how institutions can comply with this requirement is available in Annex A and a model statement is shown in Annex B

ii the total emoluments of the principal and higher paid employees. A higher paid employee is defined as an employee whose total emoluments exceed £60,000 during the financial year. Full guidance on the required disclosures is set out in Annex D

iii the compensation for loss of office paid or payable to the principal or higher paid employee (as defined in Annex D). Full guidance on the required disclosures is set out in Annex E

iv details of the net cost to an institution in respect of expenditure on overseas activities in accordance with Annex F

v within the members' report to the financial statements, a statement on the payment performance of the institution during the period. For further guidance see Annex G.

Further specific guidance

13 Additional guidance is included in Annex G on the following matters:

- enhanced pension provisions (FRS 12)
- accounting for grants, where specific guidance is provided on Disability Discrimination Act (DDA) and backlog maintenance funding
- agency costs
- prompt payments disclosures
- consortium income
- auditor fees
- changes to financial statement disclosures
- Operating and Financial Review
- the disclosures for 2012/13 relating to FRS 17 Retirement Benefits.

External audit

14 Institutions are required to ensure that their contracts for external audit make provision for an opinion on whether the institution has applied income, where appropriate, in accordance with the Financial Memorandum, and whether Welsh Government grants have been used for the purposes for which they were received.

15 Institutions should be aware that their external auditors will be reviewing the corporate governance and internal controls statement as part of their audit work

and will be including a reference to this work in their audit opinion. An example certificate is available in Annex C.

16 This Accounts Direction and the Financial Memorandum should be copied to the external auditors.

17 External auditors are reminded that where they are unable to express an unqualified opinion on the institution'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 Welsh Government, Department for Education and Skills, Deputy Director, Finance and Corporate Services Division.

18 Audit firms cannot be appointed as internal and external auditors at the same time or for the same financial year under any circumstances.

19 It is a requirement of the Financial Memorandum that the statutory accounts are published on the College's website. This may require an extra statement from external auditors. The auditors may also require an extra statement in the governing body's responsibilities in regard to the website if the audit opinion is to be published.

20 If accounts are published in Welsh this may also require a review of the Welsh version by the external auditors.

Accounting developments

21 FRS 100 (Application of financial reporting requirements) and FRS 101 (Reduced disclosure requirements) were published in November 2012. FRS 102 (the finance reporting standard applicable in the UK and Republic of Ireland) was published in March 2013. Annex H provides a summary of these standards and their applicable dates.

22 We are not aware of any significant changes in accounting standards for 2012/13.

Accounts timetable

23 Paragraph 54 of the Financial Memorandum requires institutions to provide the Welsh Government with copies of its financial statements no later than 31 December. The Welsh Government also requires the external auditor's management letter, including the institution's response, to be submitted at the same time.

Review of this Direction

24 The Accounts Direction will be reviewed each year. This Accounts Direction will remain in force unless institutions are notified otherwise.

Annex A: Guidance on the statement of corporate governance

UK Corporate Governance Code

The code issued in June 2010 superseded and replaced the Combined Code issued by the LSE in various forms since 1998. A small number of changes had been made to the previous versions of the Code but do not affect the substance of the following text.

Main features of the Code

The Code's overall aim is to enhance board effectiveness and to improve investor confidence by raising standards of corporate governance. The main features of the Code are:

- new definitions of the role of the board, the chairman and non-executive directors
- more open and rigorous procedures for the appointment of directors and from a wider pool of directors
- formal evaluation of the performance of boards, committees and individual directors, enhanced induction and more professional development of non-executive directors
- the separation of the roles of the chairman and the chief executive to be reinforced
- a chief executive should not go on to become chairman of the same company
- closer relationships between the chairman, the senior independent director, non-executive directors and major shareholders
- a strengthened role for the audit committee in monitoring the integrity of the company's financial reporting, reinforcing the independence of the external auditor and reviewing the management of financial and other risks.

The Code incorporates the substance of Derek Higgs' and Sir Robert Smith's proposals. The main areas of difference are:

- modification of the Code's structure to include not only main "principles" and "provisions" but also supporting "principles", allowing companies greater flexibility in how they implement the Code
- the board chairman to be able to chair the nomination committee
- clarification of the roles of chairman and the senior independent director, emphasising the chairman's role in providing leadership to the non-executive directors and in the communication of shareholders' views to the board

- smaller companies below the FTSE 350 only required to have a minimum of two independent non-executive directors

The intention is that provisions should be as clearly defined and verifiable as possible, so that companies can report unambiguously whether or not they have followed them. The supporting principles are cast in more general terms and leave the detailed method of implementation up to the Institution to decide.

If the Code is applicable to Colleges, they will be required to make a statement on how they have applied the main and supporting principles. The statement should also include confirmation that the College complies with the Code's provisions or, where it does not comply, provide an explanation as to why this is the case.

In September 2012, the Financial Reporting Council (FRC) published a new edition of the UK Corporate Governance Code to replace the 2010 Code. The new Code applies to accounting periods beginning on or after 1 October 2012. Therefore institution's should continue to report against the June 2010 edition of the Code, although they are encouraged to consider whether it would be beneficial to adopt some or all of the new provisions in the revised code earlier than expected.

