

## PLUMPTON COLLEGE RESPONSE TO JOINT AUDIT CODE OF PRACTICE CONSULTATION – PART 1

### **Question1**

***Should there be a Joint Code of practice for the SFA, YPLA, and Local Authorities?***

Answer 1

Yes, there should be a Joint Audit Code of Practice but only in respect of the Use of Public Money, i.e. the funding audit. It should not cover the wider issues listed in the second bullet point of para 9 of the Consultation Document. We believe that it should be much more limited in scope than the current FE Audit Code.

It seems to us entirely reasonable that the Accounting Officers of public sector funding agencies accountable to Parliament for use of Voted Funds should look for assurances on the regular and proper use of grant funding, ie that the grant is applied for the purposes intended. This is particularly so in the case of Grant-in-Aid, because of its special characteristics, but it also applies to other grant funding which is not tied to specific performance or delivery requirements.

Where payments are made on the basis of a contract or grant tied to specific performance – for example apprenticeships where the payment is made only on evidenced completion of individual apprenticeships - the assurance should lie primarily in the terms and conditions of the contract or grant, or – as in envisaged in the proposed Approved Supplier Register for post-16 providers – through a prequalification process. Although we would not object to such payments coming within the ambit of the Joint Code of Practice for the purposes of sharing information between funding bodies, the actual funding audit arrangements should be much lighter in these cases.

We do NOT support a Joint Audit Code of Practice in respect of other institutional audit and assurance requirements, eg internal control, internal audit, appointment of external auditors, etc. In our view codes dealing with wider aspects of institutional audit like these are likely to be more effective if they are tailored to the particular sector. And more efficient too, because it should be easier to integrate them into the respective wider governance frameworks. We concur with the judgement reached by LSC in 2004 and reflected at para 26 of Supplement A of their 2004 Code of Practice that “Providers are subject to many other reviews ... the scope and objectives of these reviews are often little related to the LSC’s assurance needs and reciprocal ... arrangements are unlikely to be meaningful.”

We note that the principle of parallel Audit Codes has already been accepted in respect of universities (para18), and we argue that this should also apply to the other types of provider. In the case of FE Colleges we urge that a separate Audit Code of Practice should be incorporated into the proposed FE governance code on a comply-or-explain basis – (perhaps with backstop regulatory powers in respect of colleges with financial controls that are identified as less than Good). Elsewhere the Audit arrangements should in our view be dealt with under existing local authority practice in respect of schools and other non-incorporated providers; charity regulation (in respect of non-exempt charities); or the Combined Code (in respect of PLCs).

## **Question 2**

### ***Should the Joint Code of Practice cover all types of Learning Provider?***

Answer 2

Yes, in respect of Use of Public Money, and the Joint Code of Practice must be applied even-handedly as between different types of provider.

As we argue above, there may be a case for lighter assurance arrangements in respect of public money paid for specific performance than for money paid as Grant-in Aid or as grants not tied to specific performance. But we have real and fundamental difficulties with the proposition at para 25 of the Consultation Document that audit requirements in respect of Use of Public Money should discriminate between different types of provider (as distinct from different types of provision). So for commercial and charitable providers it is not, in our view, enough simply to get assurance that the “provider has legitimately earned the funds by delivering learning”: the funding agencies should seek assurance that the grant, all the grant, has been regularly and properly applied for the purpose it was provided irrespective of the corporate status of the provider. This applies to universities and other HE institutions, too: in respect of use of FE funding, we do not believe they should benefit from a separate (and less than fully transparent) assurance regime. Likewise where these providers receive FE capital grants there should be similar audit arrangements to ensure clawback on subsequent disposals of assets funded by public grant.

Audits of regularity and propriety add not insignificant costs to college provision. If commercial and charitable providers (or HE institutions) are to be excused these assurance costs in respect of public funds, it would in our view constitute an anti-competitive feature. This may not have mattered too much in the past when colleges were largely funded by grant-in-aid. But with more and more provision being subject to tendering, and with an increasingly competitive market-place open to all types of providers, discriminatory audit requirements may lead to challenges on the part of colleges, including complaint to the EU Commission where the funds in question are related to ESF programmes or matching funds.

