Scotland's colleges 2016

AUDITOR GENERAL

Prepared by Audit Scotland
August 2016

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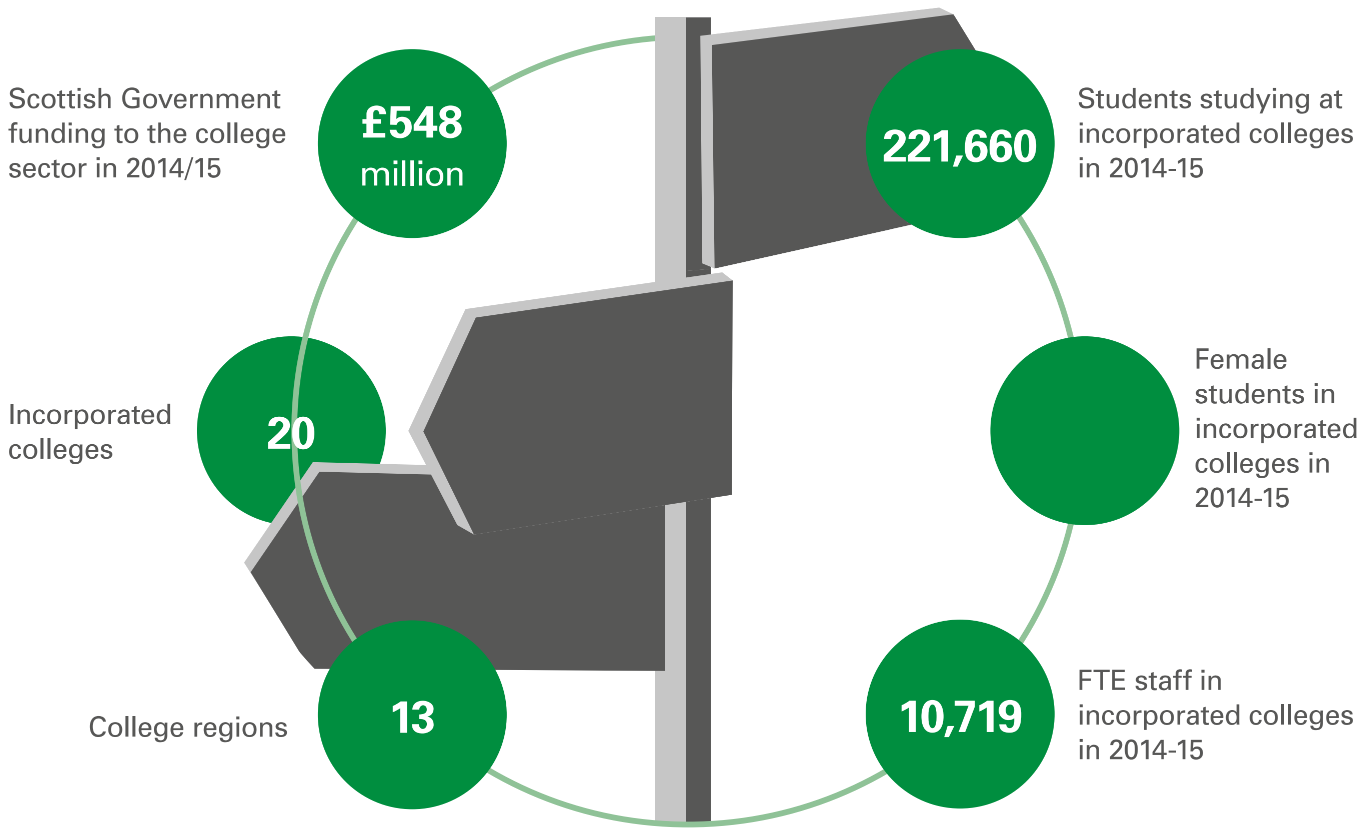

Scottish Government funding to the college sector in 2014/15
£548 million
221,660
Students studying at incorporated colleges in 2014-15
Incorporated colleges
20
Female students in incorporated colleges in 2014-15
College regions
13
10,719
FTE staff in incorporated colleges in 2014-15

Summary

Key messages

1 The college sector has continued to exceed activity targets but colleges are still adjusting to substantial changes that affect how they operate. The Scottish Government has not yet clearly articulated how it will measure and report the benefits of its programme of reform, and some of its proposed measures lack baseline information. The Scottish Funding Council (SFC) intends to publish its estimate of the total costs of mergers in August 2016. However, this will not include costs of harmonising staff terms and conditions, which could be significant. Only one of the three regional bodies was able to perform the role expected of it in 2014-15 and 2015-16.

2 The number of under-25 year olds in full-time education at college has increased by 14 per cent in the last eight years. Student numbers overall have decreased by 41 per cent over the same period, and part-time students by 48 per cent. Most of the reductions in student numbers have been among women and people aged over 25. The gender balance is now broadly equal overall but there are significant differences between subjects. The overall percentage of full-time further education students successfully completing their course increased year-on-year between 2009-10 and 2013-14, from 59 to 66 per cent, but dropped to 64 per cent in 2014-15. At least 82 per cent of students who left in 2013-14 went on to a positive destination.

the college sector has continued to exceed activity targets but colleges are still adjusting to substantial changes

3 Full-time equivalent staff (FTE) numbers decreased by nine per cent between 2011-12 and 2013-14 and increased by five per cent in 2014-15. Staff feedback on the impact of mergers is mixed.

4 The overall financial health of the sector is relatively stable. Our analysis indicates four colleges with underlying financial challenges. Colleges do not have long-term financial plans which would help them prepare for and address further financial pressures, such as national collective bargaining, estate maintenance and student support funding. The Scottish Government's current approach to funding colleges for depreciation is complex, and creates a degree of uncertainty for colleges.

5 The College Good Governance Task Group's recommendations should mitigate the risk of significant governance failures. While the SFC undertakes a range of monitoring and engagement within the college sector, this has not always resulted in timely and effective resolution of problems and issues. Despite the many changes in accountability arrangements in the sector, the Scottish Government has not

undertaken a comprehensive review of the SFC's role in the last ten years. The Scottish Government's end-to-end review of the enterprise and skills agencies in Scotland provides an opportunity to re-examine and clarify the SFC's role.

Recommendations

The Scottish Government and the SFC should:

- specify how they will measure and publicly report progress in delivering all of the benefits that were expected from regionalisation and mergers, in line with our recommendation from last year, which was endorsed by the Public Audit Committee
- publish information on the costs and savings achieved through the merger process, in line with our recommendation from last year, which was endorsed by the Public Audit Committee
- work with colleges to determine the current condition of the college estate and prepare a plan to ensure that it is fit for purpose
- use the Scottish Government's end-to-end review of the skills agencies in Scotland to re-examine, clarify and set out the role of the SFC, particularly in relation to college governance
- identify and implement a better approach to allocating depreciation budgets to colleges.

The SFC should:

- require colleges to report how they have spent depreciation cash funding in their accounts, including a breakdown of the spending
- explore with colleges a way to better assess demand for college courses across Scotland
- publish information about leaver destination at national, regional and college levels.

Colleges should:

- develop long-term (a minimum of five years) financial strategies. These should be underpinned by medium-term (between three and five years) financial plans that link to workforce plans and take account of significant financial pressures such as national collective bargaining, estate development and maintenance and student support funding
- implement a more systematic approach to workforce planning to ensure that they have the appropriate resources and skills to achieve their strategic goals

- make agendas, supporting papers and minutes (subject to confidentiality issues) for board and committee meetings publicly available within appropriate timeframes.

Glasgow Colleges' Regional Board should:

- put in place the arrangements necessary to become fully operational.

About the audit

1. This report provides an update on the various changes taking place in the college sector and, where possible, assesses their impact. It also comments on the financial standing of the sector and looks at student participation and outcomes. We set out our methodology in Appendix 1.

2. We use the term 'reform' in this report to cover mergers and regionalisation. The Scottish Government's reform programme has led to college mergers. The Post-16 Education (Scotland) Act 2013 included provisions to support the reform of the sector into 13 regions, including arrangements for how the merged colleges were to be run. There are a total of ten colleges formed through mergers, with City of Glasgow College having formed in 2010. The number of incorporated colleges decreased from 37 in 2011-12 to 20 in 2014-15. Appendix 2 provides an illustration of the current structure of colleges in Scotland.

3. Unless we state otherwise, all financial figures in the body of this report are in real terms, that is, allowing for inflation.

4. Colleges prepare their accounts based on the academic year (1 August to 31 July). This differs from the Scottish Government's financial year which runs from 1 April to 31 March. To help provide clarity, we use the convention '2014-15' when referring to figures from colleges' accounts, or relating to the academic year; and '2014/15' when referring to funding allocations made in the Scottish Government's financial year.

Part 1

Progress with reform

Key messages

1 Colleges are still adjusting to substantial changes that affect how they operate. Funding reductions, regionalisation, college mergers, reclassification, national collective bargaining and the implementation of a new funding model are some of the significant changes with which colleges are dealing.

2 The Scottish Government has not yet clearly set out how it will measure and report the benefits of its programme of reform. Some of its proposed measures lack baseline information. While the SFC completed all post-merger evaluations of colleges that merged in 2013-14, these did not provide a clear assessment of change. The SFC intends to publish its estimate of the total costs of mergers in August 2016. However, the total will not include the costs of harmonising terms and conditions, which could be significant.

3 Three of the 13 college regions are multi-college regions. These multi-college regions have regional bodies, intended to provide strategic direction and allocate funding and activity to colleges in the region. Only one of the three regional bodies was able to perform the role expected of it in 2014-15 and 2015-16. The costs of two of these regional bodies are not separately identified in published accounts.

only one of the three regional bodies was able to perform the role expected of it in 2014-15

Colleges are continuing to adjust to substantial changes that affect how they operate

5. Colleges are still adjusting to a number of significant changes that have taken place in recent years (Exhibit 1, page 10):

- The Post-16 Education (Scotland) Act 2013 included provisions to support the reform of the sector into 13 college regions, three of which are multi-college regions with regional bodies.
- Regionalisation led to college mergers. There are now 20 incorporated colleges across Scotland (see Appendix 2).
- In 2012, the SFC introduced regional outcome agreements (ROAs) to set out the aims and expectations for each region. These agreements specify the activities that regions will deliver in exchange for funding.

- The Office for National Statistics (ONS) reclassified colleges as public sector bodies with effect from April 2014, with implications for how colleges manage and report their finances.
- Changes in funding policy to prioritise full-time student places that lead to employment, reflecting the Scottish Government's response to the impact of the 2008/09 economic crisis.
- Colleges have an ongoing role in responding to the recommendations of the Commission for Developing Scotland's Young Workforce.[1] Colleges have been asked to place a particular focus on working with both schools and employers to facilitate the effective progression of young people from education into employment.

While not all colleges have merged, the other changes have affected all colleges.