Institutions need to be aware of the Code and should consider its impact on their corporate governance. A standard model has been provided (at Annex B) as a consistent starting point. However, as institutions are different in complexity and size, there may be a need to change the model which should be tailored to the institution's own requirements, showing:

- what work has been done to embed risk management in the corporate governance of the institution
- what assurance can be gained by the reader of the institution's accounts.

Maintaining a sound system of internal control

The Governing Body is responsible for the institution's system of internal control. It should set appropriate policies on internal control and seek regular assurance that will enable it to satisfy itself that the system is functioning effectively. The Governing Body must further ensure that the system of internal control is effective in managing risks in the manner which it has approved.

In determining its policies with regard to internal control, and thereby assessing what constitutes a sound system of internal control in the particular circumstances of the institution, the Governing Body's deliberations should include consideration of the following factors:

- the nature and extent of the risks facing the institution
- the extent and categories of risk which it regards as acceptable for the institution to bear
- the likelihood of the risks concerned materialising

- the institution's ability to reduce the incidence and impact on the business of risks that do materialise
- the costs of operating particular controls relative to the benefit thereby obtained in managing the related risks.

It is the role of management to implement the Governing Body's policies on risk and control. In fulfilling its responsibilities, management should identify and evaluate the risks faced by the institution for consideration by the Governing Body and design, operate and monitor a suitable system of internal control which implements the policies adopted by the Governing Body.

All employees have some responsibility for internal control as part of their accountability for achieving objectives. They, collectively, should have the necessary knowledge, skills, information and authority to establish, operate and monitor the system of internal control. This will require an understanding of the institution, its objectives, the environment in which it operates, and the risks it faces.

An internal control system encompasses the policies, processes, tasks, behaviours and other aspects of an institution that, taken together:

- facilitate its effective and efficient operation by enabling it to respond appropriately to significant business, operational, financial, compliance and other risks to achieving the institution's objectives. This includes the safeguarding of assets from inappropriate use or from loss and fraud, and ensuring that liabilities are identified and managed
- help ensure the quality of internal and external reporting. This requires the maintenance of proper records and processes that generate a flow of timely, relevant and reliable information from within and outside the organisation
- help ensure compliance with applicable laws and regulations, and also with internal policies with respect to the conduct of business.

An institution's system of internal control will reflect its control environment, which encompasses its organisational structure. The system will include:

- control activities
- information and communications processes
- processes for monitoring the continuing effectiveness of the system of internal control.

The system of internal control should:

- be embedded in the operations of the institution and form part of its culture
- be capable of responding quickly to evolving risks to the business arising from factors within the institution and to changes in the higher education sector

- include procedures for reporting immediately to appropriate levels of management any significant control failings or weaknesses that are identified together with details of corrective action being undertaken.

A sound system of internal control reduces, but cannot eliminate, the possibility of poor judgment in decision-making; human error; control processes being deliberately circumvented by employees and others; management overriding controls; and the occurrence of unforeseeable circumstances.

A sound system of internal control therefore provides reasonable, but not absolute, assurance that an institution will not be hindered in achieving its business objectives, or in the orderly and legitimate conduct of its business, by circumstances which may reasonably be foreseen. A system of internal control cannot, however, provide protection with certainty against an institution failing to meets its objectives or all material errors, losses, fraud, or breaches of laws or regulations.

Reviewing the effectiveness of internal control

Reviewing the effectiveness of internal control is an essential part of the Governing Body's responsibilities. The Governing Body will need to form its own view on effectiveness after due and careful enquiry based on the information and assurances provided to it. Management is accountable to the Governing Body for monitoring the system of internal control and for providing assurance to the Governing Body that it has done so.

The role of institutional committees in the review process, including that of the audit committee, is for the Governing Body to decide and will depend upon factors such as the nature of the significant risks that the institution faces. To the extent that designated Governing Body committees carry out, on behalf of the Governing Body, tasks that are attributed in this guidance document to the Governing Body, the results of the relevant committees' work should be reported to, and considered by, the Governing Body. The Governing Body takes responsibility for the disclosure on internal control in the annual report and accounts.

Effective monitoring on a continuous basis is an essential component of a sound system of internal control. The Governing Body cannot, however, rely solely on the embedded monitoring processes within the institution to discharge its responsibilities. It should regularly receive and review reports on internal control. In addition, the Governing Body should undertake an annual assessment for the purposes of making its public statement on internal control to ensure that it has considered all significant aspects of internal control for the institution for the year under review and up to the date of approval of the annual report and accounts.

The Governing Body should define the process to be adopted for its review of the effectiveness of internal control. This should encompass both the scope and frequency of the reports it receives and reviews during the year, and also the process for its annual assessment, such that it will be provided with sound, appropriately documented, support for its statement on internal control in the institution's annual report and accounts.

The reports from management to the Governing Body should, in relation to the areas covered by them, provide a balanced assessment of the significant risks and the effectiveness of the system of internal control in managing those risks. Any significant control failings or weaknesses identified should be discussed in the reports, including the impact that they have had, could have had, or may have, on the institution and the actions being taken to rectify them. It is essential that there be openness of communication by management with the Governing Body on matters relating to risk and control.