## **Question 3**

### ***Do you agree with the principle of one provider, one funding assurer?***

Answer 3

Yes, in respect of Use of Public Money. We agree with the principles set out at para 10, and the lead arrangements at para 13, subject to regular and transparent review that the Joint Audit Code of Practice is indeed being applied even-handedly to all recipients of FE grant irrespective of their corporate status and irrespective of their location. This is important if the sector’s confidence in the arrangements is to be sustained. The peer reviews of the JACP by mutual agreement envisaged at para 31 are not enough. The working of the JACP should be independently reviewed at three-yearly intervals (by the Audit Commission?) and the results published.

Para 14 refers to other DCSF funding paid to schools. We are concerned about capital funding channelled to schools other than through YPLA. We look for assurance that the audit arrangements for such funding streams, including matters such as clawback, will be harmonised as far as possible with the Joint Code of Practice.

#### **Question 4**

#### **What level of guidance should the SFA, YPLA and Local Authorities issue to learning providers on assurance matters?**

Answer 4

The minimum necessary to discharge statutory, legal and regulatory responsibilities.

As we explain in answer to Q1 above, we do not agree that the Joint Audit arrangements should apply outside the need for funding audits of the Use of Public Money. In particular they should not apply to audit of wider institutional aspects, such as financial statements, internal control systems, governance, appointment and management of auditors, etc. These should be dealt with under separate but parallel codes for each type of provider. We note that this will be looked at again more fully in the context of the Part 2 Consultation later this year. The Corporation at Plumpton believe that most of the institutional issues in the current LSC Audit Code of Practice for FE Colleges should be covered as an integral part of the FE Governance Code that is currently under consideration, (just as the audit arrangements of PLCs are dealt with in the Combined Code).

Para 25 of the Consultation Document asserts that the public interest in FE colleges justifies the extension of assurance needs to the college's "system of internal control, whether expenditure has been regular and proper, and whether accounting arrangements have been adhered to"; and that this need for wider assurance reflects the fact that the funding body is also the college's regulator. There may be a few Colleges where weaknesses in internal control systems have been identified, and in these cases we agree that the SFA, as a sponsoring body, should seek more detailed assurances that the weaknesses are being put right. We discuss this more fully in answer to Q5 below. But for the generality of colleges we disagree with the assertion at para 25. We explain why in the following paragraphs.

Regularity and Propriety. The current assurance arrangements largely date from incorporation, when colleges were for some years classified as public sector bodies and their whole expenditure (not just publicly funded provision) was scored as public expenditure. But colleges have for over 10 years been classified as outside the public sector, and we believe it no longer appropriate to apply Government Accounting concepts such as Regularity and Propriety to colleges' commercial business or to the income derived directly from employers, students, or charities. We have similar difficulties with the concept of the Principal continuing to be classified as an Accounting Officer with particular personal responsibility for regularity and propriety, when the reality is that all aspects of internal control, including regularity and propriety, are firmly vested in the Corporation. Perpetuating the application of the Government Accounting framework to the entire business of FE Colleges, at the same time as imposing upon them the governance requirements of both the Combined Code and the Charity Acts is a recipe for muddle. The Corporation at Plumpton believe this externally-induced muddle is itself now the biggest weakness in our internal control arrangements.

In the case of land-based colleges a high proportion of income is from private sector sources. At Plumpton LSC grants accounted for only half our income in 2007 and 2008, and our strategy is to reduce this proportion further in the coming years. Not only are we classified as being outside the public sector for Government Accounting and borrowing purposes. That is also the business reality.

We recognise that there is public interest amongst the communities we serve in how soundly we manage our finances, in the value for money we provide, and in our

investment priorities for the future. (We deal with over 40 bodies with regulatory powers or a say over how we conduct our business.) But this wider interest does not call for, and is not satisfied by, the degree of continuing SFA regulation and audit envisaged in the consultation document. What is required in our view is a much fuller regular public report to all our stakeholders about our performance, governance, and internal control procedures than is currently envisaged by the Casterbridge model of the College Annual Report; and this is what the Corporation at Plumpton has sought to deliver in each of the last four years (see the Plumpton website).