6. Further changes lie ahead:

- The new further and higher education statement of recommended practice (SORP) will change how colleges report their finances from 2015-16 (see paragraph 76).
- Education Scotland and the SFC plan to implement, in August 2016, a new approach to providing assurance on the quality of leadership, teaching and learner attainment. The new approach also aims to promote improvement and innovation.
- The SFC is implementing a new funding model (see paragraphs 72 and 73).
- The sector has introduced national collective bargaining with staff trades unions.[2] Previously each college separately negotiated staff pay, terms and conditions (see paragraph 65).

7. Most aspects of merger have been completed by merged colleges. At the time of our audit:

- All ten merged colleges had reviewed their curriculum.
- Fife College had still to fully integrate its IT systems.
- City of Glasgow College had still to fully harmonise staff terms and conditions. It has halted local job evaluations so that this work can be completed nationally as part of national collective bargaining.

It remains unclear how much of the savings from reform are a direct result of college mergers

8. The SFC estimates the sector will deliver efficiency savings of £50 million from reform by 2015-16. In response to our report last year, the Scottish Parliament's Public Audit Committee (PAC) sought greater clarity from the Scottish Government and SFC on when detailed figures could be provided and when the £50 million of savings will be achieved. The SFC responded in January 2016 stating that the sector is on track to achieve the £50 million savings by 2015-16. These projected savings are based on the sector providing a slightly increased

Exhibit 1

Changes affecting the college sector

College sector reform and other changes have had a number of far-reaching consequences.

Source: Audit Scotland

level of activity with around the same level of funding. The savings arise mainly from a real-terms reduction in funding to the sector as a whole and not just merged colleges. Therefore, as we reported last year, it remains unclear how much of these savings are as a direct result of college mergers.

The Scottish Government and the SFC still have not set out how they will measure and report the benefits of mergers

9. The Scottish Government expected college mergers to lead to a number of benefits:

- improved engagement with local employers to better understand their needs
- efficiencies through reduced duplication and unnecessary competition
- better outcomes for learners.

10. Last year, we reported that the Scottish Government and SFC had not specified how they would measure the expected benefits of mergers.[3] The Scottish Government informed the PAC in December 2015 that it would work with the SFC to report the benefits, costs and savings of mergers, based on the SFC's two-year post-merger evaluations of colleges which merged in 2012-13 and 2013-14. Despite the final college merger taking place two years ago, the Scottish Government and the SFC have still not publicly set out when the benefits will be achieved and how they will measure them.

11. Colleges have reviewed their curricula to reduce duplication and support students' progression to employment or further study. While the SFC's post-merger evaluations include commentary on changes to curricula, they do not provide any indication of how significant these changes have been, ie how many courses have been combined. The evaluations comment on how merged colleges are working with employers, but they do not assess whether this is better than it was before merger. We contacted four employer representative groups to seek their views. The two groups that responded (the Federation of Small Businesses and the Scottish Council for Development and Industry) told us that, while they supported the regional approach, there was variable evidence that it had changed how colleges were engaging with their members and responding to the labour market. The Federation of Small Businesses suggested that having a better understanding of employers' skills needs and involving employers in curriculum reviews would help colleges deliver improvements.

12. The Scottish Government told us it intends to use five broad outcome areas to measure better outcomes for learners: attainment, retention, articulation (students progressing to university), positive destinations and student satisfaction. It has not specified what indicators it will use to measure these outcomes. While trend information is available for retention, attainment and articulation rates, positive destinations and student satisfaction lack baseline information. Destination data was published for the first time for students leaving college in 2013-14 following a recommendation from the PAC last year (see paragraph 47). A pilot student satisfaction survey has now been undertaken (see paragraph 48). The lack of published trend information means it will not be possible to identify whether mergers led to improvements. In developing outcome indicators, the Scottish Government should align these to its economic strategy and the national performance framework. We discuss student participation and outcomes in Part 2.

The SFC's two-year post-merger evaluations do not provide a clear comparison of colleges before and after merger

13. Between September 2015 and June 2016, the SFC carried out post-merger evaluations of the eight colleges that merged in academic year 2013-14. The SFC will use these to inform a report on overall progress which is due to be published in August 2016. Based on the evaluations to date, feedback from staff and students was mixed, with examples of benefits and concerns expressed in all colleges. We discuss the impact of mergers on staff and students in Part 2.

14. The SFC completed its two-year post-merger evaluations to agreed timescales. Each evaluation drew on:

- a self-evaluation submitted to the SFC by the college
- Education Scotland's intelligence and review work (including external reviews and annual engagement visits)
- SFC monitoring of the college's regional outcome agreement and finances
- SFC meetings with staff, students, union representatives, external stakeholders (including employers), senior management and the college board.

15. While the post-merger evaluations were based on a range of evidence from different sources, they lack baseline information to compare how a college has changed following merger. For example, they refer to employer engagement events as evidence of improvement but make no comparison with engagement pre-merger. Our 2015 report found that colleges had not detailed in their merger business cases how they would measure the benefits. The SFC did not specify at the time of mergers what comparative information and data it needed from colleges for the post-merger evaluations. As a result, there is no baseline information on employer engagement and some aspects of outcomes for learners such as positive destinations and student satisfaction. Colleges have also found it difficult to identify savings resulting directly from mergers because of the significant amount of change more generally in the sector.

The SFC intends to publish its estimate of the total costs of mergers in August 2016 but it will not include the costs of harmonising terms and conditions

16. The PAC endorsed our recommendation last year that the Scottish Government and the SFC should publish financial information on the costs and savings achieved through the merger process. The SFC provided around £59 million to colleges that merged. Most of this (£45 million) was used to fund voluntary severance payments. Colleges also used their own funds towards the costs of mergers. Some colleges provided the SFC with cost information as part of the post-merger evaluations. However, this did not include all of the costs of merger, such as the costs of harmonising employee terms and conditions. Therefore there is currently no comprehensive analysis of the cost of mergers incorporating: college contributions to severance payments; the integration of IT systems; harmonisation of terms and conditions; management time to plan and implement mergers; and specialist advice, such as legal services.

Only one of the three regional bodies was able to perform the role expected of it in 2014-15 and 2015-16

17. Colleges are organised into 13 college regions, of which ten are single college regions (Appendix 2). The college boards in single college regions have been designated as regional college boards. Regional college boards are responsible for planning the further and higher education that colleges will deliver and providing strategic direction within the region. In the three multi-college regions (Glasgow, Highlands and Islands, and Lanarkshire), the individual colleges are 'assigned' to the regional strategic body (regional body). This body is responsible for planning their assigned colleges' further and higher education, funding them and monitoring how they perform. The board at each assigned college continues to be responsible for the governance, financial management and operation of the college. Colleges in multi-college regions are still accountable to the SFC in a number of areas, such as financial reporting, but they are also accountable to their regional body. We reported last year that introducing regional bodies has resulted in a complex framework of accountability.

18. The three multi-college regions are arranged differently from one another:

- Glasgow – The region has three assigned colleges: City of Glasgow, Glasgow Kelvin and Glasgow Clyde colleges. Glasgow Colleges' Regional Board (GCRB) was established in May 2014 as the regional body. The chairs of the three colleges are members of the GCRB board. The college principals attend GCRB board meetings but are not members.

- Highlands and Islands – The region has five incorporated colleges (Perth, Inverness, North Highland, Lews Castle and Moray colleges) and a further three non-incorporated colleges (Shetland, Orkney and West Highland). All eight colleges are academic partners within UHI.[4] The University of Highlands and Islands (UHI) was established as the regional body in August 2014, and existed prior to regionalisation. To separate the governance of its higher and further education responsibilities, UHI has established a committee of its Court, the Further Education Regional Board (FERB), to support it in its regional body role. Chairs of the eight colleges are members of the FERB. College principals are not members but may be invited to attend meetings for specific items. UHI has a number of working groups looking at specific regional operational issues, such as financial monitoring. Exhibit 2 (page 15) shows the complexity of these arrangements compared to what existed before regionalisation.

- Lanarkshire – There are two colleges in the region. New College Lanarkshire is a regional college. South Lanarkshire College is assigned to New College Lanarkshire. The Board of New College Lanarkshire (referred to as the Lanarkshire Board), established in October 2014, has a dual role as the college's board and as the regional body. The Lanarkshire Board was enlarged to include members from South Lanarkshire College in recognition of its responsibilities for that college. This includes the chair and principal of South Lanarkshire College.

19. All regional bodies have associated costs such as the chair's remuneration, members' expenses, recruitment and other administrative support costs. This is funded from each region's total allocation from the SFC. The costs of Lanarkshire and Highlands and Islands' regional bodies are amalgamated in the accounts of

New College Lanarkshire and UHI, respectively, but are not separately identified. Although this is in line with reporting requirements, the separate reporting of the costs of running the regional bodies within the UHI and New College Lanarkshire accounts would improve transparency. UHI informed us that the costs of running its regional body in 2014-15 were around £190,000 while New College Lanarkshire stated its regional body's costs were £34,000. GCRB reports its accounts separately. It spent around £280,000 between May 2014 and July 2015.

20. The terms of the Further and Higher Education (Scotland) Act 2005 are set out in such a way that assigned colleges may be funded by their regional body or by the SFC. The Scottish Government’s intention is that assigned colleges should be funded by the regional body if the SFC is confident that the regional body is able to perform this task. The regional body must first obtain ‘operational fundable body’ status from the SFC in order to receive and distribute funding to colleges.[5] In making this decision, the SFC considers:

- the composition of the board of the regional body
- the board’s committee structure
- the board’s effectiveness, including its oversight of the assigned colleges
- strategic planning
- financial management
- risk management
- internal audit.

21. Despite regional bodies being a key feature of recent college reform, none of the three is yet operating as intended. At the time of our audit, UHI had secured operational fundable body status (in April 2015) but it is still developing some of its governance arrangements (paragraphs 22–23). In the Glasgow and Lanarkshire regions, the SFC continued to fund the colleges directly in 2014-15 and 2015-16 (paragraphs 24–26)

More than a year after securing operational fundable body status, UHI has still to fully develop its monitoring and allocation processes

22. During 2015, UHI worked on establishing a financial memorandum with its assigned colleges and academic partners and refining the membership of the FERB. These were not easy to agree and took up a lot of time. As the FERB develops, it is expected to have a more prominent role in monitoring colleges’ performance, allocating funding and activity and providing strategic direction on behalf of the UHI Court.

23. In March 2016, UHI established a strategy group to review the effectiveness of the governance structure, financial sustainability and opportunities, and the cultural change needed in the region. This group is due to complete its work in September 2016. A working group is also developing proposals for the allocation of funding and activity. Concluding this work should help UHI in its role of allocating funding and activity and providing regional strategic direction.

Exhibit 2

Highlands and Islands' college arrangements for further education provision, before and after regionalisation

The Highlands and Islands' regional arrangements are complex and involve many more groups than before regionalisation.