When reviewing reports during the year, the Governing Body should:

- consider what are the significant risks and assess how they have been identified, evaluated and managed
- assess the effectiveness of the related system of internal control in managing the significant risks, having regard, in particular, to any significant failings or weaknesses in internal control that have been reported
- consider whether necessary actions are being taken promptly to remedy any significant failings or weaknesses
- consider whether the findings indicate a need for more extensive monitoring of the system of internal control.

Additionally, the Governing Body should undertake an annual assessment for the purpose of making its public statement on internal control. The assessment should consider issues dealt with in reports reviewed by it during the year together with any additional information necessary to ensure that the Governing Body has taken account of all significant aspects of internal control for the institution for the year under review and up to the date of approval of the annual report and accounts.

The Governing Body's annual assessment should, in particular, consider:

- the changes since the last annual assessment in the nature and extent of significant risks, and the institution's ability to respond to changes in its business and the external environment
- the scope and quality of management's ongoing monitoring of risks and of the system of internal control, and, where applicable, the work of its internal audit function and other providers of assurance
- the extent and frequency of the communication of the results of the monitoring to the Governing Body (or Governing Body's committee(s)) which enables it to build up a cumulative assessment of the state of control in the institution and the effectiveness with which risk is being managed
- the incidence of significant control failings or weaknesses that have been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the institution's financial performance or condition

- the effectiveness of the institution’s public reporting processes.

Should the Governing Body become aware at any time of a significant failing or weakness in internal control it should determine how the failing or weakness arose and re-assess the effectiveness of management’s ongoing processes for designing, operating and monitoring the system of internal control.

The Governing Body’s statement on internal control

In its narrative statement of how the institution has applied the principles of the Code, the Governing Body should, as a minimum, disclose that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the institution, that it has been in place for the year under review and up to the date of approval of the annual report and accounts, that it is regularly reviewed by the Governing Body and accords with the Turnbull guidance.

The Governing Body may wish to provide additional information in the annual report and accounts to assist understanding of the institution’s risk management processes and system of internal control.

The disclosure relating to the application of the principles of the Code should include an acknowledgement by the Governing Body that it is responsible for the institution’s system of internal control and for reviewing its effectiveness. It should also explain that such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Governing Body should summarise the process it (where applicable, through its committees) has applied in reviewing the effectiveness of the system of internal control. It should also disclose the process it has applied to deal with material internal control aspects of any significant problems disclosed in the annual report and accounts.

The Governing Body should ensure that its disclosures provide meaningful, high-level information and do not give a misleading impression.

Where material joint ventures and associates have not been dealt with as part of the group for the purposes of applying this guidance, this should be disclosed.

Annex B: Model corporate governance statement incorporating the statement on internal control

The Institution is committed to exhibiting best practice in all aspects of corporate governance.

This summary describes the manner in which the Institution has applied the principles set out in the UK Corporate Governance Code ("the Code") issued by the Financial Reporting Council (FRC) in June 2010. Its purpose is to help the reader of the accounts understand how the principles have been applied.

In the opinion of the governors, the Institution complies with all the provisions of the Code in so far as they apply to the Further Education Sector, and it has complied throughout the year ended 31 July 2013. The Governing Body recognises that, as a body entrusted with both public and private funds, it has a particular duty to observe the highest standards of corporate governance at all times.

The Corporation

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

The Corporation is provided with regular and timely information on the overall financial performance of the Institution, 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.

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-amend as appropriate to college*]. Full minutes of all meetings, except those deemed to be confidential by the Corporation, are available from the clerk to the Corporation at: *[x].*

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

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.

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.

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

Appointments to the Corporation

Any new appointments to the Corporation are a matter for the consideration of the Corporation as a whole. The Corporation has a search committee which is comprised of *[x]* 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.

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

Remuneration committee

Throughout the year ending 31 July 2013, the Institution's remuneration committee comprised *[x].* The committee's responsibilities are to make recommendations to the Board on the remuneration and benefits of the Principal and other senior post holders.

Details of remuneration for the year ended 31 July 2013 are set out in note *[x]* to the financial statements.

Audit committee

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

The audit committee meets on a termly basis and provides a forum for reporting by the Institution's internal and external financial statement auditors, who have access to the committee for independent discussion, without the presence of Institution management. The committee also receives and considers reports from the Welsh Government as they affect the Institution's business.

The Institution'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.

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

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

Scope of responsibility

The Corporation is ultimately responsible for the Institution'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 and not absolute assurance against material misstatement or loss.

The Corporation has delegated the day-to-day responsibility to the Principal, as Accounting Officer, for maintaining a sound system of internal control that supports the achievement of the Institution's policies, aims and objectives, whilst safeguarding the public funds and assets for which [he/she] is personally responsible, in accordance with the responsibilities assigned to [him/her] in the Financial Memorandum between the Institution and the Welsh Government. [He/She] is also responsible for reporting to the Corporation any material weaknesses or breakdowns in internal control.

The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of institution policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically. The system of internal control has been in place in the College for the year ended 31 July 2013 and up to the date of approval of the annual report and accounts.

