

Scotland's colleges 2017



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AUDITOR GENERAL 

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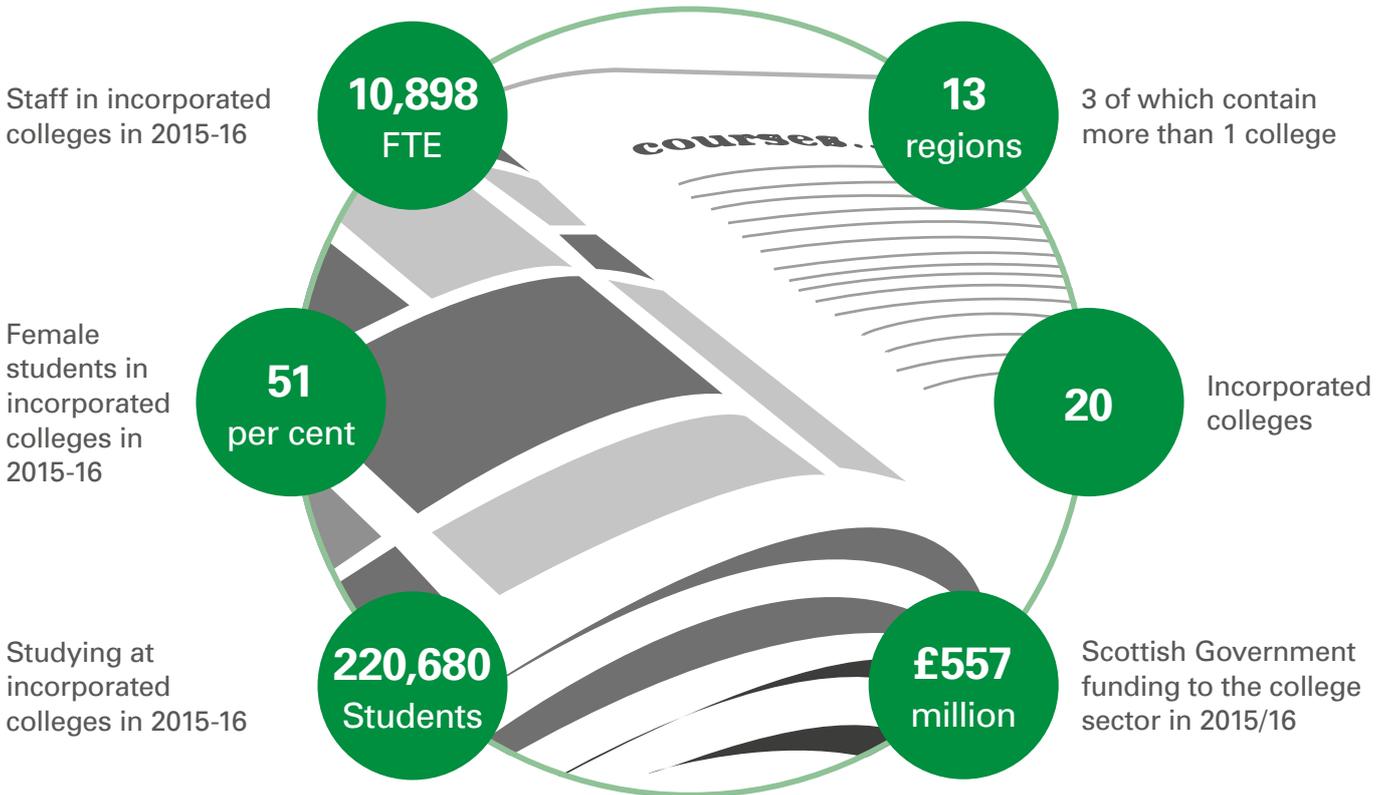


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Key facts



Summary



Key messages

- 1 The college sector has continued to exceed the national target for learning but delivered slightly less activity than in 2014-15. Two regions failed to meet their target resulting in a reduction in funding for one college. The Highlands and Islands region met its overall target but two colleges within the region failed to meet their targets. The Scottish Government currently prioritises full-time courses for younger learners, and changes in demography and in school leaver destinations will make it harder for the sector to continue to achieve the national target.
- 2 Student numbers decreased slightly in 2015-16 and FTE is at its lowest since 2006-07. Both full-time and part-time student numbers fell in 2015-16, with the latter decreasing at a greater rate. Most of the reductions in 2015-16 were in the 16-24 years old age group. Overall demand for college places is still not recorded at a national level, so it is not possible to say whether the decreases reflect a fall in demand.
- 3 Student attainment improved in 2015-16. The overall percentage of full-time further education students successfully completing their course increased in 2015-16 (from 64 to 65 per cent). Most full-time students continue to be satisfied with their college experience. At least 83 per cent of students who achieve a qualification go on to a positive destination, such as further study, training or employment.
- 4 The financial health of the college sector remains relatively stable but has deteriorated since 2014-15. The underlying deficit has increased to £8 million (representing one per cent of income) and colleges hold £11 million less cash than in 2014-15. Four colleges face particular challenges to their financial sustainability. Staff costs remain the highest area of expenditure and have increased as a percentage of total spending. The number of people employed by colleges has increased by six per cent over the last two years.
- 5 Total Scottish Government funding to the college sector will increase by five per cent between 2015/16 and 2017/18, though the bulk of this increase relates to a capital project at a single college. Funding for running costs will increase by one per cent, but colleges face a number of financial challenges. In particular, in June 2016, Colleges Scotland estimated that implementing national bargaining could cost around £80 million (not adjusting for inflation) over three years. The sector has still to develop longer-term financial planning in order to support financial decision-making that takes account of both immediate and future cost pressures.

the college sector continued to exceed targets for learning but faces financial challenges

Recommendations

The Scottish Government and the SFC should:

- model how changes in demography and school leaver destinations affect the ability of colleges to continue to meet the national learning activity target
- complete the national estate condition survey and use this as a basis to prioritise future capital investment
- work with colleges to assess demand for college courses across Scotland, in accordance with our recommendation last year, in order to plan future education provision.

The SFC should conclude its work to:

- specify the adjustments that should be made to the financial position reported in college accounts, taking account of the approach we have used in this report, in order to reach an 'underlying financial position' that reflects the immediate financial health of each college
- require each college to include, within its accounts, the underlying financial position
- specify the common assumptions to be used by colleges when developing longer-term financial plans.

Colleges should:

- prepare longer-term financial plans, as we recommended last year, in order to support financial decision-making that takes account of both immediate and future cost pressures
- calculate the cost of harmonising staff pay, terms and conditions and include these in their financial plans.

About the audit

1. This report is the latest in a series that provides an overview of the college sector in Scotland. It gives an update on college finances and an analysis of learning activity. We have set out our methodology in [Appendix 1](#). Our previous reports have commented on the various changes which have taken place in the sector in recent years including regionalisation, college mergers and reclassification of colleges as public bodies.^{1, 2}

2. Scotland's colleges play an important role in helping to achieve sustainable economic growth by contributing to the development of a highly educated and skilled workforce. In 2015-16, there were 220,680 students at incorporated colleges. They are the main providers of further education (FE) in Scotland, and also provide a significant amount of higher education (HE), with around

47,000 students studying at HE level at college in 2015-16. The college sector in Scotland comprises 20 incorporated colleges and six non-incorporated colleges organised into 13 college regions ([Appendix 2](#)).³ Ten of these regions consist of one college. College boards in these regions have been designated as regional college boards. The three remaining regions (Glasgow, Highlands and Islands, and Lanarkshire) consist of more than one college. The individual colleges in these regions are assigned to a regional body. The regional bodies for the three multi-college regions are:

- Glasgow Colleges' Regional Board (GCRB)
- The Lanarkshire Board⁴
- University of the Highlands and Islands (UHI).

3. UHI delivers its education through the various colleges within the Highlands and Islands region. Thus any higher education provided by a college is on behalf of UHI. Any further education delivered by a college is on behalf of the region. This differs from colleges elsewhere which deliver a mixture of further and higher education on behalf of the region. The participation data included in this report does not include information about students studying higher education through UHI.

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. We use the convention '2015-16' when referring to figures from colleges' accounts, or relating to the academic year; and '2015/16' when referring to funding allocations made in the Scottish Government's financial year.

5. A revised Statement of Recommended Practice (SORP) introduced in 2015-16 resulted in changes in how colleges prepare their accounts. SORPs are sector-driven recommendations on accounting and related practices as approved by the Financial Reporting Council (FRC), the UK body responsible for promoting corporate governance and reporting. The figures for the previous year are normally included in accounts to help make comparisons. As the revised SORP required colleges to restate the prior-year financial figures, the 2014-15 financial figures included in the 2015-16 accounts may differ from those included in the 2014-15 accounts. We have used the 2014-15 financial figures as presented in the 2015-16 accounts in this report.