Before regionalisation	After regionalisation	
Scottish Funding Council Directly funds colleges on behalf of the Scottish Government	**Scottish Funding Council** Transfers funding to regional body on behalf of the Scottish Government	
	UHI Court The regional body for further education in the Highlands and Islands region. It also provides overall strategic direction and governance of the university	**UHI strategy working group** Short-life group developing strategy proposals for the UHI Court that includes further education
	Further Education Regional Board (FERB) Committee of UHI dedicated to further education in colleges. It oversees colleges' performance, allocating funding and activity and providing strategic direction on behalf of the UHI Court	**Associate principal of further education** Develops regional outcome agreement, as well as processes of oversight and accountability with college principals, is a member of FERB and reports to the UHI Court
Colleges Deliver learning activity	**Further Education Executive Board (FEEB)** Committee of the FERB, chaired by the associate principal of further education. College principals and deputy principal of the university are members	**Colleges** Deliver learning activity
Directors of finance practitioners group Develop financial monitoring	**Directors of finance practitioners group** Develop financial monitoring	**Funding working group** Developing recommendations for allocating funding and activity among colleges

Note: Blue boxes indicate permanent bodies/groups, a red box indicates a temporary group and a green box indicates an individual.

Source: Audit Scotland using information from University of Highlands and Islands

The Lanarkshire Board and GCRB have made progress in addressing governance issues but GCRB is still not operationally fundable two years after its creation

24. The Lanarkshire Board (acting as the regional body) has been addressing a number of issues raised by the SFC, including cross-membership between boards of the two colleges and consistent audit arrangements. The SFC concluded in July 2016 that the Board had satisfactory arrangements in place to fund its assigned college and the regional body became fully operational from 1 August 2016.

25. In March 2016, the Auditor General reported that, following months of deterioration in key relationships, GCRB had made limited progress towards securing operational fundable body status.[6] There were significant weaknesses in governance and an absence of key systems of assurance and internal control. Several members of the board resigned in 2015 and the Scottish Government appointed an SFC board member to act as interim chair. In December 2015, the SFC decided not to grant operational fundable body status to GCRB, pending the appointment of a permanent chair and executive director.

26. The situation has since improved. GCRB now has a permanent chair and two members of staff, an executive director and executive assistant. It has also established many of the systems of assurance and internal control needed to properly manage and oversee a public body. The SFC wants to see a period of stability and effective operation before it hands over responsibility for £80 million of funding in the region. It is now over two years since GCRB began operation, but the timescale for granting it operational fundable body status is not clear.

Part 2

Students and staff

Key messages

1 The number of under-25 year olds in full-time education at college has increased by 14 per cent in the last eight years. Student numbers overall have decreased by 41 per cent over the same period and part-time students by 48 per cent. Most of the reductions in student numbers have been among women and people aged over 25. The potential impact of a policy change on these groups was not assessed prior to implementation. The gender balance is now broadly equal overall but there are significant differences between subjects.

2 The sector has continued to exceed SFC targets for activity. The overall percentage of full-time further education students successfully completing their course increased year-on-year between 2009-10 and 2013-14, from 59 to 66 per cent, but dropped to 64 per cent in 2014-15. Retention rates followed a similar pattern. It is not possible to attribute these movements to any particular aspect of reform. At least 82 per cent of students who left in 2013-14 went on to a positive destination.

3 FTE staff numbers decreased by nine per cent between 2011-12 to 2013-14 and increased by five per cent in 2014-15. Staff feedback on the impact of mergers is mixed. Despite the significant changes that have taken place in the sector, colleges do not prepare organisation-wide workforce plans. Colleges Scotland is leading work to look at the future workforce requirements for the sector.

most of the reductions in student numbers have been among women and people aged over 25

The sector has consistently exceeded its activity targets

27. Colleges and the SFC agree targets for the amount of student learning that each college will deliver each year.[7] The sector has consistently delivered above this target each year, although the level of over delivery has fallen over time. At a regional level, nine of the 13 regions delivered above target in 2014-15, the highest being West Lothian at nearly seven per cent. Of those regions that under-delivered, all achieved at least 98 per cent of their target.[8]

Policy changes have led to an increase in full-time learning, and a steep decline in part-time learning

28. In 2009, the Scottish Government asked the SFC to focus funding on courses most likely to lead to employment. This led to less funding for courses that did not lead to a recognised qualification or were less than ten hours in duration.[9] This policy contributed to an increasing percentage of students on vocational courses and a rise of 14 per cent in the number of under-25s on full-time courses since 2007-08. However, this also contributed to a steep decline in the number of students on part-time courses.

29. In 2014-15, 221,660 students were studying at the 20 incorporated colleges. The largest college was West College Scotland, with 21,607 students, and the smallest was Lews Castle, with 1,237 students. Student numbers peaked in 2007-08 and declined by around 41 per cent between 2007-08 and 2014-15 (Exhibit 3). All colleges except West Lothian saw a decrease in overall student numbers during the period. In the last year, overall student numbers fell by six per cent. Over the same period of time, the number of FTE student places remained broadly static.

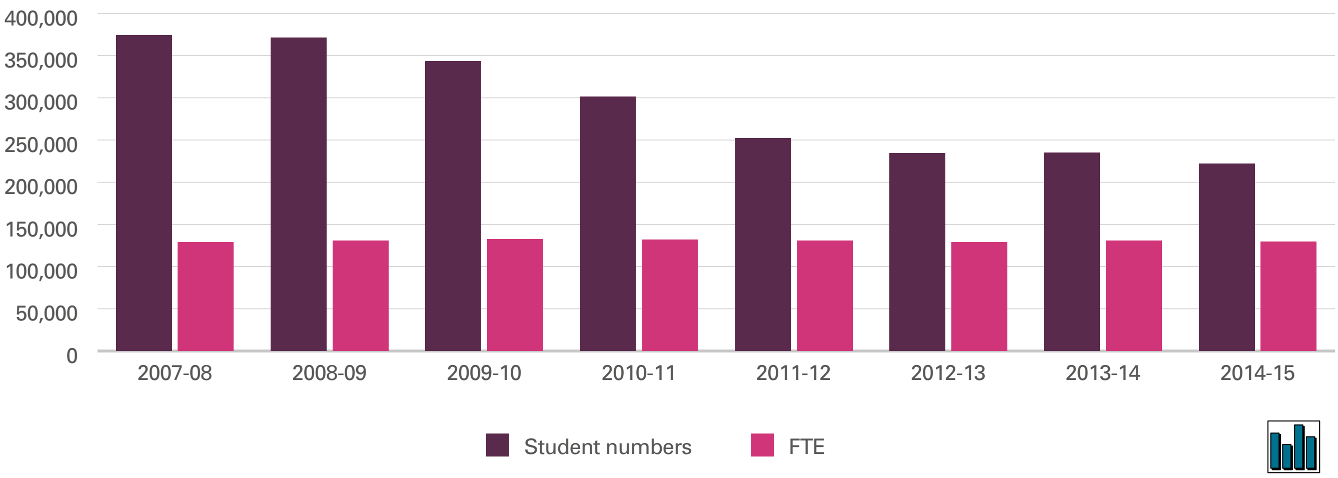
30. Following a peak in 2007-08, the number of part-time students has fallen by 48 per cent by 2014-15, from 321,281 to 165,853. During the same period, the number of full-time students increased by 18 per cent, from 66,534 to 78,318. Part-time student numbers had begun to decline when the 2009 funding change came in, but declined sharply after this.

31. There were falls in student numbers across all subjects between 2007-08 and 2014-15 (Exhibit 4, page 19). The biggest percentage falls were in printing (85 per cent), and minerals and materials (78 per cent). The Scottish Government has prioritised science, technology, engineering and maths (STEM) subjects, and these saw some of the smallest percentage falls.

Exhibit 3

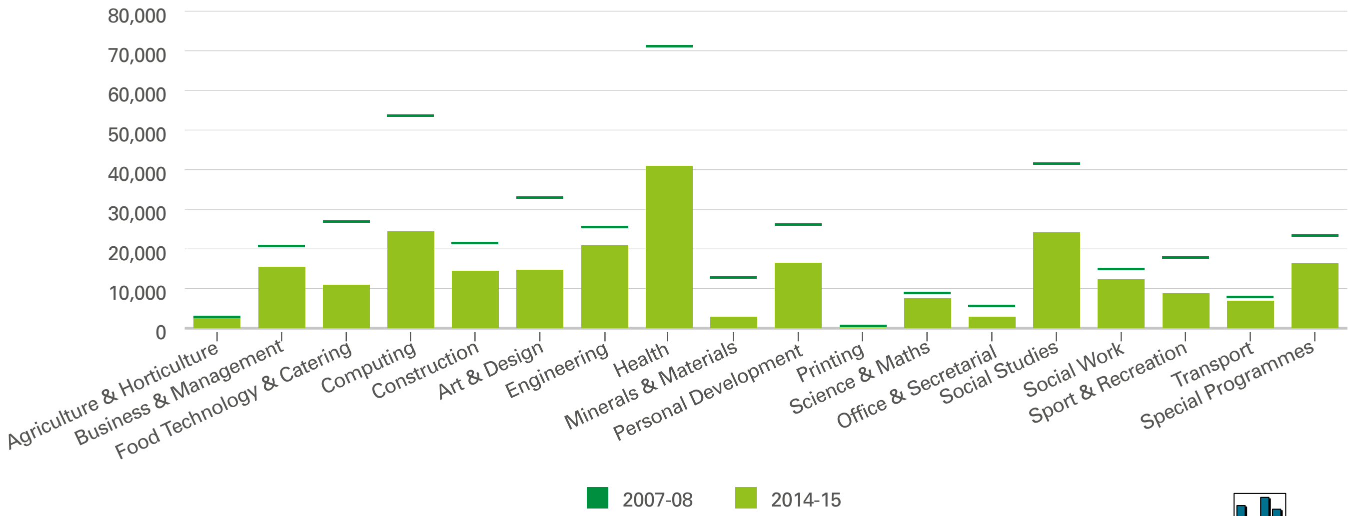
College student numbers and FTE from 2007-08 to 2014-15

College student numbers fell by 41 per cent between 2007-08 and 2014-15, while full-time equivalent rose 0.5 per cent.



Source: SFC infact database

Exhibit 4
Number of students by subject in 2007-08 and 2014-15
Computing and health are still the most popular subjects, but have had large falls in numbers between 2007-08 and 2014-15.



Source: SFC infact database

The overall gender balance among college students is broadly equal, but there are some large differences between subjects

32. The fall in part-time places following the SFC policy change has had a disproportionate effect on female students. As the number of part-time places fell, the number of female part-time students fell at a steeper rate than male part-time students (Exhibit 5). The decrease was 53 per cent for women between 2007-08 and 2014-15, compared to 43 per cent for men.

Exhibit 5
Part-time student numbers by gender from 2007-08 to 2014-15
The number of part-time female students fell by 53 per cent during the period. Part-time male student numbers fell by 43 per cent.