Accounts Direction. In some respects the LSC's current regulations have actually got in the way of the more transparent accountability we wish to offer to our wide range of stakeholders. For example the Accounts Direction is highly prescriptive as to the degree of detail we are allowed to provide in our accounts and how our income streams are described. One specific effect of this is that we find ourselves reporting as "Other Income" or "Other Expenditure" significant streams of income or cost which we believe should be separately identified, particularly in those cases where they Corporation wish to comment on them in the Annual Report. This, and some arcane accounting requirements eg the treatment of capital payments, makes our accounts quite impenetrable to many of our stakeholders, and indeed to many of our own Governors. Apart from the frustrations this causes, checking our compliance with the detail of the Casterbridge model adds to the effort required of our external auditors, and hence to our costs. The business of land-based colleges, the make-up of our income and expenditure, is now significantly different from that of General FE colleges and even more so from that of Sixth Form Colleges. We recognise the need, as statutory corporations, for a statutory Accounts Direction. But it is no longer appropriate to impose a single, prescriptive accounts format on different types of college.

The Accounts Directions for FE Colleges are much more detailed and prescriptive than applied by sponsoring departments to other statutory bodies classified as falling outside the public sector, and indeed than applied to most statutory bodies that do fall within the public sector classification.

It might be argued that LSC and its successor bodies require a prescriptive detailed Accounts Direction in order to allow them to cross-compare the financial performance, value for money, and efficiency of FE colleges. We disagree, on several grounds. First, the Annual Accounts are not an effective mechanism for such micro-monitoring and comparison, because of the different cost accounting treatment applied to particular expenditures in different colleges and the different judgements applied by different Corporations to provisions, eg for depreciation. To benchmark their own performance, most colleges are now using focused peer reviews rather than the material generated by LSC from the Annual Accounts. Secondly, the usefulness of the Accounts for cross-comparison has been largely overtaken by the introduction of the Framework for Excellence, which is essentially a statistical exercise and subject to much less audit than the Accounts Direction. And thirdly, as the Framework for Excellence recognises, there is a need to monitor the financial performance, effectiveness and efficiency of all providers, not just FE colleges: it is not appropriate to single out the accounts of colleges for such heavy-handed accounting regulation.

We wish to have the flexibility to determine the segmentation of our business income and the analysis of our costs in the way that we believe is the most informative to all our stakeholders. In our view that means replacing the Casterbridge model with a simpler Accounts Direction that requires colleges to prepare their accounts to a high professional standard and in accordance with the FE Code of Governance; an Annex

to the FE Code of Governance would set out those matters which should normally be disclosed in the Report and in the Accounts, and would be supported by a corpus of good practice notes developed by the sector which would be available to colleges for benchmarking and peer review purposes.

As regards Internal Control, we recognise the need for sponsoring departments to be satisfied that the statutory bodies which they oversee comply with statutory requirements, including, in the case of FE Colleges, the statutory requirements on Corporations to ensure effective and efficient use of resources, solvency, and the safeguarding of assets. This sponsorship function is quite distinct from the responsibility of a funding body to ensure the regular and proper use of public money and its value for money; and the Consultation Document is wrong to conflate the two functions into one.

In our view the degree of continuing assurance and audit implied by para 25 of the Consultation Document goes well beyond what is required for effective discharge of the Department's sponsoring function. Corporations should be expected in their Annual Report to give a full and published account of their internal control systems for meeting their statutory duties, and should set out the risks they see and how they are controlling them. But for the generality of colleges there should not be a need for large-scale supplementary assurance and audit every year in respect of these duties along the lines of the current very burdensome Financial Management and Control Evaluation. The scale and frequency of supplementary reporting should be risk-based (see response to Q5).

Colleges are exempt charities under the Charity Acts. It might be argued that LSC and its successor bodies need to regulate College's total income and finances in their capacity as the Regulator under the Charity Acts legislation. However the degree of regulation over Internal Control, Regularity and Propriety, and Accounting Arrangements envisaged here go well beyond what the Charities Commission require from Non-Exempt charities, and in our view go well beyond the purposes of the Charity Acts. We note in any case from para 8 of the Consultation Document that the requirements of the Charity Acts legislation are not considered in the present consultation.