6. Unless we state otherwise, all financial figures in the body of this report are in real terms, that is, adjusting for inflation. The base year for this report is 2015-16 and GDP deflators from December 2016 have been used to calculate the real-terms figures for other years.⁵

Part 1

College performance



Key messages

- 1 The college sector has continued to exceed the national target for learning but delivered slightly less activity than in 2014-15. Two regions failed to meet their target resulting in a reduction in funding for one college. The Highlands and Islands region met its overall target but two colleges within the region failed to meet their targets. The Scottish Government currently prioritises full-time courses for younger learners and changes in demography and in school leaver destinations will make it harder for the sector to continue to achieve the national target.
- 2 Student numbers decreased slightly in 2015-16 and FTE is at its lowest since 2006-07. Both full-time and part-time student numbers fell in 2015-16, with the latter decreasing at a greater rate. Most of the reductions have been in the 16-24 years age group. Overall demand for college places is still not recorded at a national level, so it is not possible to say whether the decreases reflect a fall in demand.
- 3 The overall percentage of full-time further education students successfully completing their course increased in 2015-16 (from 64 to 65 per cent). Most full-time students continue to be satisfied with their college experience. At least 83 per cent of students who achieve a qualification go on to a positive destination, such as further study, training or employment.

The college sector has continued to exceed the national target for learning activity in 2015-16 but delivered slightly less activity than in 2014-15

7. The volume of learning which colleges deliver can be measured in full-time equivalent (FTE) student places, or in units of learning known as credits. Each credit broadly equates to 40 hours of learning. Since 2012-13, the Scottish Government has set a national target for the college sector (including non-incorporated colleges) to deliver 116,269 FTE student places. The SFC set an equivalent target for 2014-15 and 2015-16 of 1,689,431 credits.⁶ The college sector exceeded this target and delivered 1,752,536 credits in 2015-16. This compares to 1,755,601 credits the previous year, a reduction of 0.17 per cent ([Exhibit 1, page 9](#)). The sector has exceeded the national target in every year since it was introduced.

colleges have exceeded the national target for learning but this will become harder because of demographic and other changes

Exhibit 1

Analysis of 16-19 year-old population compared to college activity

The population is in decline while activity targets remain relatively static.



Note: Activity is measured in academic years (eg, 2015-16) whereas population statistics are in calendar years. Activity targets and activity delivered include core and European funded places (see paragraph 54) from incorporated colleges, non-incorporated colleges and Scotland's Rural College (SRUC).

Source: ONS Labour Market Statistics; SFC Infact database; SFC Regional Outcome Agreements

8. In order to meet the national target, the SFC agrees credit targets with each of the 13 college regions. In multi-college regions, the regional body agrees the credit targets for the assigned colleges. Two regions (Edinburgh, and Dumfries and Galloway) did not meet their targets in 2015-16. The SFC subsequently reduced funding to Dumfries and Galloway for 2016-17, but allowed Edinburgh to retain funding because it was facing significant financial challenges. The Auditor General for Scotland published statutory reports on Edinburgh College in 2016 and 2017. More details are presented in [Exhibit 7 \(page 19\)](#).

9. Within the Highlands and Islands region, two colleges (Lews Castle and North Highland) delivered less FE activity than they had agreed with their regional body (UHI). Lews Castle College under-delivered by 20 per cent and North Highland College by three per cent. Due to other colleges in the region exceeding their targets, the region overall met its target and so the SFC did not seek to recover funding. UHI did not seek to recover funding from either Lews Castle College or North Highland College. The Auditor General for Scotland published a statutory report on Lews Castle College in 2017. More details are presented in [\(Exhibit 7\)](#).

Changes in demography and in school leaver destinations will make it harder for the sector to continue to achieve the national target

10. The Scottish Government's national target for the college sector has remained constant over the last four years, with a continued focus on full-time and younger learners. This has resulted in reductions in student numbers, with reductions being more pronounced for part-time and older learners. Our analysis of activity

and student population in the following sections focuses on the period from the year immediately before the national target was introduced (2011-12) to the most recent year (2015-16).

11. The Office for National Statistics' (ONS) Labour Market Statistics indicate that the number of young people (aged 16 to 19) in Scotland is reducing [Exhibit 1 \(page 9\)](#).⁷ Data is not readily comparable across all school leaver destinations, but Scottish Government data shows that more young people are going into work.⁸ Data from the SFC also shows that the number of Scottish-based people aged under 21 entering university has increased by seven per cent between 2011-12 and 2015-16, while the number of people aged under 20 entering college has decreased by four per cent. These factors are likely to make continued achievement of the national target for the college sector more difficult.

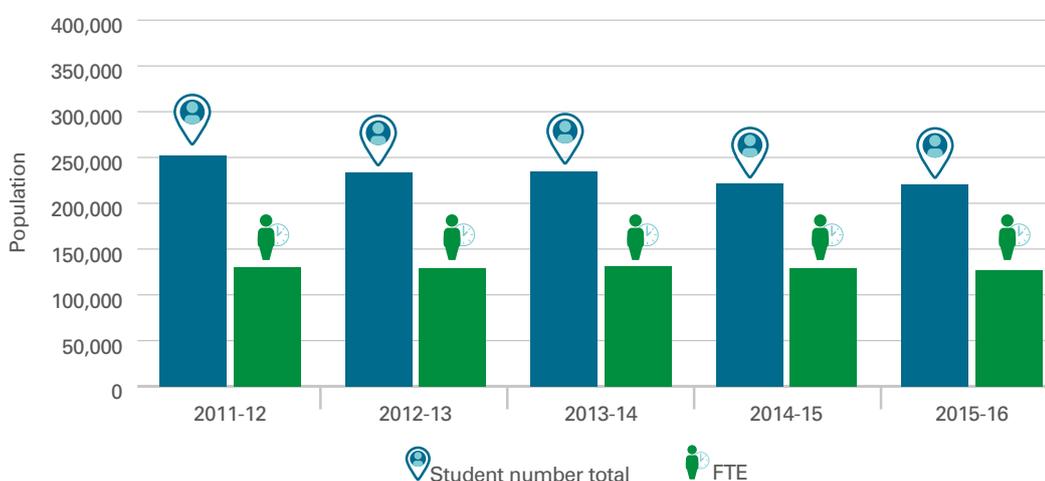
Student numbers decreased slightly in 2015-16 and FTE is at its lowest since 2006-07

12. In 2015-16, there were 220,680 students (by headcount) studying at incorporated colleges in Scotland.^{9, 10} Over the long term, student numbers have been decreasing ([Exhibit 2](#)). Decreases in the last four years have been smaller than the preceding years (2007-08 to 2010-11). The number of students at incorporated colleges decreased slightly in 2015-16, by around a half of one per cent. When measured by FTE, the student population is more stable, but decreased by around two per cent in 2015-16 – this is its lowest level since 2006-07. When those studying courses at other institutions (Scotland's Rural College (SRUC) and non-incorporated colleges) are included and when students with multiple enrolments at different colleges are removed, from the figures, there was a small increase in headcount in 2015-16. This is largely due to increases at SRUC, which is a higher education institution but counts towards the achievement of the national target for colleges. Even with the inclusion of figures for these institutions there is still a drop in FTEs since 2014-15.

Exhibit 2

Student population analysed by headcount and FTE (all ages)

The college student population continued to fall in 2015-16.



Note: The figures above includes students enrolled at more than one college.

Source: SFC Infact database

13. As overall demand for college places is not recorded at national level, it is not possible to say whether the decreases reflect a fall in demand. In our report last year we recommended that the SFC should explore with colleges a way to better assess demand for college courses across Scotland.¹¹ This would allow the SFC to identify levels of unmet demand and to assess the effect of future changes in policy or in the wider environment, such as university admissions and employment levels. The Scottish Government has commenced a project to evaluate the cost and benefits of a common application process for colleges in response to our recommendation.

14. Both full-time and part-time student numbers have decreased from 2014-15 to 2015-16. The number of full-time students has decreased by three per cent (2,266) since 2011-12, and has decreased by one per cent between 2014-15 and 2015-16. Part-time student numbers have decreased by 18 per cent (32,562) since 2011-12, and by eight per cent since 2014-15. These changes reflect Scottish Government policies to prioritise full-time courses for younger learners leading to recognised qualifications.

