Board of Management
Audit Committee

Date: 19 September 2017 **Time: 2 pm** **Room: 2009**

A G E N D A

				Presented by
1	Welcome and Apologies			HC
2	Declaration of Interest			HC
3	Minute of Meeting of 15 May 2017		(attached)	HC
4	Matters Arising			HC
	4.1	General Data Protection Regulation (GDPR)		CT
	4.2	Income Generation		CT
5	*Internal Audit Reports			
	5.1	*Estates Management – Reactive Maintenance - 8.16/17	(report attached)	PC
	5.2	Internal Audit Annual Report 2016-17	(report attached)	PC
6	Audit Scotland Reports			HC/KH
	6.1	2015-16 Audit of Edinburgh College	(report attached)	
	6.2	2015-16 Audit of Lews Castle College	(report attached)	
	6.3	2015-16 Audit of Moray College	(report attached)	
	6.4	Scotland's Colleges 2017	(report attached)	
7	2015-16 Draft Audit Committee Annual Report		(report attached)	HC
8	Draft Marketing Strategy		(report attached)	CT
9	Scottish Funding Council Financial Memorandum		(verbal)	KH
10	Strategic Risk Register		(report attached)	CT
11	Any Other Business			
12	Date and Time of Next Meeting – Tuesday, 21 November 2017 at 2pm			
13	Good Governance - Annual discussion with internal auditors without members of college staff			HC

*Individual Internal audits reports are not published on the website; they are included in the published annual internal audit report

Board of Management-Audit Committee

Minute of the Meeting of the Audit Committee of the Board of Management of Dumfries and Galloway College held on 19 September 2017 at 2 pm in Room 2009

Present:	Hugh Carr (Chair) Stuart Martin Delia Holland	Pat Kirby Naomi Johnson
In attendance:	Carol Turnbull, Principal Philip Church (RSM) Helen Pedley, VP Corporate Services Ann Walsh (Board Secretary)	Karen Hunter, Finance Manager Brian Johnstone (Board Chair)
Minute Taker	Heather Tinning, (Executive Team Assistant),	

1 Apologies

The Chair welcomed members to the meeting, in particular Naomi Johnson as a new member of the Audit Committee. The Secretary to the Board confirmed the meeting was quorate with enough members present to allow decisions to be made.

2 Declaration of Interest

Members agreed to indicate declarations of interest as appropriate throughout the meeting.

3 Minute of Meeting of 15th May 2017

The Minute of the meeting of 15th May 2017 was approved.

4 Matters Arising

4.1 General Data Protection Regulation (GDPR)

Following previous discussion at the last Committee meeting, the Principal advised that she had discussed the changes to the framework, with the Student Records Manager, in terms of the Data Protection Rules for 2017-18. The Vice Principal Performance and Planning and Student Records Manager are attending national meetings with regard to the changes. The Principal advised that the Committee would be updated of any implications that are non-operational.

4.2 Income Generation

Following discussion at the last Committee meeting, with regard to setting targets for Commercial, (non-SFC) Income the Principal reported on two targets that had been set, including:

- Credit Target achieved 4,082 for 2016-17
    - ➢ Proposed increased target of 4,500 for 2017-18

The Principal also reported on targets set for Surplus:

- The income for 2015-16 was £672,188
- The income for 2016-17 was £732,529
    - ➢ Proposed increased target of £750,000 for 2017-18

The Principal explained the Income target figure includes direct expenditure, but no overhead costs. Members agreed that the CTS Income is a valuable contribution to the income of the college. The Principal advised that a report will be presented to the Board of Management that includes details of Income and Expenditure for the last two years.

Decision: The Committee accepted the decision to increase the non-SFC Surplus and activity targets to £750,000 and 4,500 credits as recommended.