Capacity to handle risk

The Corporation has reviewed the key risks to which the Institution 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 Institution's significant risks that has been in place for the period ending 31 July 2013 and up to the date of approval of the annual report and accounts. This process is regularly reviewed by the Corporation.

The risk and control framework

The system of internal control is based on a framework of regular management information, administrative procedures including the segregation of duties, and a system of delegation and accountability. In particular, it includes:

- comprehensive budgeting systems with an annual budget, which is reviewed and agreed by the governing body
- regular reviews by the governing body of periodic and annual financial reports, which indicate the financial performance against forecasts
- setting targets to measure financial and other performance
- clearly defined capital investment control guidelines
- the adoption of formal project management disciplines, where appropriate.

The College has an internal audit service, which operates in accordance with the requirements of the Welsh Government. The work of the internal audit service is informed by an analysis of the risks to which the institution is exposed, and annual internal audit plans are based on this analysis. The analysis of risks and the internal audit plans are endorsed by the Corporation on the recommendation of the audit committee. At minimum annually, the Head of Internal Audit provides the governing body with a report on internal audit activity in the institution. The report includes the Head of Internal Audit's independent opinion on the adequacy and effectiveness of the Institution's system of risk management, controls and governance processes.

Review of effectiveness

As Accounting Officer, the Principal has responsibility for reviewing the effectiveness of the system of internal control. [His/Her] review of the effectiveness of the system of internal control is informed by:

- the work of the internal auditors
- the work of the executive managers within the Institution who have responsibility for the development and maintenance of the internal control framework
- comments made by the Institution's financial statements auditors and the Welsh Government's auditors in their management letters and other reports.

The Principal has been advised on the implications of the result of [his/her] review of the effectiveness of the system of internal control by the audit committee, which oversees the work of the internal auditor [and Risk Committee, if appropriate] and a plan to address weaknesses and ensure continuous improvement of the system is in place.

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 thereon from the senior management team and the audit committee. The emphasis is on obtaining the relevant degree of assurance and not merely reporting by exception. At its October 2013 meeting, the Corporation carried out the annual assessment for the year ended 31 July 2013 by considering documentation from the senior management team and internal audit, and taking account of events since 31 July 2013.

Significant internal control problems [if applicable]

[If there are significant internal control problems, record here an outline of the actions taken, or proposed, to deal with them. The wording should be tailored to reflect the circumstances of the case.]

Going concern

After making appropriate enquiries, the Corporation considers that the Institution 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.

Approved by order of the members of the Corporation on [x] and signed on its behalf by:

[Signed]	[Signed]
[Date]	[Date]
[Chair]	[Principal]

Annex C: Guidance on the suggested form of wording for the audit report by an Institution’s external auditors for the year ended 31 July 2013

Independent auditors’ report to the Governing Body of [XYZ] Institution

We have audited the financial statements of [XYZ] Institution for the year ended 31 July 2013, which comprise the Income and Expenditure Account, the Balance Sheet, the Cash Flow Statement, the Statement of Total Recognised Gains and Losses and the related notes. The financial reporting framework that has been applied in their preparation is applicable law, UK accounting standards (UK Generally Accepted Accounting Practice) the Statement of Recommended Practice – Accounting for Further and Higher Education and the Accounts Direction issued by the Welsh Government.

Respective responsibilities of the Governing Body and Auditor

As explained more fully in the Statement of Governing Body’s responsibilities set out on page [ ], the Governing Body is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board’s (APB’s) Ethical Standards for Auditors.

This report is made solely to the Governing Body, as a body, in accordance with *Article [x]* of the Institutions articles of government. Our work has been undertaken so that we might state to the Governing Body, as a body, those matters we are required to state to them in an auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Governing Body, as a body, for our audit work, for this report, or for the opinions we have formed.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Institution’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Governing Body; and the overall presentation of the financial statements.

We report to you whether in our opinion, in all material respects, monies expended out of Welsh Government grants and other funds from whatever source administered by the Institution for specific purposes have been properly applied to those purposes and, if appropriate, managed in compliance with all relevant legislation and whether in our opinion, in all material respects, income has been applied in accordance with the financial memorandum with the Welsh Government.

We also report to you if, in our opinion, the Governing Body' Report is not consistent with the financial statements, if the Institution has not kept proper accounting records, if the accounting records do not agree with the financial statements, or if we have not received all the information and explanations we require for our audit.

We read the Report of the Governing Body including the corporate governance statement and the statement of internal control and consider the implications for our report if we become aware of any apparent misstatement within it.

Opinion on financial statements

In our opinion:

a) the financial statements give a true and fair view of the state of the Institution's affairs as at 31 July 2013 and of its surplus of income over expenditure and cash flows for the year then ended;

b) the financial statements have been properly prepared in accordance with the Accounts Direction issued by the Welsh Government, the 2007 Statement of Recommended Practice – Accounting for Further and Higher Education, and United Kingdom Generally Accepted Accounting Practice;

c) proper accounting records have been kept; and

d) the financial statements are in agreement with the accounting records.

Opinion on other matters prescribed in the Further Education Audit Code of Practice 2007 issued by the Welsh Government

In our opinion:

a) in all material respects, monies expended out of Welsh Government grants and other funds from whatever source administered by the Institution for specific purposes have been properly applied to those purposes and, if appropriate, managed in compliance with all relevant legislation;

b) in all material respects, income has been applied in accordance with the financial memorandum with the Welsh Government.