15. The number of students aged between 16 and 24 years old fell by three per cent in 2015-16. The number of under-16, part-time learners increased by 18 per cent (**Exhibit 3**). The SFC reports that the Developing Young Workforce programme has resulted in more school age children attending courses at college, for example construction and hairdressing.¹² However, the number of part-time students aged 18-19 years old decreased by 28 per cent since 2014-15. The population for this group in 2014-15 was a high point and the reduction is less when comparing over a number of years. The SFC was unable to provide specific reasons for the reduction but referred to younger people leaving school with more qualifications and improved employment prospects as being significant factors.

Exhibit 3

Analysis of student numbers by age, 2015-16

The number of students aged under 16 increased in 2015-16 but the number of students aged 16-24 decreased.

Student age	Full-time students		Part-time students	
	Number of students 2015-16	Change from 2014-15	Number of students 2015-16	Change from 2014-15
 Under 16	423	2%	20,685	18%
16-17	12,850	-3%	19,642	-12%
18-19	26,552	-1%	14,339	-28%
20-24	18,325	-4%	21,747	-15%
Over 25	19,182	3%	75,085	-6%
Total	77,332	-1%	151,498	-8%

Note: The total number of students reflected here differs from the total in Exhibit 2 as part-time students can undertake multiple courses at one or more colleges.

Source: SFC Infact database

16. Forty-two per cent of students are aged 25 and over, consistent with 2014-15. The number of full-time students aged 25 and over increased by three per cent in 2015-16 while the number of part-time students aged 25 and over decreased by six per cent. There was a smaller overall decrease in the number of older part-time learners than in those aged between 16 and 24 years.

There are still some courses with significant gender imbalances

17. The overall gender balance of the student population remains broadly even, with females representing 51 per cent and males 49 per cent in 2015-16. Full-time female students decreased by almost three per cent, while full-time male students remained static in 2015-16. Since 2011-12, full-time male students have decreased by four per cent and full-time female students have decreased by two per cent.

18. The reduction in part-time female students in 2015-16 was slightly more than for males, though both fell by over eight per cent. Female part-time students have reduced by 21 per cent since 2011-12. Male part-time students have decreased by 14 per cent over the same period.

19. Key performance indicators in the SFC's gender action plan (published in 2016) are to:

- increase the minority gender share in the most unbalanced subjects (by five percentage points) by 2021
- have no subjects with more than 75 per cent of students being from one gender by 2030.

20. The overall gender split remained static between 2014-15 and 2015-16. There have been some improvements in male-dominated subjects (engineering and transport). Gender imbalance has, however, increased in some female-dominated subjects (social work and health) ([Exhibit 4, page 13](#)). Addressing this issue will take a number of years and will require joint working between schools, colleges, Skills Development Scotland (SDS), the SFC and employers.

21. The SFC has created a Gender Governance Group made up of representatives from partner organisations including the Scottish Government, Education Scotland, SDS, National Union of Students Scotland, College Development Network and representatives from both college and university sectors. A report to this group in December 2016 noted that all college regional outcome agreements for 2016-17 included some activities focused on addressing gender imbalances, compared to 2015-16 where some made no reference to the issue. The SFC has asked each college to produce institutional plans by July 2017. These plans should set out the steps the college is taking to implement the relevant aspects of the SFC's Gender Action Plan.

Exhibit 4

Changes in subjects with greatest gender imbalances

The most male-dominated subjects have improved slightly, but in two female-dominated subjects, the imbalance has increased.

Subject	Male students in 2015-16 %	Female students in 2015-16 %	Percentage point change in minority gender from 2014-15
 Engineering	84.7	15.3	▲ 1.6
 Transport	92.3	7.7	▲ 0.9
 Health	22.1	77.9	▼ -3.0
 Social Work	12.9	87.1	▼ -1.2

Source: SFC Infact database

The percentage of students from ethnic minority backgrounds has remained static in recent years

22. The number of students from an ethnic minority background increased from 13,563 in 2011-12 to 13,618 in 2015-16. The percentage of ethnic minority students has remained at six per cent of the total student population over this period.

An increasing percentage of students are from deprived backgrounds

23. While there has been an overall drop in student numbers since 2011-12, the number of students from the 15% most deprived SIMD areas has increased from 47,783 in 2011-12 to 48,475 in 2015-16 (1 per cent).¹³ The percentage of students from these areas increased to almost 22 per cent of the total student population and it is at its highest percentage since 2006-07.

Student attainment improved between 2014-15 and 2015-16

24. Attainment rates measure how many students successfully completed their course and gained the appropriate qualification. The rates improved for all HE students and full-time FE students in colleges in 2015-16. The percentage of full-time FE students successfully completing their course decreased from 66 to 64 per cent in 2014-15, but increased to 65 per cent in 2015-16. HE attainment remained static between 2013-14 and 2014-15 but improved for both full-time students (from 71 to 72 per cent) and part-time students (78 to 79 per cent) in

2015-16. The picture is different for part-time FE students, where attainment decreased (for the second year in a row) by two percentage points to 73 per cent.

Retention rates remain lower for full-time students than those attending part-time

25. Retention rates measure the percentage of students who complete their course. The rates for all categories of student (apart from HE full-time) decreased slightly in 2015-16. The overall rates are:

- FE full-time: 74 per cent (a decrease of 0.2 per cent since 2014-15)
- FE part-time: 90 per cent (a decrease of 1.4 per cent since 2014-15)
- HE full-time: 82 per cent (an increase of 0.1 per cent since 2014-15)
- HE part-time: 91 per cent (a decrease of 1.2 per cent since 2014-15)

While the SFC has not been able to explain the reasons for these reductions, it suggested that efforts to target harder to reach students and the numbers leaving for employment explained the lower retention rates for full-time students (both FE and HE).

26. In March 2017, the Minister for Further Education, Higher Education and Science outlined the development of a new improvement project designed to raise attainment and improve retention rates in Scotland's colleges.¹⁴

The SFC's survey indicates that most full-time students continue to be satisfied with their college experience

27. The SFC undertook a second student satisfaction survey in 2016. This was the first time the SFC surveyed all colleges and modes of study (ie, full time, part-time and distance/flexible), and achieved an overall response rate of 26 per cent, with response rates at individual colleges ranging from under five per cent to 75 per cent.¹⁵ There was a good level of response from full-time students from which to draw conclusions. While there are some colleges with high response rates from part-time and distance/flexible students, there was some significant variation. Five colleges did not survey students on distance/flexible courses, but one of these (Perth College) has surveyed these students in 2016-17.¹⁶

28. Satisfaction ratings are based on the number of students who 'agree' or 'strongly agree' to questions. The overall satisfaction ratings were:

- 90 per cent for full-time students (response rate of 37 per cent; 25,981 students)
- 93 per cent for part-time students (response rate of 11 per cent; 5,138 students)
- 88 per cent for distance/flexible students (response rate of four per cent; 354 students).

29. In terms of full-time students, most questions within the survey elicited a satisfaction response of 80 per cent and above. Responses relating to survey questions about whether student suggestions were taken seriously and the ability of student associations to influence change for the better received the lowest satisfaction ratings (74 and 59 per cent respectively).

At least 83 per cent of college students who achieve a qualification go on to a positive destination

30. The SFC published its second report on destinations for college students in September 2016. This looked at students who gained a qualification in 2014-15.¹⁷ This does not solely represent college leavers, as students can gain a qualification and then go on to another college course. It excludes students who do not pursue a formal qualification and those who do not complete their course. It noted that:

- 69 per cent of qualifiers went on to education or training (2013-14, 65 per cent)
- 14 per cent went into employment (2013-14, 17 per cent)
- four per cent were either unemployed or unable to work (2013-14, four per cent)
- the destinations of the remaining 13 per cent were unknown (2013-14, 14 per cent)

The number of people that colleges prepare to join the workforce has an impact on how successfully the Scottish Government achieves its economic strategy.

31. As this is only the second such survey to have been carried out by the SFC, the quality of the data is still improving. Last year we recommended that the SFC should publish leaver destination at national, regional and college levels.¹⁸ The report published in September 2016 did so.¹⁹ The next report is due out in September 2017 and will focus on college students who gained a qualification in 2015-16.