Source: SFC infact database

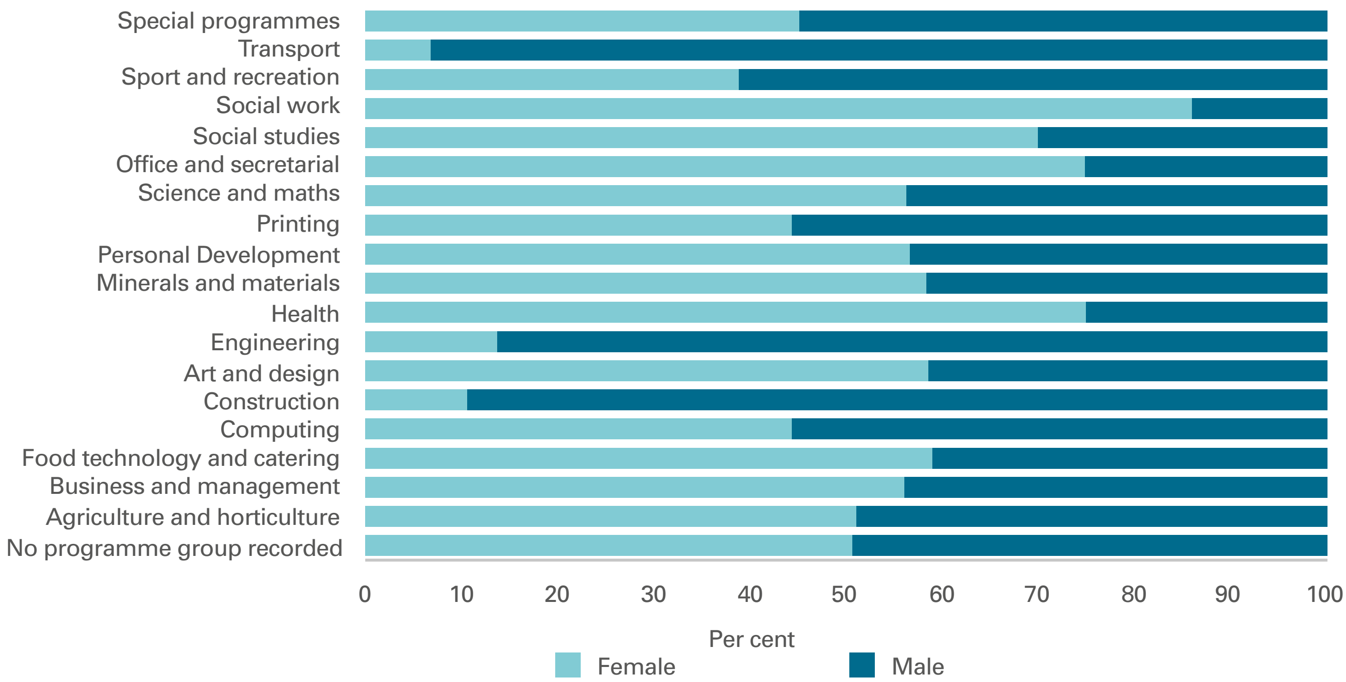
33. The number of male and female full-time students has been increasing, though the number of men fell slightly between 2013-14 and 2014-15. These changes have affected the overall gender balance of college students. Women made up 52 per cent of the total student population in 2014-15, a steady year-on-year decline from 56 per cent in 2007-08. At a college level, the gender balance varies between 45 per cent female at Glasgow Kelvin, Inverness and Lews Castle colleges, to 61 per cent female at West Lothian College. This variation across the country does not seem to reflect the general population of those areas, but may reflect course availability and local demand.

34. Although the overall gender balance was broadly equal in 2014-15, there are still large differences between subjects (Exhibit 6). The picture has remained much the same over the last ten years, particularly in the subjects with the most extreme differences, such as social work and engineering. Reducing gender inequality is a Scottish Government priority, and is being addressed through a number of policies and strategies, including the Economic Strategy and the Commission on Developing Scotland's Young Workforce. The SFC has published a report on progress with its gender action plan. This comments on how it plans to work with colleges to address these imbalances. The plan notes that gender imbalances can limit young people's individual potential, affect wages and create a system where they cannot make genuinely free choices about their future career options. A key performance indicator in the plan is to increase the minority gender share by five percentage points in the most unbalanced subjects by 2021, and to have no subjects with more than three-quarters of students being one gender by 2030. The SFC will use ROAs to specify what actions regions should take.

Exhibit 6

Male and female students by subject 2014-15

Some subject areas have large gender differences.



Source: SFC infact database

The number of older students, particularly those on part-time courses, has decreased significantly in recent years

35. Over-25 year olds are the largest age group among college students, representing 42 per cent of the student population (92,318 students). The percentage of over-25 year olds varies from 32 per cent at Ayrshire College, to 54 per cent at Dumfries and Galloway College. Students aged over 25 years experienced the largest reduction in numbers of all age groups, 51 per cent, between 2007-08 and 2014-15.[10] In 2011, the Scottish Government made its 'Opportunities for all' commitment. This involved prioritising a place in learning or training for young people aged 16-19 who are not in employment and led to an increase in the number of younger full-time students. This commitment may have contributed to this reduction, though the trend had already started when this commitment was made.

36. The number of part-time students aged over 25 years fell by 54 per cent between 2007-08 and 2014-15, from 179,685 to 82,402. The number of part-time 16-17 year olds fell by 24 per cent.

The fall in college places has had less impact on students from ethnic minority and deprived backgrounds

37. The policy changes, described in (paragraphs 28 and 35), have affected students from ethnic minorities and deprived areas less adversely than women and older students. In all these factors, there can be wide variation among colleges; in many cases, these patterns reflect the demography of the area.

38. The number of students from an ethnic minority background fell by less than the number of white students between 2007-08 and 2014-15, by 30 per cent compared to 42 per cent. The percentage of ethnic minority students has increased from five per cent to 6.3 per cent over the same period. According to the 2011 census, four per cent of the total Scottish population are from ethnic minority backgrounds.

39. The number of students from the most deprived areas also fell by less than the rest of the student population, by 24 per cent compared to 47 per cent, between 2007-08 and 2014-15. The percentage of students from the most deprived areas has increased from 17 to 22 per cent over the last ten years.

40. In 2014-15, around 13 per cent of students were recorded as having some form of disability. Trend information is less reliable in this area owing to large numbers of students being recorded as 'disability status unknown' in previous years.

The Scottish Government and the SFC did not assess the impact of all policy changes on student participation before implementation

41. The Equality Act 2010, and earlier Equality Act 2006, places duties on public bodies to use equality-impact assessments to assess the potential impact of proposals for new or revised policies or practices. This relates to characteristics like gender, race and disability. The SFC did not conduct an equality-impact assessment on the 2009 funding change (paragraph 28) that led to the fall in part-time student places. The Scottish Government did not carry out an impact assessment on its 2011 'Opportunities for all' commitment to focus on younger students, but the SFC did. The SFC identified that there was already a trend of decreasing numbers of older students at the point of the decision. While not mentioned in the impact assessment, this is likely to have been at least partly caused by the SFC's 2009 change to how it funded colleges.

42. Neither the SFC nor the Scottish Government have analysed how the fall in part-time places and the focus on younger students have affected those who have not been able to get a place at college, and what they chose to do instead. There is currently no way to tell if these decreases in student numbers reflect a fall in demand. Students currently apply to individual colleges and each college chooses how to record and classify applications. Having a national picture of demand would allow the SFC to identify levels of unmet demand. It would also allow the SFC to assess the effect of future policy changes, or changes in the wider environment, such as university admissions and employment levels. The Scottish Government and the SFC would also be able to draw on this data to inform future funding decisions. Our recent report on higher education in Scottish universities recommended that the Scottish Government and the SFC should undertake research to assess what impact the limits on funded places are having on Scottish students.[11] Without an accurate picture of total demand for Scottish colleges, it will be very difficult to assess the impact of the limits on funded places.

Further education attainment fell from 66 to 64 per cent in 2014-15

43. Attainment and retention data by college is available for six years for full-time students and for three years for part-time students. Between 2013-14 and 2014-15, further education attainment fell, while higher education attainment remained the same (Exhibit 7)

Exhibit 7

Attainment trends in colleges

Attainment has been generally increasing over the last few years, but either fell or remained the same between 2013-14 and 2014-15.

Full time measure	Long term trend, 2009 10 to 2014 15	2013 14 to 2014 15 trend
Further education full-time attainment	59-64% ↑	66-64% ↓
Higher education full-time attainment	63-71% ↑	71% ↔
Part time measure	**Long term trend, 2012 13 to 2014 15**	**2013 14 to 2014 15 trend**
Further education part-time attainment	76-75% ↓	77-75% ↓
Higher education part-time attainment	76-78% ↑	78% ↔

Source: SFC College Performance Indicators 2014-15 report

44. Full-time attainment fell in nine colleges between 2013-14 and 2014-15, by between one and eight per cent. Both merged and unmerged colleges experienced falls in attainment.

Retention rates for both higher and further education fell in 2014-15

45. Retention rates measure the percentage of students who completed all or part of their course. Like attainment rates, retention rates fell between 2013-14 and 2014-15. Between 2009-10 and 2013-14, retention rates in full-time further and higher education courses rose from 75 to 80 per cent, but fell to 78 per cent in 2014-15. Retention decreased in most colleges during this period, but increased slightly at Glasgow Clyde, South Lanarkshire, Moray and North Highland colleges.

46. Colleges suggested that the amount of change experienced by the sector in recent years could have contributed to the reductions in attainment and retention. They also suggested increased efforts to target harder to reach students could be a factor, for example widening access to students from more deprived areas. The SFC shares these views.

At least 82 per cent of students who left college in 2013-14 went on to a positive destination

47. The SFC published leavers' destinations for the first time in 2016, showing the destinations of 2013-14 college students. This highlighted that 82 per cent of college leavers were known to have gone on to a positive destination:

- 65 per cent went on to education or training
- 17 per cent went into employment, which compares to 25 per cent of school leavers and 51 per cent of university leavers entering work
- of the remaining 18 per cent, four per cent of leavers did not go on to further education or to employment and the outcome for the remaining 14 per cent of leavers is not known.

This data has not been published by college or region, as happens for schools and universities. Making this information available by college would provide a clearer picture of post-education employment opportunities at a local level, as well as whether the college curriculum is providing students with the skills employers in the area require.

Almost 90 per cent of students surveyed in 2015 were satisfied with their college experience

48. A pilot survey on student satisfaction by the SFC in 2015 found that 89 per cent of respondents were satisfied with their college experience. This survey took place at 16 volunteer colleges (both merged and non-merged), sampled just over 55,000 students, and had a 29 per cent response rate. It had no specific questions on mergers reflecting, in part, the generally shorter attendance duration of college students. As we note in Part 1, it is not possible to assess the impact of mergers on student satisfaction as there is no baseline data for this.

49. Colleges carry out regular surveys of their students. Some colleges provided us with results of surveys from before and after the merger period. However, since college students are often at college for a short period, many current students may not have been studying at college at the time of the mergers. For those colleges that sent us both pre-merger and post-merger information, the results indicated a drop in overall student satisfaction during this period. This mirrored the results from non-merged colleges over the same time period.