Name
Registered Auditors
Address
Date

Annex D: Emoluments of the principal and higher-paid employees

Disclosure requirements:

1 These disclosures apply to the Principal and any higher paid employee. A higher paid employee for the purposes of this disclosure is one whose total emoluments paid or payable during the financial year exceeded £60,000.

2 Institutions are required to disclose the following in their audited financial statements:

- the emoluments of the Principal, disclosing a sub total that excludes the employer's pension contributions and a total that includes these contributions
- the emoluments of the highest paid employee, if that is not the Principal
- emoluments due to a higher paid employee but waived by the employee
- the salary bands of higher paid employees (including the Principal), giving the number of such employees that fall into each band. The width of each salary band should be £10,000
- the aggregate amount of any compensation paid to any Principal or higher paid employee for loss of office, excluding any payments in lieu of notice (as these form part of the annual emoluments) (see Annex E)
- the number of employees who have been paid such compensation.

3 'Emoluments' mean emoluments paid to or receivable by any person for:

- services to the institution
- services as a director or officer of any subsidiary of the institution,.

4 For this purpose, 'emoluments' paid to, or receivable by, an employee include their normal remuneration salary, and the following:

- fees
- any expense allowance (to the extent that they are chargeable to UK income tax)
- employer's pension contributions
- the estimated money value of any benefits received other than in cash (the money value of benefits in kind should be estimated by reference to the market value of the facility provided)

5 Emoluments should not include the employer's national insurance contributions. Compensation for loss of office is a category of payment different from an 'emolument'. Consequently, it should not be included in that person's emoluments for banding purposes.

6 If more than one person has been Principal during the year, each such person's total emoluments for the year must be attributed to that part of the year during which they were Principal, and these amounts must be disclosed separately.

7 Disclosure of the various emoluments should show the analysis between:

- salaries
- benefits in kind
- pension contributions.

Benefits in kind

8 As noted in 4 above, wherever possible the money value of benefits in kind should be estimated by reference to the market value of the facility provided. Where it is not practicable to use market values, taxable values should be used. Guidance that institutions should discuss with their auditors on the treatment of motor cars and subsidised accommodation is set out below.

Motor cars

9 Where an institution provides a leased motor car the market value could be calculated with reference to the lease payments and additional running costs borne by the institution. Likewise, if the institution purchases a car then the sum disclosed could be calculated by reference to annual running costs including depreciation and associated interest costs. This may involve distinguishing between private and business mileage and require the Principal/higher paid employee to keep a record of his or her private and institutional mileage. These amounts may more properly represent the cost to the institution than the taxable benefit.

Subsidised accommodation

10 Where the institution owns the property, the benefit derived by the Principal/higher paid employee is the difference between the rent he/she paid (if any) and the estimated market rent for that property which the institution would receive if it were to lease the premises on a commercial basis. If the institution merely leases the property, the benefit could be assessed as the difference between the rent and other expenses paid by the institution and that paid by individual. Private and institutional use of the accommodation will need to be apportioned on a fair and consistent basis; and it would be helpful if the individual kept a record of institutional use to help with the calculation of a fair apportionment.

11 Where an institution makes it a condition of employment that an individual resides in an official residence, then disclosure on the basis of treatment for tax purposes is reasonable. Institutions and their auditors should reach a judgement that apportionments about private use are fair. The line adopted by the HMRC can serve to inform that judgement.

Annex E: Compensation for loss of office

Disclosure requirements:

1 This disclosure applies to the Principal and any higher paid employee. A higher paid employee for the purposes of this disclosure is one whose total emoluments paid or payable during the financial year (or the preceding financial year) exceeded £60,000 or whose total emoluments paid or payable during the financial year exceeded £60,000 on a per annum basis.

2 Institutions shall show the aggregate amount of any compensation paid or payable to the Principal or any higher paid employee in respect of loss of office.

3 This amount disclosed must also include and distinguish between compensation paid or payable for loss of:

- any other office in connection with the management of the institution's affairs
- any office in connection with the management of the affairs of a subsidiary undertaking of the institution.

4 Compensation disclosed shall include the estimated monetary value of any non-cash benefits paid or payable and the disclosure will also describe the nature of such compensation.

5 References to compensation for loss of office include compensation paid or payable in consideration for, or in connection with, retirement and/or enhancement of pension scheme benefits.

Annex F: Costs in respect of overseas activities

Disclosure requirements

	Travel and accommodation £k	Subsistence and Hospitality £k	Other Costs £k	Number of Visits No
Governors				
Senior Post Holders				
Other individuals				

Explanatory Notes and Guidance

Certain costs incurred in relation to the undertaking of overseas activities will need to be disclosed in the audited financial statements of the institution. The disclosure requirements relate to the net cost to the institution in respect of expenditure on overseas activities incurred by or on behalf of:

- members of the governing body
- senior post holders
- other individuals.

Institutions should expand on this minimum disclosure where this would contribute to the overall understanding of their financial statements. The disclosure note should appear immediately after the detailed note on ‘other operating expenses’.