Part 2

College finances



Key messages

- 1** The financial health of the college sector remains relatively stable but has deteriorated since 2014-15. The underlying deficit has increased to £8 million (representing one per cent of income) and colleges hold £11 million less cash than in 2014-15. Four colleges face particular challenges to their financial sustainability.
- 2** Staff costs remain the highest area of expenditure and have increased as a percentage of total spending. The number of people employed by colleges has increased by six per cent over the last two years.
- 3** Total Scottish Government funding to the college sector will increase by five per cent between 2015/16 and 2017/18, though the bulk of this increase relates to a capital project at a single college. Funding for running costs will increase by one per cent, but colleges still face a number of financial challenges. In particular, in June 2016, Colleges Scotland estimated that implementing national bargaining could cost around £80 million (not adjusting for inflation) over three years.
- 4** The SFC is coordinating a national estates condition survey to inform the preparation of a sector capital plan. The sector has still to develop longer-term financial planning to support financial decision-making that takes account of both immediate and future cost pressures.

The financial health of the sector remains relatively stable but has deteriorated since 2014-15

32. The sector reported an overall deficit of £19 million in colleges' 2015-16 audited accounts. After adjustments are taken into account (outlined in [Appendix 1](#), and in line with adjustments made in last year's report), the underlying deficit is £8 million. This represents one per cent of total income (£655 million), and is a deterioration from the underlying deficit of £1 million in 2014-15 ([Exhibit 5, page 17](#)). Eleven colleges had an underlying deficit in 2015-16, compared to 9 in 2014-15.

college finances have deteriorated – funding will increase in 2017-18 but implementing national bargaining is likely to involve significant costs

Exhibit 5

College sector financial results

The underlying financial position has deteriorated since 2014-15.

	2014-15 ¹ (£m)	2015-16 (£m)
Reported surplus/(deficit)	(10)	(19)
Asset revaluation reductions	5	4
Pension adjustments	14	12
Donations to arm's-length foundations (ALFs)	7	0
Net Depreciation cash spending ²	6	9
Non-Government capital grant	(23)	(14)
Underlying surplus/(deficit)	(1)	(8)

Notes:

1. The 2014-15 position differs from the £3 million deficit we presented in 2016 as all colleges have now adopted an accounting adjustment in respect of employees' untaken leave at the year-end, where previously only some colleges had adopted this.
2. The 2015-16 net depreciation cash adjustment figure is based on figures presented in the 2015-16 college accounts and returns provided by colleges to the SFC. The 2014-15 figure is based on an analysis performed by the SFC in 2016 with some further adjustments as advised by colleges.

Source: 2015-16 audited college accounts; *Governance and financial health of the college sector: Analysis of 2014-15 financial statements*, SFC, March 2016

33. An organisation's balance sheet indicates its overall financial health. It reports the value of assets held by an organisation, including properties and equipment. It also reports the value of financial obligations which an organisation is required to meet. These include any amounts owed at the balance sheet date for buying goods and supplies and any outstanding loans. Comparing these two figures provides the 'net assets' position. In situations where an organisation's financial obligations outweigh its assets, this results in a 'net liabilities' position. This measure can be used as an indicator of the college sector's financial health ([Exhibit 6](#)). However, net assets include some items which do not reflect actions taken by colleges and are outside their immediate control, such as pension liabilities. The impact of the new SORP on the net asset position is covered in [Appendix 1](#).

Exhibit 6

College sector net assets position

The net assets position deteriorated in 2015-16.

	2013-14 (£m)	2014-15 (£m)	2015-16 (£m)
Sector net assets	261	257	209
Number of colleges in a net liabilities position	3	3	5

Note: 2012-13 figures have not been recalculated under the new SORP so are not available on a consistent basis with figures from later years and have not been included in the table.

Source: 2015-16 audited college accounts

34. The reasons for the movements were:

- an increase in the value of fixed assets (due to new properties at City of Glasgow and Inverness colleges)
- an increase in longer-term financial obligations (due to the financing for new properties at City of Glasgow and Inverness colleges and increases in pension obligations)
- a decrease in current assets (due to a reduction in the amount of cash held).

35. The amount of cash held by colleges has decreased since colleges were reclassified as public bodies in 2014, and reduced by £11 million in 2015-16 (from £55 million to £44 million). This is included within current assets in college balance sheets. The SFC's financial memorandum sets out the terms and conditions with which colleges must comply.²⁰ It recommends that colleges maintain cash balances at a minimum, consistent with the level of funds required to meet any relevant liabilities. A target amount is not specified. Four colleges have maintained cash reserves specifically to pay off outstanding loans and other financial commitments. Balances for these colleges are therefore expected to reduce year on year. These repayments in 2015-16 were £2 million. The reduction in cash balances (over and above these repayments) has contributed to the reduction in the net assets position in the balance sheet. Two colleges (Moray College and New College Lanarkshire) have also experienced problems in their management of cash, as described in [Exhibit 7 \(page 19\)](#) and [Exhibit 8 \(page 20\)](#).

Four colleges face particular challenges to their financial sustainability

36. The Auditor General for Scotland has the power to prepare a statutory report (under section 22 of the Public Finance and Accountability (Scotland) Act 2000) to draw to the Scottish Parliament's and the public's attention matters of concern arising from an audit of accounts. The Auditor General prepared three such reports based on the 2015-16 accounts of Edinburgh College, Lews Castle College and Moray College ([Exhibit 7, page 19](#)).

Exhibit 7

Three colleges with financial challenges in 2015-16

The Auditor General for Scotland prepared statutory reports on Edinburgh College in 2016 and 2017, and on Moray College and Lews Castle College in 2017.¹

College	Description of issue
Edinburgh College	The college reported deficits in 2014-15 and 2015-16. A decision by the SFC to recover funding from the college for under-delivering activity in 2014-15 led to the college identifying underlying problems with student recruitment and with its curriculum. The college is implementing a business transformation plan, with significant financial support from the SFC. The college anticipates continued financial challenges until 2018-19, when it expects to return to a surplus position.
Lews Castle College	The college has persistently under-delivered against its FE activity target over a long period (at least eight years). The level of under-delivery has increased significantly over the last four years, and it delivered only 80 per cent of its FE target in 2015-16. While the college is not in immediate financial difficulty, continued under-delivery could result in financial penalties, a reduction in funding, or both of these. It is working with UHI and the SFC to implement changes to its operating model. The college and UHI have also agreed a reduced activity target for 2017-18.
Moray College	The college required an advance of funding from UHI to meet short-term obligations in 2015-16. This was the second year the college had required such an advance. The college had problems with financial management and planning, and the auditor concluded that fundamental changes were required for the college to achieve financial balance. The college has developed a recovery plan and is working with UHI and the SFC to implement the plan.

Note: 1. The 2015/16 audit of Edinburgh College, Auditor General for Scotland, March 2017; The 2015/16 audit of Moray College, Auditor General for Scotland, March 2017; The 2015/16 audit of Lews Castle College, Auditor General for Scotland, March 2017.

Source: Annual audit reports and 2015-16 audited college accounts

37. In addition, New College Lanarkshire has experienced difficulties during 2016-17 ([Exhibit 8, page 20](#)).

Exhibit 8

New College Lanarkshire has requested support from the SFC during 2016-17.

Description of issue

In its financial statements for the year ending 31 July 2016, the college reported a deficit of £1.953 million (equivalent to around four per cent of total income). In the performance report that accompanied the accounts, the college made adjustments for non-cash items that reduced the deficit to £52,000. However, the college was aware that its underlying position was a deficit of around £2.1 million (consistent with our analysis). In the annual audit report for 2015-16, the auditor highlighted that the college's cash balances would be under significant pressure going forward.

During 2015-2016, the college had faced cash flow pressures and had taken steps to mitigate these by adjusting timescales for payments for debtors and creditors. However, the steps taken by the college did not address underlying cash flow problems. The college was in discussion with the SFC about its financial position from July 2016 and cash flow forecasts provided to the SFC from September 2016 indicated that the college would have a significant cash shortfall by March 2017. In December 2016, the cash shortfall at March 2017 was estimated to be £2.118 million.

The college attributes the cash shortfall to a combination of lower than expected levels of fee income and higher than expected costs associated with national bargaining, pensions and national insurance contributions. In March 2017, the SFC agreed to provide an advance of £2 million of the college's remaining 2016-17 allocation, on the condition that the college develop a plan to address known cost pressures. At the time of this report, the college is working with the SFC to agree the plan, which is expected to cover a five-year period.

Source: Audit Scotland, New College Lanarkshire and the SFC

The SFC remains the largest source of funding for colleges

38. We compared college income and expenditure figures for 2015-16 to 2012-13 ([Appendix 1](#)). Overall income to colleges has reduced by £25 million (four per cent) since 2012-13 ([Exhibit 9, page 21](#)). The SFC remains the largest source of funding to the sector, at 73 per cent of total income. This percentage has not changed since 2012-13 although the amount of SFC funding has reduced by £15 million. SFC funding varies from 58 per cent at Perth College to 83 per cent at Ayrshire College. Colleges which earn more income from other sources have a lower percentage of their income from the SFC. The income can be derived from courses which attract funding from employers. The Student Awards Agency Scotland (SAAS) also provides funding for HE courses. When this is included, 79 per cent of college income in 2015-16 was from Scottish Government sources compared to 78 per cent in 2012-13.