50. Student feedback gathered though the SFC's post-merger evaluations was mixed. Students in some merged colleges expressed concerns about the delays in receiving support payments caused by issues with IT systems integration, the impact of losing teaching staff mid-year, and worries that discontinuing part-time and recreational courses may affect the college's place in the community. Some students felt that there were additional learning opportunities, and more options for progression, whether on their original campus or at another one. The National Union of Students (NUS) told us it had concerns about courses being centralised within merger colleges and funding for student associations, but was not able to provide evidence to support these points at the time of our fieldwork. As part of the reform process, the SFC provided transitional funding for student associations for a finite period, after which time colleges require to fund these from their own resources.

Staff numbers had been falling, particularly in colleges that merged, but increased in 2014-15

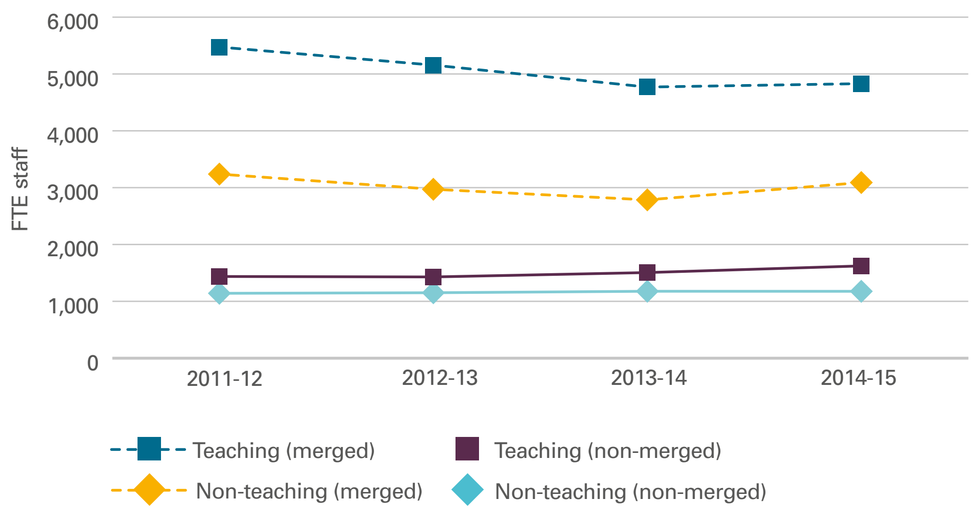
51. Staff costs accounted for £539 million (62 per cent) of college expenditure in 2014-15.[12] This is an increase from 2013-14 (59 per cent), after adjusting for donations to arm's length foundation of £99 million. Colleges employed 10,719 FTE staff in 2014-15. Teaching staff (teaching and teaching support staff) accounted for 6,453 FTE, with the remaining 4,266 FTE being non-teaching staff.

52. Between 2011-12 and 2013-14, there was a nine per cent fall in FTE staff, made up of a nine per cent fall in teaching staff and a ten per cent fall in non-teaching staff (Exhibit 8). The numbers increased by five per cent in 2014-15, with a three per cent rise in teaching staff in 2014-15, and an eight per cent rise in non-teaching staff.

Exhibit 8

FTE staff in merged and non-merged colleges

FTE staff at merged colleges fell during the period, though rose between 2013-14 and 2014-15.



Source: College accounts

Staff feedback on mergers is mixed

53. The SFC's post-merger evaluations highlight staff concerns about the impact of voluntary severance on workloads and the reduced level of support staff. Some staff felt mergers had been successful and cited benefits from sharing best practice and more opportunities for development. This was based on the SFC speaking to around 600 staff, covering a range of different departments and campuses, and taking views from both teaching and support staff.

54. The two largest college staff trades unions, the Educational Institute of Scotland (EIS) (representing teaching staff) and UNISON (representing mainly non-teaching staff), surveyed their members in 2015. The EIS survey (largely from members in merged colleges) had a response rate of 20 per cent (950 respondents). Eighty-nine per cent of staff who responded considered that the mergers had not improved the quality of learning, and 81 per cent felt it had increased their workload. Respondents felt that there had been a negative impact on morale. The UNISON survey sought the views of 923 members from merged and non-merged colleges and had a response rate of 28 per cent. Among respondents from merged colleges, 63 per cent felt there was a lack of transparency about the merger process while only 16 per cent felt there was proper communication between management and staff during the merger process. Where staff were more positive, they said strong leadership and management made the difference.

55. Nine colleges provided us with a copy of their most recent staff survey. Of the remainder, two (Ayrshire and Dumfries and Galloway) stated that their survey had recently been completed. Fife College referred to the post-merger evaluation and Inverness College stated that in the last three years its surveys had focused on specific areas. None of the other seven colleges provided details. North East Scotland College's survey had specific questions on merger, with 69 per cent of respondents stating that they had seen benefits, such as increased opportunities to share knowledge and improved resources. A quarter said they had seen no benefit from the merger.

56. Four colleges (City of Glasgow, Glasgow Clyde, Glasgow Kelvin and North East Scotland) provided us with details of actions they took in response to the staff survey results. These included improving communication from management and performing a workload assessment.

Colleges do not prepare organisation wide workforce plans

57. A workforce plan allows an organisation to identify the size and skills mix it requires to meet its stated objectives. Alongside financial planning (covered in Part 3), this is a key element in helping organisations achieve their strategic goals. The PAC endorsed our recommendation last year that colleges should review workforce plans, to identify any gaps in the skills, knowledge and resources required to deliver high-quality learning. Even though colleges have been making significant staff changes (Exhibit 8), there is limited evidence of systematic workforce planning. Colleges review workforce requirements in response to curriculum changes; and five colleges covered workforce in other plans, such as ROAs or financial plans. Two were preparing a workforce plan and four had high-level workforce strategies. At the time of our audit, none had a workforce plan in place that was in line with our good practice guide issued in March 2014.[13] Colleges Scotland is taking forward a project – 'Workforce for the future' – that aims to create a workforce to meet future needs. It will involve a job evaluation exercise. This project should aid future workforce planning.

Part 3

College finances

Key messages

1 The overall financial health of the sector is relatively stable. Scottish Government funding to the sector has been reduced by 18 per cent in real terms since 2010/11, but remains broadly static for 2015/16. The financial performance of the sector in 2014-15 deteriorated from the previous year with four colleges experiencing underlying financial challenges.

2 Capital funding has decreased by over 77 per cent since 2010/11. The current method of allocating capital funding does not take account of need. This is due to the absence of a complete and up-to-date national condition survey of the college sector estate. The Scottish Government is supporting investment of over £300 million to the college sector through a form of public private partnership. Colleges still do not prepare long-term financial plans which would help them prepare for uncertainty and address further financial pressures, such as national collective bargaining, estate maintenance and student support funding.

3 Colleges are adjusting to new arrangements arising from their reclassification as public bodies, in order to comply with HM Treasury and Scottish Parliament reporting requirements. While this has led to more work for colleges, with no direct business benefits, it provides the SFC with better and more timely information. It also enhances accountability for public expenditure in the sector. The Scottish Government's current approach to funding colleges for depreciation is complex, and creates a degree of uncertainty for colleges.

the overall financial health of the sector is relatively stable - with four colleges experiencing underlying financial challenges

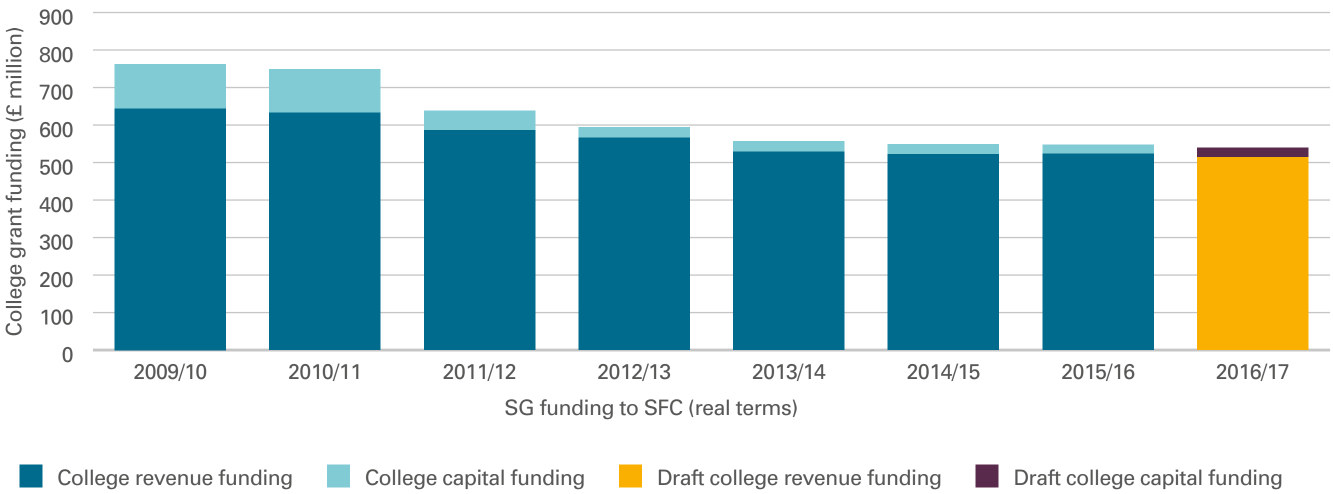
Scottish Government funding to the sector is broadly static for 2015/16

58. Scottish Government funding to the sector decreased by 18 per cent between 2010/11 and 2014/15 (Exhibit 9, page 27). Overall funding for 2015/16 will be increased by 0.2 per cent from the 2014/15 level. The total proposed allocation for 2016/17 represents a reduction of 1.4 per cent (£7.9 million) from the 2014/15 level.

Exhibit 9

Scottish Government funding to colleges, 2009/10 to 2016/17

Funding to the sector is relatively stable from 2014/15 to 2016/17 following some significant reductions in previous years.



Source: Scottish Government budget publication

The underlying financial health of the overall sector is relatively stable

59. The sector reported an overall deficit of £28 million in 2014-15 in audited accounts. After adjustments (outlined in the following paragraphs) are taken into account, the deficit decreases to £3 million. This represents less than one per cent of total income. This is deterioration from an underlying surplus of £15 million in 2013-14 (Exhibit 10) which represented three per cent of total income.

Exhibit 10

College sector financial results 2014-15 and 2013-14

The underlying financial performance has deteriorated from a surplus in 2013-14 to a deficit in 2014-15.

	2014 15 (£m)	2013-14 (£m)
Reported surplus/(deficit)	(28)	(95)
Asset revaluation reductions	7	10
Pension adjustments	5	1
Donations to ALFs	7	99
Additional spend	6	0
Underlying surplus/(deficit)	**(3)**	**15**

Note: Further explanation of the additional spend in 2014-15 of £6 million is presented in paragraphs 69 to 71.