#### **Question 4a**

***Which areas of assurance activity would you welcome guidance on, if any?***

Answer 4a

In respect of Use of Public Money, the issues include

- Will colleges' 14-19 business will be funded by grant-in-aid or grant from local authorities from April 2010? (We understand that grant-in-aid is not a vehicle normally available to local authorities, and anyway does not sit so easily with the concept of annual commissioning envisaged in the proposed commissioning framework)
- Para 3.2.3 of the National Commissioning Framework Consultation Document refers, in connection with reconciliation and in-year adjustment of funding, to the need for in-year validation of how much the provider has earned through an audit of the provider's delivery. How will this work? When in the year will it be carried out? Is independent audit envisaged? How can speed in adjusting allocations be assured?
- Framework for Excellence is envisaged as an important tool for commissioning. How will the data fed into FfE be audited? In particular, how

and by whom will assurance be obtained that the success rates and other performance indicators are being calculated consistently by all providers?

- Capital grants are likely to be much lower than in the past. Nevertheless it would be helpful to understand how the LSC's successors propose to audit future capital grant expenditure.

In respect of guidance about the audit and assurance on institutional matters (i.e. other than Use of Public Money), we believe the starting points should be the Combined Code and the requirement in the statutory Articles for an Audit Committee. The vehicle should be the FE Code of Governance, in which a separate section should be reserved for an FE Audit Code of Guidance. The FE Audit Code of Guidance would be drawn up essentially by the sector itself in discussion with the SFA, and it would be for the sector itself to propose subsequent changes. Assurance should be through "comply-or-explain" reporting in the Corporation's Annual Report. The requirement in the Articles for the Audit Committee to "operate in accordance with any requirements of the LSC" does not reflect the more autonomous governance arrangements now being developed, and should be dropped. The FE Audit Code of Guidance would be much shorter and less prescriptive than the current LSC Audit Code.

We envisage that the FE Audit Code of Guidance, (or perhaps the FE Code of Governance itself), would include guidance on:

- Audit Committee membership (the stipulation in the current LSC Code that members of the Audit Committee should not also be members of the finance committee prevents the best use of scarce financial talent amongst governors, is not normal practice elsewhere, and should be dropped);
- On Audit Committee terms of reference and responsibilities (the minimum cycle of audit committee business is too prescriptive, and should be replaced by good practice notes prepared by the sector for benchmarking purposes);
- The role and relationships of Internal Audit (the requirement to comply with the Government Internal Audit Standards should be replaced by references to good practice guides drawing on the private as well as the public sector.);
- The need for an agreed, risk-prioritised IA strategy (but dropping the prescriptive mandatory requirements at Annex C of Schedule B of the current LSC Code),
- The appointment, payment and oversight of external auditors (in line with the Combined Code).

Other parts of the FE Governance Code would deal with Internal Control, Risk Management, and the Annual Report and Accounts. The statutory Accounts Direction would, as discussed above, be more focussed on process and purposes than the specifics of content; and the prescriptive Casterbridge model would be dropped.

#### **Question 5**

***Should assurance work be consistent for similar types of learning provider, and proportional in approach (that is, with lower risk providers receiving less assurance coverage)?***

Answer 5

No, assurance work in respect of use of public money should be consistent across all recipients of grant,. The funding audit should be consistent for similar types of learning provision, irrespective of the corporate status of the provider.

As regards audits of institutional controls and standards, our responses to QQ4 and 4a set out the much lighter touch we believe is now appropriate for the generality of FE colleges. We recognise that there will however be a small minority of colleges, where weak finances, poor management, or poor controls pose a material risk to the Corporation's ability to carry out its statutory functions and/or to deliver the provision for which it is receiving, or is about to receive, public money. These risks may be identified through the Annual Report, or the Framework for Excellence returns, or the reports of auditors, or as a result of failures in respect of publicly-funded provision. In these cases, but only in these cases, we agree that the SFA as the FE sponsoring body should call for supplementary assurance and audit.

The form that such supplementary assurance and audit should take, and how long it needs to remain in place, will depend on the individual circumstances. But for colleges that are in danger of insolvency, the SFA should be asking for more frequent information (monthly?). And for colleges with internal controls that are considered inadequate, the SFA should be much prompter in installing their own adviser on the Governing Body.