39. The reduction in SFC funding has occurred at the same time as the college sector's other sources of income – including tuition fees, education contracts and donations and investment – have decreased. The combined reductions mean the college sector is working with less funding and less flexibility.

Exhibit 9

Analysis of income to colleges

The level of income to colleges has reduced by four per cent in real terms.

Type of income	2012-13 (£m)	2015-16 (£m)	Difference (£m)
SFC income	496	481	(15)
Tuition fees and contracts	119	117	(2)
Donations, endowments and investment income	3	1	(2)
Other income	62	56	(6)
Total income	680	655	(25)

Note: Colleges received £38 million of funding from SAAS in 2015-16 (£36 million in 2012-13). This income is included in Tuition fees and contracts.

Source: 2012-13 and 2015-16 audited college accounts

Staff costs continue to be colleges' largest area of spending

40. Colleges' total spending has decreased by £9 million (one per cent of total spending) since 2012-13 ([Exhibit 10, page 22](#)). This is due in part to a £19 million reduction in exceptional costs (£18 million of which related to staff severance). Colleges also reduced depreciation costs by £2 million and other operating expenditure (relating to items such as maintaining college properties and paying for utilities) by £17 million. These reductions have been offset by increases in staff costs ([paragraph 41](#)) and interest payments. The latter having increased by £5 million due to non-profit distributing (NPD) building projects at two colleges (City of Glasgow and Inverness).²¹

41. Staff costs continue to be the largest area of spending for colleges and have increased by £24 million since 2012-13. Staff costs have increased from 62 per cent of total spending in 2014-15 to 64 per cent in 2015-16. This figure is not separately identified in accounts but colleges estimated additional costs of £6 million in 2015-16 as a result of increases in pensions and national insurance contributions. Other parts of the public sector have also seen increases in staff costs due to these changes. A further £7 million is due to accounting adjustments relating to pension obligations, and £1 million due to the introduction of an accounting adjustment for untaken annual leave at the end of the year. The remaining £10 million increase in staff costs is likely to be due (at least in part) to the increase in the number of people employed by colleges. Pay awards could also be a factor.

Exhibit 10

Analysis of college spending since 2012-13

Spending has decreased by £9 million since 2012-13.

Type of spending	2012-13 (£m)	2015-16 (£m)	Difference (£m)
Staff costs	409	433	24
Exceptional staff costs	25	7	(18)
Other exceptional costs	2	1	(1)
Other operating spending	183	166	(17)
Depreciation	49	47	(2)
Interest payable	4	9	5
Total spending	672	663	(9)

Source: 2012-13 and 2015-16 audited college accounts

The number of people employed by colleges has increased by six per cent over the last two years

42. In 2011-12, before the Scottish Government's reform programme, colleges employed 11,290 staff (FTE) ([Exhibit 11, page 23](#)). This fell to 10,238 in 2013-14 (a reduction of nine per cent), and increased to 10,898 by 2015-16 (an increase of six per cent since 2013-14), despite the large number of departures associated with the Scottish Government's reform programme and the associated mergers. The number of non-teaching staff has increased by 343 (nine per cent) since 2013-14. Colleges with the most significant increases told us that the main reasons are services being brought in-house, curriculum changes and employing more apprentices.²²

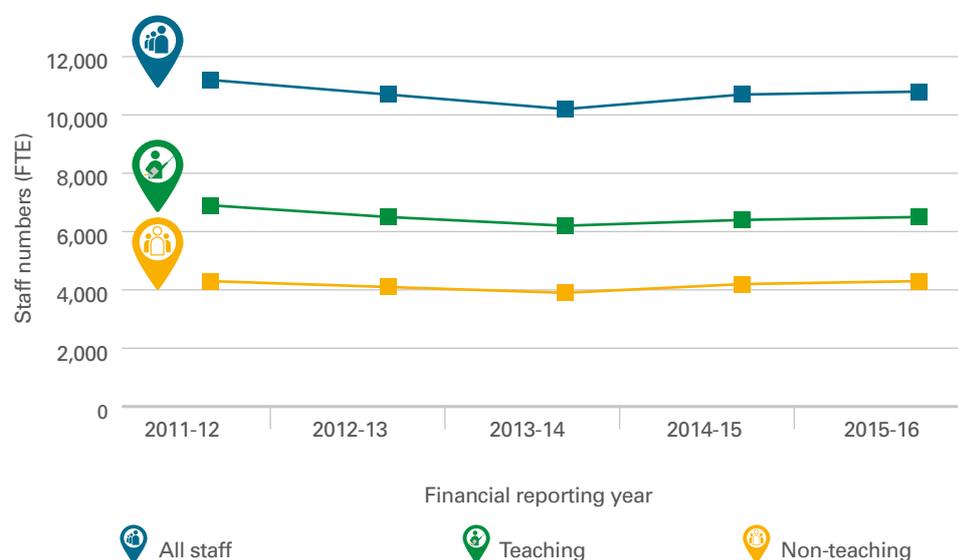
43. Teaching staff numbers have risen by 317 (five per cent) since 2013-14. From discussion with colleges, the main reasons for the increases are increasing credits targets for expanding colleges (including European funded places) and changes in curriculum or service delivery. An element of the increase is also due to changes in prior-year figures. This was caused by a combination of an eight-month accounting period and the merging of different information systems.

44. In 2016, we recommended that colleges should implement a more systematic approach to workforce planning.²³ Colleges Scotland is leading work on behalf of the sector called 'Workforce for the future'. This aims to create a 'fit for purpose, cost effective and professional workforce to meet the needs of the college sector in the future'.^{24, 25} The sector intends to use the agreed 'Workforce for the future' vision as the basis for future workforce plans.

Exhibit 11

Staff levels in incorporated colleges from 2011-12 to 2015-16

Staff numbers decreased following the programme of mergers in 2012-13 but have been increasing for both teaching and non-teaching staff since 2013-14.



Source: 2011-12 to 2015-16 audited college accounts

Scottish Government funding to the sector will increase in 2017/18

45. The Scottish Government announced the budget for 2017/18 in December 2016. The Scottish Government's allocation to the sector had decreased between 2009/10 and 2014/15. The allocation increased slightly in 2015/16 to £557 million, and again in 2016/17 to £577 million. In its December 2016 budget the Scottish Government indicated that it will provide a total of £582 million for colleges in 2017/18, a rise of five per cent from 2015/16 ([Exhibit 12, page 24](#)).

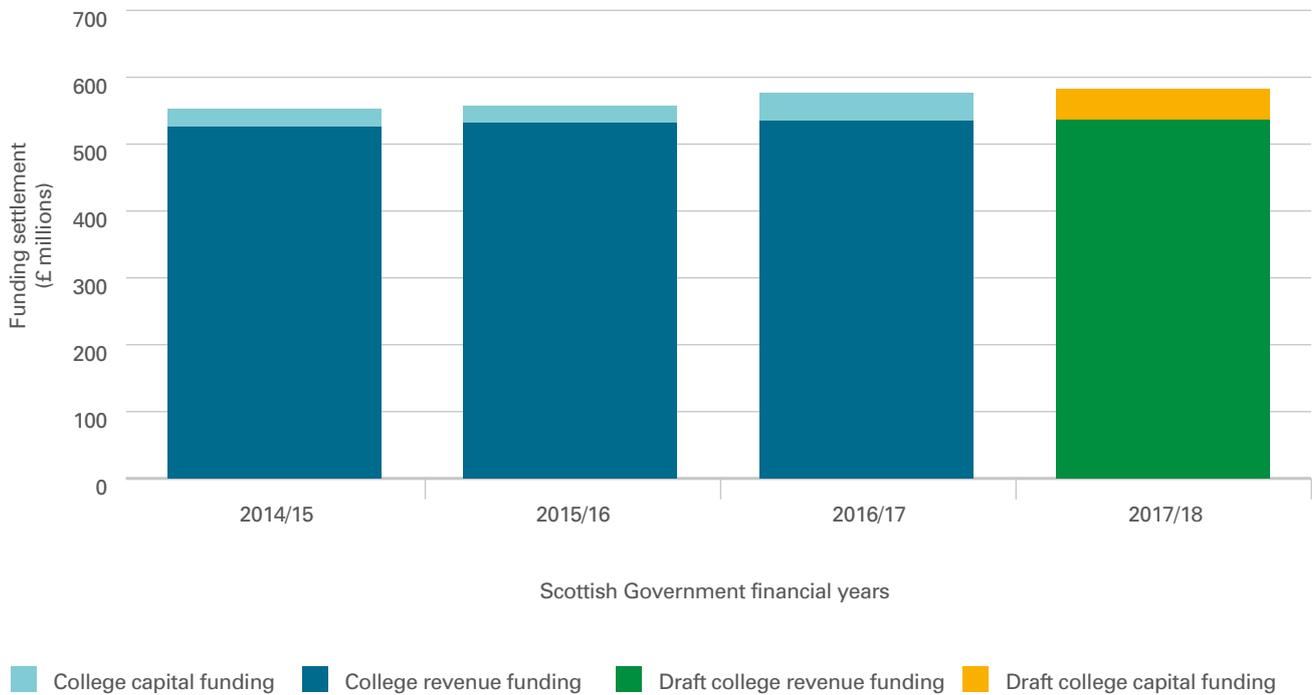
46. The Scottish Government funding allocation to the sector is in two distinct parts. The larger part (95 per cent in 2015/16) is called revenue funding and is used to fund running costs such as paying staff and buying goods and services. The sector is due to receive an increase in revenue funding of £5 million (one per cent) in 2017/18. The Scottish Government's draft budget announcement for 2017/18 stated that this increase is 'to ensure that colleges continue to add value to the economy and offer opportunities to adults of all ages.'²⁶ It also stated a commitment for the sector to continue to provide 116,000 FTE college places.