Source: 2013-14 and 2014-15 audited accounts

60. Colleges' accounts include technical accounting adjustments that do not reflect actions taken by colleges and are outside their immediate control. These include property asset valuation reductions and pension adjustments. These two items account for £12 million of the £28 million reported deficit in 2014-15.

61. We have also removed donations to arm's-length foundations (ALFs) from our analysis.[14] We adjusted for these in last year's report as they accounted for £99 million of expenditure but did not indicate any concerns relating to the financial sustainability of the college sector. Colleges can apply for and have received funding from ALFs, generally for capital purposes (referred to in paragraph 66).

62. We also used standard accounting ratios and analysis to assess the underlying financial health of the sector (Exhibit 11). Our analysis indicates that the sector overall was stable in 2014-15.

Exhibit 11

Analysis of college sector finances using financial ratios, 2014-15

The sector's financial position has deteriorated in the last year but remains stable overall.

Balance sheet measure	Finding
Net assets or liabilities	
The net asset position shows the value of an organisation's assets (such as buildings and money held in bank accounts) after deducting the value of its liabilities (amounts owed to other parties such as creditors and loans). A positive figure indicates solvency. A negative figure ('net liabilities') indicates insolvency.	Overall, colleges reported a combined net assets position on their balance sheets of £848 million. No individual colleges were in a net liabilities position. The net assets position decreased by £63 million from the previous year.
Liquidity ratio	
The liquidity ratio reflects an organisation's ability to pay off its short-term debt obligations. It does this by comparing its liquid assets (such as cash held in bank accounts and accounts receivable) to the amount it owes its creditors. Where the value of creditors outweighs assets, a result of less than 1 is shown. This may indicate underlying financial issues although different organisations will determine results which best fit their business model. The SFC's Financial Memorandum with colleges recommends that colleges should keep cash balances to the minimum level consistent with the efficient operation of the institution and the level of funds required to meet any relevant liabilities at the year end.	The sector returned an average of 1.05, compared to 1.07 the previous year. Ten colleges returned a result of less than 1 in 2014-15, compared to eight in 2013-14.

Source: 2013-14 and 2014-15 audited accounts

Four colleges had underlying financial challenges

63. In 2014-15, the annual audit reports of four colleges identified concerns about finances (Exhibit 12).

Exhibit 12

Colleges where the auditor raised concerns about finances in 2014-15

Two colleges had significant underlying deficits; and the auditors for another two colleges raised other concerns about their financial situation.

College	Explanation of deficit or financial challenge
Edinburgh	The reported deficit was £5.1 million, 5.7 per cent of total income. The college faces significant financial challenges after it agreed with the SFC to reduce its activity target by six per cent. This has resulted in a reduction of SFC income for 2015-16 of £2.5 million, while its main costs, such as staff and accommodation, remain the same. The Auditor General has prepared a separate report on Edinburgh College.
Moray	The reported deficit was £0.8 million, 6.7 per cent of total income. The college experienced difficulties in managing its finances within budget. Higher education funding had decreased but the college did not adjust budgets to reflect this. UHI paid a cash advance of £0.5 million to the college.
North Highland	The auditor concluded that the forecast deficits for 2015-16 and 2016-17 cast doubt on the college's ability to continue operating. The regional body (UHI) provided assurances that it would work with the college to improve the financial position.
Lews Castle	The auditor reported that the college was not likely to meet its activity targets, and that this could result in reduced SFC funding. As income from the SFC accounts for around two-thirds of the college's total income, this would significantly affect the college's financial sustainability.

Source: Annual audit reports 2014-15

64. In June each year, colleges submit Financial Forecast Returns (FFRs) to the SFC, for the current and two subsequent financial periods. The combined FFRs from June 2015 forecast deficits of £0.9 million and £4.0 million respectively for 2015-16 and 2016-17. Eight colleges are forecasting a deficit in 2015-16, and 11 in 2016-17.

National collective bargaining is likely to result in an increase in costs for colleges

65. Historically, colleges have negotiated their own staff terms and conditions. A review of college governance in 2012 recommended moving towards national terms and conditions across Scotland.[15] The Scottish Government, in the Post-16 Education (Scotland) Act 2013, sought to reintroduce national collective bargaining in the college sector. The sector has sought to meet this government policy on a voluntary basis, although there is scope within the legislation for Scottish Ministers to compel colleges to do so. The sector and the staff trades unions have established the National Joint Negotiating Committee to take this forward. The committee has agreed a one per cent pay offer for 2015-16 (and a further 1.5 per cent in 2016-17 for teaching staff, converted to a flat cash sum of money) with the unions. It has also given commitments on a number of aspects around terms and conditions which will result in new contracts for staff. Colleges Scotland is leading work to estimate the potential costs, which could be significant.[16]

Colleges face challenges in financing improvements to their estate

66. The Scottish Government reduced its capital funding to colleges by 77 per cent between 2010/11 and 2014/15 (from £90 million to £26.6 million). Before reclassification, colleges could use reserves to fund capital projects, but this is no longer possible. Colleges currently have two options. The first option is to apply for funds from ALFs. All applications must comply with the ALF's stated purpose. In 2014-15, colleges received £23 million of funding for capital projects from ALFs. The FFRs for June 2015 forecast that over £59 million of capital expenditure would be funded from ALFs over the subsequent four years to 2018-19.

67. The second option is through the Non Profit Distributing (NPD) programme.[17] The Scottish Government is supporting investment of over £300 million to the college sector through the NPD programme. Four colleges are funding capital projects under this programme. One of these projects has been completed (Inverness), while two more are ongoing (City of Glasgow and Ayrshire). The remaining college (Fife) is at the full business case stage of the project. The Scottish Government and the Scottish Futures Trust are considering the impact on the financing arrangements for future NPD projects in light of guidance issued by Eurostat.[18] Eurostat will provide additional clarification on that guidance in September 2016. No new NPD projects are being taken forward whilst this guidance is being considered. As a result, a project at Forth Valley College is being taken forward using traditional capital funding from the Scottish Government.

68. The SFC allocates capital funding to colleges largely on the basis of teaching activity. While this is reasonable, information on the condition of the college estate should also be considered in calculating this funding allocation. An up-to-date condition survey for the entire college estate is not available. An SFC-commissioned study in 2014 covered 29 per cent of the sector's gross floor area and focused on colleges that had not recently received significant capital funding. The study estimated that it would cost £256.3 million to bring these properties back to 'as new' condition, and £289.6 million to replace them altogether.[19] The SFC is working with four colleges (Dundee and Angus, Edinburgh, Moray and West College Scotland) to develop business cases with a view to bidding for future capital funding. The SFC and Colleges Scotland have also formed a Capital Working Group that is preparing a capital plan for the sector.

The Scottish Government's approach to funding colleges for depreciation is complex, and creates a degree of uncertainty for colleges

69. Before reclassification in April 2014, the Scottish Government included an amount for depreciation within its funding allocation for colleges. As depreciation did not require a cash spend in the year of allocation, colleges were able to spend this cash or set it aside to meet future needs. Following reclassification, the Scottish Government provided a non-cash budget to cover depreciation. But the cash allocation to colleges still includes a sum equivalent to the amount previously set aside for depreciation. Colleges are potentially left with an amount of unspent cash (referred to in the sector as 'net depreciation cash') but require approval from the Scottish Government to spend it. In 2014-15, following discussions among the Scottish Government, the SFC and the college sector, colleges spent this cash on student support funding, loan repayments and 'regional priorities'. Three colleges donated an element of the cash to ALFs.

70. Because the items on which this net depreciation cash may be spent are not approved until mid-way through the college financial year, colleges do not know if or how they will be able to spend it, creating uncertainty in determining how to spend their allocation. Additionally, while the SFC recommended that colleges disclose the impact of this spend on their operating position, this was not disclosed in all cases. The SFC worked with colleges to calculate a total spend of £17.5 million in 2014-15.[20]

71. We acknowledge that reclassification has led to a mismatch between Scottish Government accounting rules and the further and higher education SORP (Statement of Recommended Practice). However, the current approach to addressing this mismatch is complex and creates uncertainty for colleges. It was also intended as a short-term measure. The mismatch has existed since April 2014. The Scottish Government, SFC and the sector are working together to develop a solution but have not set a date by which the issue will be resolved.

The SFC has begun to introduce a new funding model for colleges

72. The SFC is changing the way in which it allocates funding to colleges. Allocations are based on the amount of learning activity that colleges provide. Historically, this learning activity was expressed in 'student units of measurement' (SUMs), where one SUM equated to 40 hours of learning. Therefore, a course that involved 640 hours of learning would equal 16 SUMs. Over and above this, the SFC applied a weighting for each subject in recognition that some courses cost more to run than others, eg engineering courses cost more than social studies courses. The adjusted units were referred to as weighted SUMs (WSUMs).

73. The SFC has developed a new funding model which removes the weightings applied under WSUMs and instead categorises courses in five price groups. Each group has a credit value attached to it. The SFC has also changed the way in which it provides funding for colleges to assist students with additional support needs. The new funding model is being introduced on a transitional basis, during which time no college will receive a reduction in funding of more than one per cent. This approach has been adopted to allow the sector to prepare for any changes it introduces. There is currently no timescale for full implementation.

Reclassification has resulted in more work but greater accountability

74. In addition to changes to rules on retaining reserves and borrowing, reclassification has resulted in new arrangements for colleges. This includes more financial returns to the SFC and the Scottish Government, and the use of ALFs. In addition, colleges' decision to revert back to an academic year-end (31 July) for their financial statements, whilst requiring to break even at the end of March, means they work with two financial year-ends. The requirement to break even in March has meant some colleges have had to adopt bureaucratic, and potentially risky, approaches to managing surpluses. For example, Forth Valley College donated £1.1 million to an ALF in March 2015 and then applied to the ALF for £1.8 million in June. In March 2016, the SFC allowed colleges to transfer any cash surplus held back to the SFC rather than donating to an ALF, thereby minimising the risk of not receiving the funding back at a later date. The SFC was then able to manage the cash through its funding of universities which are not subject to the same budgeting rules regarding the Scottish Government's financial year-end. There is a limit on how much cash the SFC can manage in this way. This option would not have accommodated the full amount of funds (£99 million) which were donated to ALFs in 2013-14.

75. The new reporting arrangements arising from reclassification are required for HM Treasury and Scottish Parliament reporting purposes. They mean more work for staff within colleges, particularly finance staff. While there is no direct business benefit for colleges, the SFC now has access to more timely information about the finances of the sector. This allows the SFC to make more timely financial returns to the Scottish Government and is consistent with the reports required from all public bodies. As such, accountability for public expenditure has been enhanced. The number of returns that colleges make is currently fewer than other public bodies.

76. The new Further and Higher Education SORP comes into effect in 2015-16. The new SORP requires colleges to present financial information differently from before. This creates further work for college finance staff and will also make it more difficult to compare trend information.