Foreign activities are defined as ‘expenditure incurred outside the United Kingdom, or incurred in connection with travel outside the United Kingdom’. Institutions need not disclose expenditure incurred in respect of:

- students involved in course related overseas activity
- staff (but not governors) travelling with students involved in course related overseas activity
- overseas activities where the full costs are met by students.

The number of visits column is designed to reflect the number of person visits. For example if three people went on one trip, and four people went on another trip, then the column would show seven, not two. To simplify the disclosure, institutions may show the cost of breakfast in the accommodation column if it is integral to the room rate.

Where any items are recorded under expenditure for or on behalf of ‘Other individuals’, who are not members of staff, full details (including the names of the travellers and the reason for the expenditure) also need to be disclosed. For example, this additional disclosure would be needed where expenditure had been incurred for or on behalf of the spouse of a governor.

Annex G: Specific guidance

Enhanced pension provisions

A college's enhanced pension provision can constitute two different types of provision:

i) enhanced pensions resulting from redundancy (termination related pension entitlements)

ii) enhanced pensions relating from early retirement, where an expectation of that payment existed prior to retirement.

It is expected that the majority of enhanced pensions in colleges are termination related pension entitlements and these are outside the scope of FRS 17 and therefore should be treated as a provision under FRS 12 Provisions, Contingent Liabilities and Assets and should be disclosed separately from FRS17.

Institutions must use the tables supplied by the Skills Funding Agency / Association of Colleges in calculating any provision for enhanced pension. ***The use of these tables is recommended unless a more accurate estimate can be obtained from the Institution's actuaries.*** The CPI option should be used following the Governments announcement in 2010 that CPI will be used, rather than RPI, for public sector pensions. The tables were updated in 2010 for more recent mortality tables amongst other things and further updated versions for market indices will be issued shortly after 31st July 2013 when these are known and should be included within the accounts. The current tables, together with updated versions, can be found at the link below:

http://www.aoc.co.uk/en/policy-and-advice/funding-and-finance-pensions/finance-directors/finance-guidance.cfm

Accounting for grants

Any grants received from public funds should be accounted for in accordance with SSAP 4 Accounting for Government Grants. This means that the income should be matched to the relevant expenditure. Any capital grant received should be credited to a deferred capital grant account and not deducted from the purchase price of the assets concerned. The amount of the grant should be credited to the I&E account over the useful economic life of the related asset, on a basis consistent with the depreciation policy. If a capital grant is received before the purchase of the relevant asset, then the grant should be held in payments on account until spent. Where the conditions attached to an award of a grant state that the grant should be directed towards capital expenditure, it should be treated as a deferred capital grant.

Specific grants for DDA work and backlog maintenance have been distributed during the year. To the extent that these grants have not been spent at the year end they should be included in payments received in advance within creditors. Once spent they should either be shown as revenue or credited to deferred capital grants as appropriate in line with the nature of the expenditure.

Agency costs

Institutions should review and consider the guidance set out in paragraph 55 of the SORP in respect of agency costs.

Where the institution disburses funds it has received as paying agent on behalf of another body and it has no beneficial interest in the funds the receipt and subsequent disbursement of the funds should be excluded from the income and expenditure of the institution where the FRS 5 test for the recognition of an Asset is not met, ie, where the institution does not have control over the future economic benefits.

What constitutes an agency arrangement will depend upon each individual fund and its own individual characteristics. However, financial contingency funds (access funds) and Educational Maintenance Allowances are such funds that institutions will need consider to assess if the FRS 5 test would be met or not.

The key test is whether the institution has any future beneficial interest in the funds. In the majority of cases the funds will be given to students to support their studies, and so the beneficial interest will be transferred from the institution to the learner. Where this occurs, the funds should be excluded from the income and expenditure account. In the institution’s year-end financial statements there should be a separate note for each of the funds showing how they have been treated.

In some cases, funds might not be passed direct to the student but to a third party, in order to pay for student-related transactions, such as residential costs and equipment. In these cases, as the contract is between the institution and the third party, the beneficial interest is not transferred from the institution to the learner. Where this occurs, the funds should be included within the income and expenditure of the institution. For example, large items of equipment purchased from the access fund for a student’s need might remain the property of the institution.

Institutions are recommended to include a new accounting policies note on agency arrangements in their financial statements, for example:

> The institution acts as an agent in the collection and payment of financial contingency funds and educational maintenance allowances. Related payments received from the Welsh Government and subsequent disbursements to students and institutions are excluded from the income and expenditure account and are shown separately in note xxxx.

If you have any queries over the interpretation of this guidance please contact your external auditor.

Payment performance

The Better Payments Practice Code

The four key principles of the Better Payments Practice Code, which institutions should adopt are:

- agree payment terms at the outset of a deal and stick to them
- explain the payment procedures to suppliers
- pay bills in accordance with any contract agreed with the supplier, or as required by law
- tell suppliers without delay when an invoice is contested and settle quickly on receiving a satisfactory response.

HM Treasury expects public sector bodies to comply with this code as it represents best practice.

The Late Payment of Commercial Debts

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. If no credit period has been agreed, then the Act sets a default period of 30 days after which interest can run.