47. The second part is capital funding, which is used to buy or build new assets and enhance existing ones. This is due to rise by £21 million, £19 million of which (90 per cent) is for a single project at Forth Valley College.

Exhibit 12

Scottish Government funding to the college sector

The Scottish Government has confirmed a one per cent rise in revenue grant funding (in real terms) for 2017/18.



Notes:

- The above allocations do not include additional amounts provided to the college sector to support NPD unitary charges. These were: 2015/16 – £6m; 2016/17 – £24m; 2017/18 – £28m (all in real terms).
- Since 2014/15 the Scottish Government has made in-year adjustments to transfer an element of the capital allocation to revenue. These were: 2014/15 – £12m; 2015/16 – £10m; 2016/17 – £17m (all in real terms). We have not incorporated these changes in the exhibit.

Source: Scottish Government draft budgets and budget revisions (2014/15 to 2017/18)

48. The SFC splits the Scottish Government revenue allocation into separate elements before distributing it to colleges in academic years (August to July). In multi-college regions, the regional body is expected to carry out this role. The regional bodies were established in 2014, but in 2015-16 only UHI was able to distribute funding. UHI has continued to distribute funds to colleges in the region on the same basis as previously used by the SFC. The Lanarkshire Board has been able to fulfil this role since August 2016 and GCRB since April 2017.

49. The main element of a college's funding is the teaching grant. This is used to provide FE and HE learning. The SFC allocation for 2017-18 is £404 million. This is an increase of £10 million (2.5 per cent) compared with 2015-16. All colleges and college regions will receive an increase of two per cent, with seven receiving a further increase in the transition to the new funding model ([paragraphs 55–57](#)).²⁷ All regions, apart from the Highlands and Islands, will receive a share of £1.6 million of funding specifically for running childcare courses. The Glasgow region will also receive funding of £0.2 million to implement the Glasgow Curriculum and Estates Review.

The college sector continues to face a number of significant financial challenges

50. The college sector faces several financial challenges, as described in the following paragraphs.

National bargaining

51. Negotiations on pay and conditions for college staff are now conducted at a sector level, with a negotiating committee structure comprised of sector and trades union representatives. Prior to this, negotiations took place at each college, which resulted in differences in rates of pay and in terms and conditions. Negotiations cover annual pay increases and harmonisation of pay and conditions. Annual pay increases for 2015-16 and 2016-17 were agreed separately for both lecturing and support staff in 2015 and 2016.

52. Harmonising pay and conditions has been difficult. While negotiations are underway, details have still to be agreed and differences between the parties have already led to some employees taking industrial action. In Colleges Scotland's June 2016 spending review submission to the Scottish Government, it estimated the cost of implementing national bargaining to be £79.5 million (not adjusting for inflation) over a three year period. Following the latest rounds of negotiation, both the Scottish Government and the SFC have been working with Colleges Scotland to produce a final estimate of the cost of implementing national bargaining and this will be considered as part of the spending review process.

Student support funding

53. Colleges receive a separate allocation for student support funding to pay for things such as bursaries, childcare and discretionary funds (discretionary funds replaced hardship funds from 2007-08). College accounts report that £101 million was paid out in student support payments in 2015-16. In 2014-15 the figure was higher (£130 million) but this mainly reflected the 16-month accounting period. In 2014-15, the Scottish Government authorised colleges to use depreciation funding to meet any shortfall in student support funding ([paragraphs 65–67](#)). In 2015-16, colleges were again authorised to spend depreciation funding on student support. The 2015-16 accounts report that £1 million of depreciation funding was spent on student support. It is not possible to draw an equivalent figure for 2014-15 as some colleges did not include this detail in their accounts. The Scottish Government has commissioned a review of student support funding, which is due to report its findings in autumn 2017.

European funding

54. The Ministerial letter of guidance from October 2013 requested that the SFC should, in collaboration with SDS and colleges, 'maximise funding available through the 2014-20 European Funding programme'.²⁸ In response, the SFC has administered several programmes such as the Youth Employment Initiative, which will end in 2017-18, and Developing Scotland's Workforce which will run until 2020-21. These programmes are part European funded. In total, these projects will provide £70 million worth of funding between 2014-15 and 2017-18.²⁹ Colleges receiving these funds will have to plan for the end of these programmes. The UK Government's commitment to provide certainty regarding future European funding means that the decision to leave the European Union should not affect these programmes.³⁰

New funding model

55. The SFC is changing the way it allocates funding to college regions. Allocations are based on the amount of learning activity that colleges provide. Previously, courses were weighted to recognise that some courses cost more to run than others. The SFC has developed a new funding model which removes the weightings and instead categorises courses into five price groups. The SFC has also changed the way it provides funding for colleges to help students with additional support needs and to reflect rurality.

56. The SFC is introducing the funding model on a transitional basis, starting from 2015-16. This is intended to avoid colleges experiencing significant changes to their funding in a short timeframe. During this transitional period, the SFC has guaranteed that no college will receive a reduction in funding of more than one per cent in any one year (unless the college agrees to a larger reduction). The SFC expects that the new funding model will be fully implemented by 2020-21. The SFC's modelling indicates that, had the model been fully implemented in 2015-16, six regions would have received a total of £1.3 million more funding than they did, while the remaining seven would have received £1.3 million less.³¹ Highlands and Islands' allocation was one and a half per cent below what the region would have received under the new model. The differences for the other five regions which would have received more funding under the new model amounted to less than one per cent of the region's allocation.

57. The final funding allocations for 2017-18 show that the funding for three regions will be in line with the new model.³² Of the remainder, four will receive less and six will receive more than under the new model. Most differences are less than two per cent. Two regions (Ayrshire, and Dumfries and Galloway) are due to receive three and four per cent more than they would have, had the new model been fully implemented.³³ All regions (and colleges) should be working to match their future budgets to the allocations under the new model.

The SFC is coordinating a national estate condition survey

58. The current Scottish Government capital allocation to colleges is not enough to pay for significant capital projects, other than that for Forth Valley College. Last year we highlighted that there was no national condition survey of the college sector estate on which to base capital allocations. The SFC is coordinating an exercise to determine the condition of the college estate - that is, all property that colleges own. It is due to be complete in July 2017, after which a national capital plan will be developed. This follows a recommendation in our report last year to determine the current condition of the college estate and prepare a plan to ensure that it is fit for purpose.³⁴

59. The Scottish Government is supporting investment of over £300 million to the college sector through the NPD programme.³⁵ This is a form of public private partnership administered by the Scottish Futures Trust. Colleges receive funding for NPD assets as part of their revenue allocation. This is currently not available to colleges for new building projects because the Scottish Government is considering the impact of guidance issued by Eurostat (the statistical office of the European Union).

60. Colleges can also apply for funds from arm's-length foundations (ALFs). These are independent, charitable bodies which were set up when colleges were reclassified as public bodies. As colleges could no longer retain significant cash reserves as a result of public sector rules, colleges donated £99 million to ALFs

in 2014, with a further £7 million donated in 2014-15. Colleges' accounts report that £42 million was received from ALFs in the last two years. The majority of this (£39 million) was used for capital spending. ALFs prepare annual sets of accounts but these do not conform to the college academic year, and so cannot be compared directly with college accounts.³⁶ The ALFs' accounts report that they held £57 million in 2016. Colleges forecast that they will require a further £34 million of funding from ALFs for capital projects from 2016-17 to 2018-19.