Colleges still do not prepare long-term financial plans

77. Colleges still do not prepare long-term financial plans. Colleges contend that the short-term nature of their funding allocations makes future planning difficult, but this uncertainty is similar to other public bodies. The volume of change in the sector was also highlighted as a factor which makes longer-term planning difficult. We recognise these challenges. However, in line with our report from last year, we recommend that colleges should work towards developing long-term financial plans. These should involve a long-term financial strategy (five or more years) supported by medium-term financial plans (three to five years). These would allow colleges to prepare for issues such as estate development, national collective bargaining and student support funding.

Part 4

Governance and the role of the SFC

Key messages

1 There have been a small number of high-profile governance failures in the college sector in recent years. The Auditor General has reported on failures relating to severance payments at the former North Glasgow and Coatbridge colleges, and on the issues that led to Scottish Ministers removing board members at Glasgow Clyde College. The College Good Governance Task Group's recommendations should help to mitigate the risk of such significant governance failures.

2 While the SFC undertakes a range of monitoring and engagement within the college sector, this has not always resulted in timely and effective resolution of problems and issues. Despite the many changes in accountability arrangements in the sector, the Scottish Government has not undertaken a comprehensive review of the SFC's role in the last ten years. The Scottish Government's end-to-end review of the enterprise and skills agencies provides an opportunity to re-examine and clarify the SFC's role.

3 College board activities are not sufficiently transparent. Only one college complied fully with the Code of Good Governance for Scotland's Colleges and published all agendas, minutes and papers within appropriate timeframes.

despite many changes in the sector, the Scottish Government has not reviewed the SFC's role

There have been a small number of high-profile governance failures in the college sector in recent years

78. The Auditor General prepared three statutory reports following the 2014-15 audits, two of which highlighted governance concerns (Glasgow Clyde College and GCRB). These are detailed in (Exhibit 13, page 34), which also includes an update on previous reports by the Auditor General on the former North Glasgow and Coatbridge colleges.

The College Good Governance Task Group's recommendations should help to mitigate the risk of significant governance failures

79. The Cabinet Secretary for Education and Lifelong Learning established the College Good Governance Task Group as part of the government's response to the governance failures at Coatbridge, Glasgow Clyde and North Glasgow colleges.

Exhibit 13
Summary of statutory reports prepared by the Auditor General in recent years

Body	Issues identified in statutory report
North Glasgow College (May 2014) update[1]	The PAC published its final report on the management of severance payments in October 2015. It concluded that poor governance and the lack of openness and transparency resulted in a lack of accountability in respect of the use of public funds. The PAC asked for further information from the Scottish Government and the SFC on options for disciplinary action in the event of failings. This was taken forward by the College Good Governance Task Group.
Coatbridge College (June 2015) update[2]	Following the publication of the Auditor General's report on the college in June 2015, the PAC undertook an extensive inquiry. The PAC concluded that information was deliberately withheld from the college's Remuneration Committee and that information about the severance arrangements was deliberately withheld from the college's auditors. The PAC submitted its report to Police Scotland. The SFC wrote to the former principal to ask him to return some of the money he received but this did not result in any funds being returned. Legal advice obtained by the SFC suggested that there were no grounds to pursue this matter further. During 2014-15, New College Lanarkshire undertook work to identify any other legacy issues from Coatbridge College. Work is ongoing to resolve some identified issues and the auditor will report on progress in the 2015-16 annual audit report.
Edinburgh College (March 2016)[3]	The college exceeded the SFC limit for the level of additional education it provided to already enrolled students in 2014-15. This led to the SFC requesting that the college pay back £0.8 million. A review by the new college principal found other problems with how the college set activity targets. This led to the college agreeing with the SFC to reduce its activity target for 2015-16 by around six per cent, placing the college under significant financial pressure.
Glasgow Clyde College (March 2016)[4]	Scottish Ministers took the unprecedented decision to remove some members of the board of the college in October 2015. The Auditor General's report highlighted that the college board had failed to comply with a number of aspects of the sector's Code of Good Governance. This included not appropriately considering strategic business items and failing to seek further information about governance issues raised by the principal. The report highlighted a lack of open and transparent decision-making, with minutes not being circulated and agreed in a timely manner. The college also failed to comply with the SFC's Financial Memorandum on a delegated financial spending limit for procurement. The report recognised that the Emergency Board and the Executive Management Team had taken positive steps to address the weaknesses identified.
GCRB (March 2016)[5]	The statutory report found that GCRB had not put in place key systems of assurance and internal control. As a result, the SFC was not prepared to grant GCRB operational fundable body status. GCRB has made a number of improvements but, at the time of our audit, it had still not secured operational fundable body status. This means GCRB is not yet able to completely fulfil its role.

Notes:
1 *The 2012/13 audit of North Glasgow College: Governance and financial stewardship*, Auditor General for Scotland, May 2014.
2 *The 2013/14 audit of Coatbridge College: Governance of severance arrangements*, Auditor General for Scotland, June 2015.
3 *The 2014/15 audit of Edinburgh College,* Auditor General for Scotland, March 2016.
4 *The 2014/15 audit of Glasgow Clyde College,* Auditor General for Scotland, March 2016.
5 *The 2014/15 audit of Glasgow Colleges' Regional Board,* Auditor General for Scotland, March 2016.

Source: Audit Scotland

80. In March 2016, the group made recommendations to make governance in the sector more effective and focused on:

- board member recruitment, development and appraisal
- governance support for boards (introduce a national governance portal with links to guidance and good practice case studies; update guidance on board effectiveness; enhance and strengthen the board secretary role; provide resources and networking opportunities)
- external assurance (creating a more proactive, risk-based approach to monitoring by the SFC; and looking at how direct observation of board meetings could provide assurance)
- sanctions open to Ministers (the power to suspend any or all board members; the power to direct colleges in the face of a board not governing appropriately).

Implementation of these recommendations should help to mitigate the risk of significant governance failures.

College board activities are not sufficiently transparent

81. The College Code of Good Governance specifies that board agenda, minutes, policies and reports are published within appropriate timeframes.[21] Although the code does not specify the timeframes (and does not refer to committees), we consider good practice involves:

- agendas and reports for board and committee meetings made available at least a week before the day of the meeting
- board and committee minutes made available within one week after they are approved (likely to be at the first subsequent meeting).

82. Our review of college websites in February 2016 found that Glasgow Kelvin College complied fully with the code in terms of openness and transparency of board and committee activities. Glasgow Kelvin College published up-to-date agendas, minutes and relevant reports online. Eight colleges published up-to-date board and committee minutes but did not provide links to relevant reports. One college published reports (including the agendas) but not the approved minutes. Ten colleges published board minutes, but only seven of these were up-to-date.

The SFC's role in regulating college governance is not clear and it has not been effective in dealing with some issues

83. The SFC's statutory duty is to secure coherent, high-quality further and higher education by colleges and universities in Scotland. It is a non-departmental public body of the Scottish Government. The Cabinet Secretary for Education and Lifelong Learning issues Letters of Guidance (at least once a year) to the SFC. These set out the Scottish Government's expectations for the next academic year.

84. The SFC's relationship with the Scottish Government is formalised in a Management Statement and Financial Memorandum. This document was created in 2006 and states that the SFC's role is 'to promote sound governance and the highest standards of management by colleges and universities.' The document provides no further reference to the SFC's role specifically relating to college governance. A number of significant changes and issues have arisen in the sector since this was last reviewed. The PAC's report on Coatbridge College in January 2016 recommended that the Scottish Government look at the effectiveness of the SFC's supervisory role.[22] In May 2016, the First Minister indicated that the Scottish Government would undertake '*…an end-to-end review of the roles, responsibilities and relationships of our enterprise, development and skills agencies, covering the full functions of Scottish Enterprise, Highlands and Island's Enterprise, Skills Development Scotland and the Scottish Funding Council, to ensure that all of our public agencies are delivering the joined up support that our young people, universities, colleges and businesses need.*'[23]

85. The SFC has prepared a draft framework document with the Scottish Government which will replace the Management Statement and Financial Memorandum. This draft document proposes a more regulatory role for the SFC on governance arrangements in colleges, but it does not specify how the SFC should enforce this role.

86. The SFC introduced ROAs in 2012. The SFC now works with each college region to produce an ROA. This sets out the activities that the region will deliver in exchange for an agreed level of funding from the SFC. This essentially formalises pre-existing expectations and creates a contract between each region and the SFC. The SFC can enforce the contract by withholding or recovering funding.

87. The SFC created new posts for ROA managers, who are now colleges' nominated first point of contact with the SFC. ROA managers have also developed relationships with regional bodies. Both the sector and the SFC feel that this has improved relations and allows both parties to identify and resolve issues sooner than would have happened previously. Despite these improved relationships, the statutory reports at Coatbridge College and GCRB indicate that these have not been enough to quickly resolve some significant governance failures.

88. The Scottish Government specifies a national activity target and the SFC determines the contribution that each region will make to this national target. If a region does not meet the agreed targets, the SFC may decide to recover funding from the region. In 2014-15, the SFC sought to recover funding from three regions because they had not met their activity targets (Ayrshire, Dumfries and Galloway, and Edinburgh). Further details on Edinburgh College are provided in Exhibit 13. Ayrshire and Dumfries and Galloway colleges missed their targets by 1.2 per cent and 0.3 per cent, respectively. In these instances, the SFC normally reduces the following year's allocation by the amount equal to that to be recovered.

The SFC is currently preparing a workforce plan

89. The SFC employed 103 FTE staff in 2014/15 and had an operational budget of £7.6 million. SFC staffing reduced by around 13 per cent between 2010/11 and 2014/15, and its budget reduced by 16 per cent.

90. The SFC has restructured the organisation several times in recent years. Each of these has impacted negatively on staff morale. Its 2015 staff survey found that, while 87 per cent of respondents were committed to helping the SFC achieve its goals, only 49 per cent stated their intent to still be working there in a year's time. A staff survey in May 2016 reported that these responses had increased to 95 per cent and 57 per cent, respectively.

91. The SFC is currently managing a further operational funding reduction that is likely to require more voluntary severance. The SFC does not have a workforce plan to allow it to approach this from an informed position, although it is working on one. Having such a plan in place will help to ensure that the SFC has the right capacity and skills for the requirements under the new framework document it is preparing with the Scottish Government.

92. The SFC's financial plan only covers the period to 31 March 2017, owing to uncertainties surrounding grant settlements. The SFC's auditor has recommended that it develops a longer-term financial plan.

Endnotes

1 *Developing Scotland's Young Workforce final report*, June 2014.

2 Post-16 Education (Scotland) Act 2013 had a provision for collective bargaining in section 18.

3 *Scotland's colleges 2015*, Audit Scotland, April 2015.

4 UHI's 13 academic partners are made up of eight assigned colleges and Highland Theological College, Argyll College, Sabhal Mor Ostaig UHI, NAFC Marine Centre and Scottish Association of Marine Science.

5 It is an operational matter for the SFC to determine when a regional body should be funded by it. This involves the SFC making a judgement as to whether a regional body is in a position to administer effectively the funding for its assigned colleges. The Further and Higher Education (Scotland) Act 2005 empowers (but does not require) the SFC to fund a regional body.