Required disclosures

The institution's policy and practice on payment of creditors should be disclosed in the Members Report. This should include a policy statement for the following financial year and the number of days (calculated in the prescribed manner) taken to pay bills in the current financial year.

The statement must include whether:

- it is the institution's policy to follow any code or standard on payment practice and, if so, give the name of the code or standard
- in respect of some, or all, of its suppliers, it is the institution's policy to:

  i settle the terms of payment with those suppliers when agreeing the terms of each transaction

  ii ensure that these suppliers are made aware of the terms of the payment

  iii abide by the terms of payment.

Where the statement does not cover all suppliers, the policy for the other suppliers needs to be disclosed.

The amount of any interest paid under The Late Payment of Commercial Debts (Interest) Act 1998 should also be disclosed.

Calculation of payment days

The number of days represented by trade creditors falling due for payment within one year at the year end, compared to the total amounts invoiced to suppliers during the year. This calculation method, which should be familiar to your external auditors, is as follows:

Trade creditors at the end of the year are £100k.

Amounts invoiced during the year by suppliers are £1m

Number of days in the financial year is 365.

$$\frac{100}{1,000} \times 365 = 36.5 \text{ days}$$

Consortium income

There are an increased number of consortium arrangements in place for example where colleges are lead providers in Worked Based Learning consortia. If the institution is acting as the lead in the consortium, it should only include its own income earned in the I&E, not that passed onto other consortium members. An extra note under the funding council grants note will be required to detail consortium income as follows :

“The Institution is the lead partner in a consortium to deliver xxxx. The income included in these accounts is earned by the institution in its capacity as a provider and consortium lead. All other income relating to the consortium and payable to consortium members has been excluded from the accounts. Total income claimed in the year and the related payments to partners was as follows”:

Total income	x
Payments to FE partners	x
Payments to non FE partners	x
Net income	x

Where there is not a consortia arrangement, but an institution is the lead in a work based learning contract, then the total income should be recorded in the I&E, however the amount paid to other providers as subcontractors should be included in a note to the accounts as above.

Auditor fees

The Companies Act 2006 required a more detailed breakdown of auditor's fees for years beginning on or after 1 Oct 2005, this requirement is transferred to the FE sector. The disclosures required are a split between audit fees and other services fees for both the internal and external auditors. Comparatives are required.

The ICAEW has issued TECH 04/11 Disclosure of Auditor Remuneration which provides draft guidance on the disclosure of auditor remuneration for the audit of accounts and other (non audit) services, in accordance with the requirements of the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2008 (Statutory Instrument 2008/489) amended by Regulations 2011 (Statutory Instrument 2011/2198). These come into effect for financial years beginning on or after 1 October 2011 and are considered best practice for the FE sector.

The disclosure of auditor remuneration has been extended to include remuneration receivable by associates of the auditor in respect of the audit of the institution. Associates include (but are not limited to) any entity controlled by the auditor or under common control or otherwise affiliated or associated with the auditor through the use of a common name or through the sharing of significant common professional resources.

The analysis for other services is split into eight categories :

1. The auditing of accounts of any associate of the company.
2. Audit related assurance services.
3. Taxation compliance services.
4. All taxation advisory services not falling within 3.
5. Internal audit services.
6. All assurance services not falling within 1-5.
7. All services relating to corporate finance transactions entered into, or proposed to be entered into, by or on behalf of the company or any of its associates not falling within 1-6.
8. All non audit services not falling within 2-7.

College mergers and partnerships under the transformation programme

A number of mergers will be created, along with partnerships and other arrangements under transformation. The Welsh Government will not be publishing specific guidance on the accounting treatment of these as they will all potentially require individual treatment. For further information with regard to the accounting standards relating to mergers and partnerships see the Association of College Accounts Direction handbook, chapter 6 section 6.23-6.45 at the following link.

http://www.aoc.co.uk/en/policy-and-advice/funding-and-finance-pensions/finance-directors/finance-guidance.cfm

Financial Reporting Standard 17 retirement benefits

The full disclosure notes required can be found in the Casterbridge College model financial statements. The model for 2012/13 can be found on the AoC website at the following link:

http://www.aoc.co.uk/en/policy-and-advice/funding-and-finance-pensions/finance-directors/finance-guidance.cfm

There have been no additional changes to FRS 17 disclosure requirements during the year.

Please note that the Casterbridge Accounts Teachers Pension Scheme disclosure narrative has been updated. Please refer to this along with any information you have from the scheme to ensure that your accounts disclosures are up to date.

Operating and Financial Review

The Operating and Financial Review may also be called the members report or the report of the Governing Body. The SORP 2007 requires the review to provide an overview of the institutions finances and operations and should follow best practice as set out in the Reporting Statement 'The Operating and Financial Review' issued by the Accounting Standards Board in January 2006.

http://www.frc.org.uk/News-and-Events/FRC-Press/Press/2006/January/ASB-Issues-Reporting-Statement-on-the-Operating-an.aspx

Extract from the SORP 2007 with regard to the Operating and Financial Review:

> 'Specifically the OFR should provide a comprehensive and balanced analysis, consistent with the size and complexity of the institution, of:
>
> (a) the development, performance and operation of the business and operation of the institution during the financial year;
>
> (b) the position of the institution at the end of the year;
>
> (c) the main trends and factors underlying the development, performance and position of the business of the institution and its academic performance during the financial year; and
>
> (d) the main trends and factors which are likely to affect the institution's future development, performance and position.