The sector has still to develop longer-term financial planning to support financial decision-making

61. Having longer-term plans in place will allow colleges to better prepare for the challenges ahead and ensure their future budgets are in line with likely funding under the new model. Last year we recommended that colleges develop long-term financial strategies, underpinned by medium-term (between three and five years) financial plans.³⁷ Most colleges continue to budget for a single year, but some are now preparing longer-term financial plans.

62. The SFC requires colleges to provide an annual financial forecast return (FFR). The most recent FFRs (in June 2016) provided forecasts for July 2016, 2017 and 2018. These forecasts do not include either pension adjustments or non-government capital grant income and therefore are comparable to the underlying position presented at [paragraph 32](#). The June 2016 FFRs forecast a sector deficit of £20 million in 2016-17, with 16 colleges forecasting a deficit. The forecast deficit for 2017-18 was £13 million, with 13 colleges forecasting a deficit.³⁸ These forecasts were prepared before the funding increase announced by the Scottish Government (December 2016).

63. The forecast figures should be treated with a degree of caution. We compared the forecasts for 2015-16 (from the June 2015 FFRs) to the underlying position in [paragraph 32](#). These forecast that the sector would break even with eight colleges in deficit, while the final position was an underlying deficit of £8 million with 11 in deficit. Of the eight which forecast a deficit in 2015, three returned a surplus.

64. The SFC has been working with the sector to improve longer-term financial planning. One element of this is developing common assumptions for all colleges, for example around Scottish Government funding and cost inflation.

Reporting on the use of depreciation funding should improve in 2016-17

65. Last year, we noted that the need for Scottish Government approval for the use of net depreciation funding created uncertainty for colleges. We recommended that the Scottish Government and the SFC should identify and implement a better approach to allocating depreciation budgets to colleges. The SFC has introduced changes to address this recommendation. The SFC will allocate each college a fixed cash amount which they can spend on loan repayments, staff pay awards or student support funding.³⁹ This cash amount will remain unchanged in future years. This should provide colleges with greater certainty over future spending plans.

66. Last year we also recommended that the SFC should require colleges to report how they have spent depreciation funding in their accounts, including a breakdown of the spending. As a result, the SFC amended the accounts direction for 2015-16 to recommend what college accounts should report where the college has incurred a deficit as a result of spending net depreciation cash. The SFC provided an illustrative table to demonstrate how the breakdown of the spending should be shown. There was an improvement in how the spending was reported with all but one college including details in the 2015-16 accounts. Ayrshire College chose not to provide the breakdown using this table and therefore it was not clear how much net depreciation cash had been spent on the items specified by the SFC.

67. The SFC has also changed the presentation of college accounts (in 2016-17) to improve how colleges report deficits resulting from how they spend this cash. The accounts will continue to report surpluses or deficits in the same way as now, but colleges will be required to include a note which includes the non-cash budget from the Scottish Government. This non-cash budget is designed to cover the cost of depreciation for Scottish Government reporting requirements. This will report an adjusted surplus or deficit.

Endnotes



- ◀ 1 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 2 [Scotland's colleges 2015](#) , Audit Scotland, April 2015.
- ◀ 3 Until 1992, all publicly funded colleges were run by local authorities. Under the Further and Higher Education (Scotland) Act 1992, most of these colleges established their own corporate body and boards of management. The boards of management took over responsibility for the financial and strategic management of the colleges. These colleges are referred to as incorporated colleges and produce accounts subject to audit by the Auditor General for Scotland. The remaining six colleges are generally referred to as non-incorporated colleges. Scotland's Rural College (SRUC) is classed as a higher education institution but counts towards the achievement of the national target for colleges.
- ◀ 4 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.
- ◀ 5 The GDP deflator can be viewed as a measure of general inflation in the domestic economy. These are produced by HM Treasury and published on the gov.uk website.
- ◀ 6 Before credits were introduced, college activity was previously measured in Weighted Standard Units of Measurement (WSUMs) broadly equated to 40 hours of learning. They also included full-time tariffs. In 2014-15, colleges had to achieve a WSUMs target, as the credit target was not introduced until 2015-16. The target for 2015-16 was the WSUMs target in 2014-15 rolled forward and converted to credits.
- ◀ 7 *NOMIS Labour Market Statistics, Population estimates – local authority based by single year of age*, Office for National Statistics, February 2017.
- ◀ 8 *Summary statistics for attainment, leaver destinations and healthy living – No. 6: 2016 Edition 22*, Scottish Government, June 2016.
- ◀ 9 Headcount counts the number of students.
- ◀ 10 The student population data from the SFC's Infact database includes data for two non-incorporated colleges (Argyll and West Highland) within the figures for North Highland College (which is an incorporated college).
- ◀ 11 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 12 The Scottish Government established the Commission for Developing Scotland's Young Workforce in January 2013, asking it to make recommendations that would help Scotland to produce better qualified, motivated young people who are ready for work. The Scottish Government's response in December 2014 outlined the early progress that had been made and the additional work proposed to implement the Commission's recommendations. Colleges will play a central role in implementing many of the Commission's recommendations. The Scottish Government published its most recent progress report in December 2016.
- ◀ 13 SIMD refers to the Scottish Index of Multiple Deprivation. We use 15 per cent which is a commonly used percentile and is consistent with the approach taken in 2016. The Scottish Government has recently started measuring by ten per cent and 20 per cent. In 2015-16, students from the ten per cent most deprived SIMD areas accounted for 16 per cent of the student population, while students from the twenty percent most deprived SIMD areas accounted for 28 per cent of the student population.

- ◀ 14 Colleges of success - Raising attainment, improving retention and making Scotland's colleges world class, Scottish Government website, <https://beta.gov.scot/news/colleges-of-success-2017-03-31/>, March 2017
- ◀ 15 The SFC targeted a response rate of 50 per cent and achieved a response rate of 26 per cent across all modes of study.
- ◀ 16 The following colleges did not survey students on distance/flexible courses: Edinburgh College, Glasgow Kelvin College, Perth College, Lews Castle College and Moray College. South Lanarkshire College does not have any students on distance/flexible courses.
- ◀ 17 *College Leaver Destinations 2014-15*, SFC, September 2016.
- ◀ 18 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 19 *College Leaver Destinations 2014-15*, SFC, September 2016.
- ◀ 20 *Financial Memorandum with Fundable Bodies in the College Sector*, SFC, December 2014.
- ◀ 21 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.
- ◀ 22 Modern apprenticeships help employers to develop their workforce by training new staff, and upskilling existing employees. For individuals, a modern apprenticeship is a job which lets them earn a wage and gain an industry-recognised qualification.
- ◀ 23 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 24 *Submission to the Scottish Government's Spending Review 2017*, Colleges Scotland, June 2016.
- ◀ 25 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.
- ◀ 26 *Scotland's Budget: Draft Budget 2017-18*, Chapter 6 Education and Skills, Scottish Government, December 2016.
- ◀ 27 The seven colleges/regions to receive an additional funding increase in 2017-18 in transition to the new funding model are: Dundee and Angus College; Edinburgh College; Forth Valley College; Glasgow College Region; Highlands and Islands College Region; North East Scotland College and West Lothian College.
- ◀ 28 *Letter of Guidance to the Chair of the SFC*, Cabinet Secretary for Education and Lifelong Learning, October 2013.
- ◀ 29 The Regional Outcome Agreement documentation for 2014-15, 2015-16, 2016-17 and 2017-18 provides details of European funding. This includes both the part funded by the SFC and the match funded element from the European Structural Funds. These funds also include an element for student support.
- ◀ 30 Chancellor Philip Hammond guarantees EU funding beyond date UK leaves the EU, www.gov.uk, <https://www.gov.uk/government/news/chancellor-philip-hammond-guarantees-eu-funding-beyond-date-uk-leaves-the-eu>, August 2016.
- ◀ 31 The 2015-16 regional outcome agreement documentation (Annex B - College sector funding and targets 2015-16) indicated that Borders, Glasgow, Highlands and Islands, Lanarkshire, North East Scotland and West Lothian regions received less than they would have done had the new funding model been fully implemented in 2015-16. It also indicates that Ayrshire, Dumfries and Galloway, Dundee and Angus, Edinburgh, Fife, Forth Valley, and West regions all received more than they would have done under the new funding model.
- ◀ 32 The 2017-18 final regional outcome agreement documentation (*Table 2: Activity (Credit) targets and final funding allocations 2017-18*) indicated that Dundee and Angus, Highlands and Islands and West Lothian regions are due to receive an allocation in line with the new funding model in 2017-18. Edinburgh, Forth Valley, Glasgow and North East Scotland regions are due to receive less than that calculated by the new funding model whilst Ayrshire, Borders, Dumfries and Galloway, Fife, Lanarkshire and West regions are due to receive more.
- ◀ 33 Ayrshire College's final allocation for 2017-18 is three per cent higher than under the new model. This is because the college provides a higher number of courses in a lower price group than previously. Dumfries and Galloway College's allocation is four per cent higher than under the new funding model. This is because the college now provides more HE courses which attract funding from the Student Awards Agency for Scotland (SAAS). The SFC reduces its income to reflect this.