6 *The 2014/15 audit of Glasgow Colleges' Regional Board*, Audit Scotland, March 2016.

7 Learning activity is measured by weighted student units of measurement (WSUMs), where one SUM means 40 hours of classroom-based learning and one Scottish Qualifications Authority credit. The SFC weights (W) these units by subject to reflect the differing costs of teaching different subjects. With the new funding model in the future this will be replaced by credits.

8 The four regions that under-delivered against their student learning targets in 2014-15 were Ayrshire, Dumfries and Galloway, Edinburgh and North East Scotland. The figures exclude European Social Fund activity and targets.

9 *Scottish Funding Council circular SFC/26/2009*, Para 22: 'The SUMs guidance gives early notice of a change to the eligibility for funding of short courses (less than 0.25 SUMs or 10 hours) that will be introduced from 2010-11.'

10 Excluding under-16s. In 2011-12, the SFC reduced funding for school students below S3 as these students are expected to study full-time in school.

11 *Audit of higher education in Scottish universities*, Audit Scotland, July 2016.

12 Staff costs cover wages and salaries, employers' national insurance contributions and pension contributions (including any accounting adjustments) but not severance payments which are accounted for as exceptional costs.

13 *Scotland's public sector workforce: Good practice guide*, Audit Scotland, March 2014.

14 Under reclassification, colleges are no longer permitted to retain reserves or take out new borrowing as this would count towards the Scottish Government's total spending. Colleges can therefore transfer any surplus to an ALF. In 2013-14, we adjusted the surplus/deficit position to take account of ALF transfers.

15 *Report of the Review of Further Education Governance in Scotland*, conducted by Professor Russel Griggs OBE, submitted to the Scottish Ministers, 20 January 2012.

16 Colleges Scotland is a charitable company which is funded through subscriptions from member colleges. It acts as the collective voice for Scottish colleges. The Colleges Scotland Board is made up of the 13 regional chairs plus four principals and the Chief Executive of Colleges Scotland.

17 The Scottish Futures Trust runs the NPD programme. The programme is a form of public private partnership and was developed as an alternative to Private Finance Initiatives.

18 Eurostat is the statistical office of the European Union.

19 RICS Building maintenance indicators other than A indicate some remedial work is required (A: As new; B: Sound, only minor deterioration; C: Operational, major repair or replacement needed; D: Inoperable, serious risk of failure).

20 Included within the SFC's analysis of the £17.5 million spend of net depreciation cash were loan repayments of £8.5 million that did not impact on the surplus/deficit position of colleges. The remaining £9 million, that did impact on the surplus/deficit position, included donations to ALFs from three colleges (City of Glasgow, Fife and Forth Valley) totalling £3 million, hence a net spend of £6 million in Exhibit 12.

21 The College Code of Good Governance was developed by a steering group which involved regional chairs, college chairs, principals, staff and student representatives, board secretaries, Colleges Scotland and the College Development Network. This was in response to a requirement as a result of the Post-16 Education (Scotland) Act 2013 provisions in relation to the identification of principles of good governance practice for the college sector. The first Code was produced in December 2014 and will be reviewed formally every three years but given the transformational changes that have been in the college sector specifically, and developments in good governance more generally, the Code will be kept under ongoing review.

22 *Report on The 2013/14 audit of Coatbridge College: Governance of severance arrangements, 1st Report*, Public Audit Committee, 2016.

23 *Taking Scotland Forward, First Minister: Priorities speech*, The Scottish Parliament, 25 May 2016.

Appendix 1

Methodology

Our audit involved:

- an analysis of information held by the SFC including performance and activity data, post-merger evaluations of merged colleges and communications with the sector
- interviews with a wide range of stakeholders. These included college principals, senior college finance staff, regional chairs, Colleges Scotland, staff and student unions, the Office of the Scottish Charity Regulator (OSCR), the Federation of Small Businesses, Education Scotland, the SFC and the Scottish Government
- a data request completed by auditors
- review of college documents such as financial plans, staff and student surveys and curriculum reviews
- analysis of relevant Scottish Government budget documentation and colleges' and Glasgow Colleges' Regional Board's audited accounts and auditors' reports covering the financial periods ending:
  - July 2015 (12-month period for the University of Highlands and Islands (UHI) colleges)
  - July 2015 (16-month period for non-UHI colleges)
  - These financial periods differ owing to a change in the accounting arrangements for non-UHI colleges which reported an eight-month period to the end of March 2014 in the previous set of accounts. This situation arose as HM Treasury confirmed to the Scottish Government in May 2012 that retaining a 31 July year-end for colleges was not possible and recommended that colleges would need to move to a March financial year-end. The SFC informed colleges in May 2013 that their financial year-end would be changing to March from 2014. In November 2013, HM Treasury offered the option for colleges to retain the academic year (August to July) for financial reporting. However, this required additional negotiations between HM Treasury and the Scottish Government, and consultations between the SFC and colleges, which were not concluded until June 2014. As a result, colleges were required to prepare accounts covering only an eight-month period, from 1 August 2013 to 31 March 2014. This did not apply to all colleges. UHI colleges continued to use a year-end of 31 July, and produced full-year accounts for the year ended 31 July 2014. This was to ensure

alignment of their financial year with UHI and other academic partners. In 2014-15, non-UHI colleges again used a different accounting period (16 months).These inconsistent accounting periods create difficulties in analysing some financial trend data. We refer to this in appropriate parts of the report.

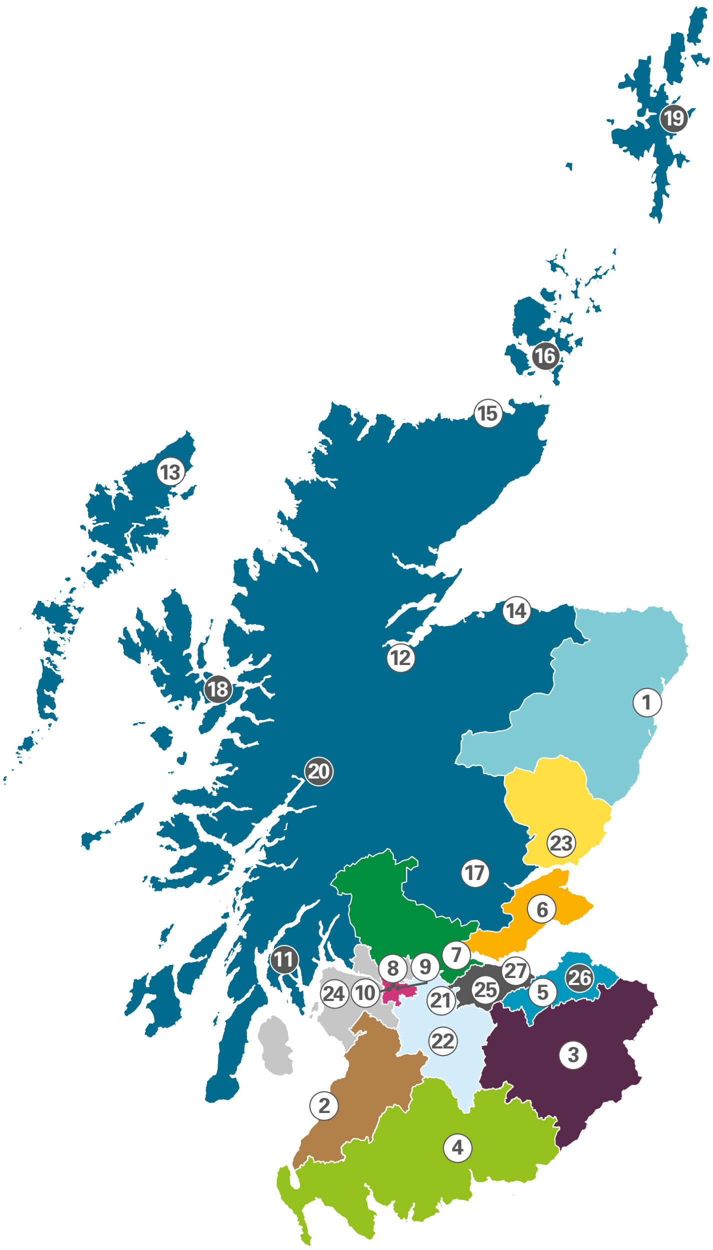
– These periods differ from the Scottish Government's financial year which runs from 1 April to 31 March. To help provide clarity, we use the convention '2014-15' when referring to figures from colleges' accounts, or relating to the academic year; and '2014/15' when referring to funding allocations made in the Scottish Government's financial year.

Our report reflects mainly the most recent college year (2014-15), unless particular issues arose from 2013-14, or where additional information helps in comparing different years. The longer financial period for non-UHI colleges in 2014-15 means it is not always appropriate to compare 2014-15 figures with previous years. We have applied different timescales in different sections of this report depending upon information available.

Figures and exhibits relating to colleges' audited accounts are for incorporated colleges only. Scottish Government budget information within this report refers to both incorporated and non-incorporated colleges; all other financial information relates to incorporated colleges only. Until 1992, all publicly funded colleges were run by local authorities. Under the Further and Higher Education (Scotland) Act 1992, most colleges established a distinct corporate body and board of management, which then assumed responsibility for financial and strategic management of the college. These 20 colleges are referred to as incorporated colleges and produce accounts subject to audit by the Auditor General for Scotland. The accounts of two of the three regional bodies are also subject to audit by the Auditor General for Scotland, those of the Glasgow Colleges' Regional Board and of New College Lanarkshire which is an incorporated college. Other publicly funded colleges are generally referred to as non-incorporated colleges.

Appendix 2

Scotland's colleges 2016



Region		College
Aberdeen and Aberdeenshire	1	North East Scotland College
Ayrshire	2	Ayrshire College
Borders	3	Borders College
Dumfries and Galloway	4	Dumfries & Galloway College
Edinburgh and Lothians	5	Edinburgh College
Fife	6	Fife College
Central	7	Forth Valley College
Glasgow	8	City of Glasgow College
	9	Glasgow Clyde College
	10	Glasgow Kelvin College
Highlands and Islands	**11**	**Argyll College**
	12	Inverness College
	13	Lews Castle College
	14	Moray College
	15	North Highland College
	16	**Orkney College**
	17	Perth College
	18	**Sabhal Mòr Ostaig**
	19	**Shetland College**
	20	**West Highland College**
Lanarkshire	21	New College Lanarkshire
	22	South Lanarkshire College
Tayside	23	Dundee and Angus College
West	24	West College Scotland
West Lothian	25	West Lothian College
n/a	**26**	**Newbattle Abbey College**
n/a	27	SRUC

Note: The map shows the 20 incorporated colleges, the six non-incorporated colleges in Scotland (in bold) and Scotland's Rural College (SRUC) which is classed as a higher education institution.

Source: Audit Scotland

Scotland's colleges 2016

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ISBN 978 1 911494 04 1 AGS/2016/8

This publication is printed on 100% recycled, uncoated paper