The OFR should be produced in accordance with the following principles, in that it should:

(a) set out an analysis of the institution through the eyes of the institution's governing body (or equivalent);

(b) focus on matters that are relevant to the interests of funders and financial supporters;

(c) have a forward-looking orientation, identifying those trends and factors relevant to the funders and financial supporters' assessment of the current and future performance of the institution and the progress towards the achievement of long-term academic and business objectives;

(d) complement as well as supplement the financial statements, in order to

(e) enhance the overall corporate disclosure;

(f) be comprehensive and understandable;

(g) be balanced and neutral, dealing even-handedly with both good and bad aspects; and

(h) be comparable over time.

The OFR should provide information to assist funders and financial supporters to assess the strategies adopted by the institution and the potential for those strategies to succeed. The key elements of the disclosure framework recommended to achieve this are, where significant:

(a) the nature of the institution including a description of the competitive and regulatory environment in which it operates, and the institution's objectives and strategies;

(b) the development and performance of the institution, both in the financial year under review and in the future;

(c) the resources, principal risks and uncertainties and relationships that may affect the institution's long-term financial position; and

(d) the position of the institution including a description of the long-term financing, treasury policies and objectives and liquidity of the institution both in the financial year under review and the future.

The form and content of the OFR is not prescribed, the principles set out in paragraph 26 above set a framework for the disclosures to be provided by the governing body (or equivalent) in the OFR. The institution's governing body (or equivalent) should consider how best to use the framework to structure the OFR and the precise content, including the level of detail to be disclosed, relating to the key elements set out in paragraph 27, given the particular circumstances of the institution.'

The OFR can also include sustainability reporting focusing on big impacts, with numerical information if there are good quality metrics available, together with a narrative. HM Treasury guidance on sustainability reporting includes usage of water, gas , electric, waste and emissions.

Any institutions that are registered charities must make specific reference in their OFR as to how they meet the 'public benefit test' from the Charities Act 2011.

Annex H: Recent financial reporting developments

The Accounting Standards Board (ASB) of the Financial Reporting Council published on 30 January 2012, Financial Reporting Exposures Drafts (FREDs) 46 to 48 setting out the revised proposals for the future of financial reporting in the UK and Republic of Ireland. The exposure drafts were as follows:

- FRED 46 ‘Application of Financial Reporting Requirements’ (draft FRS 100);
- FRED 47 ‘Reduced Disclosure Framework’ (draft FRS 101); and
- FRED 48 ‘The Financial Reporting Standard applicable in the UK and Republic of Ireland’ (draft FRS 102)

The revised proposals recommend:

- replacing all extant FRSs (Financial reporting standards), SSAPs (Statements of Standard Accounting Practice) and UITF (Urgent Issues Task Force Abstracts) with a single FRS
- introducing a reduced disclosure framework for the financial reporting of certain qualifying entities
- retaining the ‘Financial Reporting Standard for Smaller Entities’ (FRSSE) and updating it following planned changes at EU level to financial reporting requirements for small companies.

The proposal for an adaption of the IFRS for SMEs to replace current FRSs remains the same.

On 22 November 2012, the FRC issued its first accounting standards under the new UK financial reporting regime:

- FRS 100 Application of financial reporting requirements; and
- FRS 101 Reduced Disclosure Framework

FRS 100 sets out the available reporting frameworks and how an entity works out which it must or may apply. The framework sets out three types of 'Companies Act accounts', i.e., those prepared using any of FRS 101; (draft) FRS 102; or the FRSSE.

Those companies that are required to apply EU-IFRS by law or regulation will continue to do so: the new framework does not impose EU-IFRS beyond the requirements of existing law and regulation but an entity may choose to adopt it. Such accounts are 'IAS accounts' as set out in the Companies Act 2006.

FRS 101 allows qualifying parent and subsidiary entities to apply the recognition and measurement requirements of EU-IFRS but with exemption from some of the disclosures. FRS 101 applies in the individual accounts only.

Both FRSs 100 and 101 apply for accounting periods beginning on or after 1 January 2015.

The final part of the new UK GAAP, FRS 102 was issued on 5 March 2013. It is also effective for periods beginning on or after 1 January 2015.

Therefore the proposals will be applicable to the FE sector for the 2015/16 financial year, but comparatives will be needed for the year before. Until such time though, UK GAAP will continue to be applicable.

Further and Higher Education SORP

The Further and Higher Education SORP (Statement of recommend Accounting Practice) and Charities SORP are being updated to reflect the changes to UK Generally Accepted Accounting Practice (GAAP) which has adopted FRS 100, 101 and 102 for financial years beginning on or after 1 January 2015. The FE/HE SORP development project is coming to an end and the draft will shortly be out for consultation with approval being sought from the ASB in 2014. The FE/HE SORP will come into force for financial year 2015/16 and consequently institutions should not apply early adoption of FRS 102. The revised SORP is being developed in order to be available in advance of the earliest date that the new standards will apply to Institutions (i.e. before 1 August 2014).