- ◀ 34 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 35 The Scottish Government is supporting investment of over £300 million to three colleges (Inverness, City of Glasgow and Ayrshire). The Scottish Government has supported these projects with payments (via the SFC) totalling £35 million by the end of 2015-16.
- ◀ 36 ALFs prepare sets of accounts which have different year-end dates to that of colleges. Generally ALF accounts are based on the year to the end of March (as opposed to July for colleges) so it is not possible to accurately reconcile ALF accounts to college accounts.
- ◀ 37 [Scotland's colleges 2016](#) , Audit Scotland, August 2016.
- ◀ 38 Ayrshire College did not provide a forecast for 2017-18 in its June 2016 FFR as it felt that there were significant uncertainties on underpinning assumptions.
- ◀ 39 The SFC now refers to a fixed cash budget earmarked for priorities (CBP) which is no longer linked to depreciation.

Appendix 1

Audit methodology



Our audit involved:

- an analysis of information held by the SFC including performance and activity data 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 SFC and the Scottish Government
- a data request completed by auditors
- analysis of relevant Scottish Government budget documentation and colleges' audited accounts and auditors' reports covering the financial periods ending July 2016.

This report focuses on incorporated colleges. Where it is necessary to include data relating to non-incorporated colleges, this is clearly stated.

Detailed methodology for specific sections in the report:

Accounting adjustments to audited accounts ([paragraph 32](#))

In line with our 2016 report, we have adjusted the sector's deficit as it includes 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. We also made adjustments for donations to arm's-length foundations (ALFs) as these do not indicate any concerns about financial sustainability. The Office for National Statistics (ONS) reclassified colleges as public bodies from April 2014. Following reclassification, colleges are no longer permitted to build up cash or take out new borrowing as this would count towards the Scottish Government's total spending. Colleges can therefore donate any surplus to an ALF. In 2013-14 and 2014-15, we adjusted the deficit position to take account of donations to an ALF. Colleges can apply for and have received funding from ALFs, generally for capital purposes, for example spending on buildings. No college made a donation to an ALF in 2015-16 and the sector expects the funds held by ALFs to reduce over time. The overall level of funds held by ALFs has reduced from £99 million in 2014 to £57 million in 2016.

We have made adjustments totalling £9 million in 2015-16 and £6 million in 2014-15 for colleges spending 'net depreciation cash'. Part of a college's allocation is for depreciation, reflecting the loss of value over time of assets such as equipment. But as this does not involve spending money, this is available for other purposes. Historically, colleges tended to transfer this money to their reserves to use for future capital spending or finance loan repayments. Following reclassification,

colleges can no longer build up cash but if the money is spent it will have an adverse effect on the reported financial position. In some cases, it could result in a college reporting a deficit. In previous years, the Scottish Government gave colleges permission to spend this money on specified items (for example, paying off loans and funding student support). This permission also extended to colleges recording deficits as a direct result of spending this money in this way.

We have introduced one further adjustment to the deficit position. The previous SORP required capital grants from non-government bodies (such as ALFs) to be shown as income. This was spread over the expected lifetime of the assets the grants were used to buy. Under the new SORP, capital grants from ALFs are still shown as income. But they are now shown, in full, in the year in which they are received. This resulted in an increase of £14 million in the income recognised in 2015-16 accounts and a £23 million increase in the income for 2014-15. We have made adjustments for these figures.

Changes to the net assets position from the introduction of the new SORP (paragraph 33)

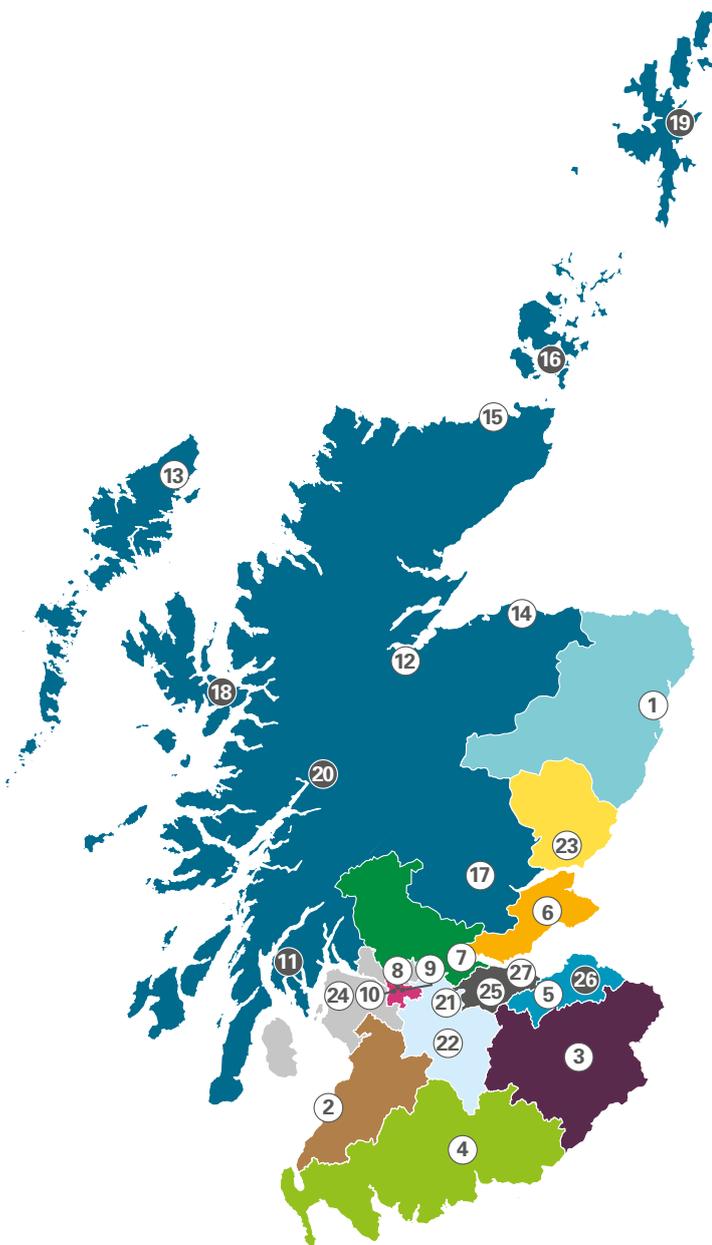
The introduction of the new SORP has led to a significant decrease in college net assets and to five colleges reporting a net liabilities position, where previously there was none. This is because of a change in how government capital grants are presented in college accounts. These grants are shown as income in the accounts, spread over a number of years dependent on the expected useable life of the asset it was used to buy. As only a part of the grant can be shown in any one year, the amount of the grant which has not yet been shown as income (the deferred part) is shown as a financial obligation in the balance sheet. The previous SORP required a similar treatment but did not report the deferred part as an obligation. As these deferred amounts do not require a future external payment they do not represent a risk to financial sustainability.

Financial trend analysis (paragraph 38)

Financial trend analysis is complicated due to changes in the financial periods covered by college accounts. When incorporated colleges were reclassified as public bodies in 2014, all colleges (other than those in the Highlands and Islands region) changed their accounting year-end to March. This resulted in colleges preparing accounts covering an eight-month period in 2013-14 (August to March). The sector reverted to a July year-end in 2014-15, and prepared accounts covering a 16-month period for 2014-15 (April to July). The accounts for 2015-16 were the first set of accounts for all 20 incorporated colleges to be prepared for a 12-month period since 2012-13. To reflect this, at some points in the report, we have used 2012-13 as a baseline period for comparison.

Appendix 2

Scotland's college landscape 2017



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
	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 but counts towards the achievement of the national target for colleges.

Source: Audit Scotland

Scotland's colleges 2017

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