5 Internal Audit Reports

5.1 Estates Management – Reactive Maintenance 8.16/17

Phillip Church spoke to the Final Estates Management – Reactive Maintenance Internal Audit Report, reporting on a review of Estates Management including how works are raised, prioritised and given to members of the Estates Team. The report confirms that reasonable assurance has been provided for the Board that controls are in place. The Vice Principal of Corporate Services provided an update on completing the actions agreed, advising that the Facilities Manager has been working very closely with the Estates Team. Moving forward, the Facilities Manager is also working on a Guidance for the TSRs (Technical Support Requisitions) which are requests submitted by staff, and KPIs for the Estates Team.

Action: Following discussion, it was agreed to remove the names recorded in all Audit Reports moving forward and include only job titles

Members were re-assured that action has been taken in terms of all points raised in the Audit.

5.2 Internal Audit Annual Report 2016-17

Philip Church spoke to the Annual Internal Audit Report up to 31 July 2017, approved by the Audit Committee in May 2017. In terms of Governance, the report confirms that an appropriate Governance Structure is in place. The Internal Audit opinion confirms that an adequate and effective framework for Risk Management and Governance is in place. Philip reported on the three specific reviews that have been undertaken in terms of Risk Management, providing substantial assurances.
Decision: Members recommend the Internal Audit Annual Report 2016-17 to the Board of Management

6 Audit Scotland Reports

Audit Scotland Reports were provided to the Committee for information, allowing members the opportunity to view other Colleges' reports, including:

- 2015-16 Audit of Edinburgh College
- 2015-16 Audit of Lews Castle College
- 2015-16 Audit of Moray College
- Scotland's Colleges 2017

Members noted the content and some of the similar challenges faced on activity credit targets.

7 2015-16 Draft Audit Committee Annual Report

The Chair spoke to the Annual Report, which provides an overview of the Committee's work for the year and also reporting to the Board governance issues. The report summarises internal audits during the year and assurances gained. Feedback from External Audits undertaken in the next year will be presented with 2016-17 accounts at the next Audit Committee.
Decision: Members recommend the Draft Audit Annual Report 2015-16 to the Board of Management

Members noted the report.

8 Draft Marketing Strategy

The Principal spoke to the Draft Marketing Strategy, advising that the Strategy has been presented to Audit Committee members in order to give assurance that an action point from an Internal Audit report has been dealt with. The Principal advised that the Draft Marketing Strategy will now be presented to the Board of Management.

Decision: Members approved and recommended to present the Draft Marketing Strategy to the Board of Management for approval on 10th October 2017

9 Scottish Funding Council Financial Memorandum

The Finance Manager reported on the SFC Financial Memorandum, advising that following the move to the RBS/ Government Bank Account the college is now fully compliant with the Financial Memorandum, including cash management and banking requirements.

10 Strategic Risk Register

The Principal spoke to the Strategic Risk Register, highlighting recent changes and revised ratings.

With regard to the Cyber Attack, the principal assured members that the Fire Walls and Preventions in place were sufficient measures to prevent any attack.

In terms of achieving activity target, the Principal advised on the shortfall of planned enrolments, amounting to 150 full-time, advising that the situation will be monitored throughout the year.

The Principal reported on the risk referring to the Student Support Funds, Bursaries and Funds, advising that in the last three years the college has paid back some grant income, owing to surplus, advising that this is required on an annual basis and surplus cannot be accumulated.

Decision: Members approved the Strategic Risk Register

11 Any other business

None.

12 Date and time of Next Meeting

The next meeting of the committee is to take place on Tuesday 21 November 2017, at 2 pm.

13 Good Governance

The Good Governance Annual Discussion with the Internal Auditors took place after the Audit Committee Meeting allowing the Committee to meet privately with the internal auditors, in accordance with the Code of Good Governance for Scotland's Colleges.

Philip Church advised that there are no issues or criticism of the college from internal audit, and that good risk management was being undertaken.

Discussions took place regarding:

i) GDPR and what future requirements may be required both of the college and of the Board with regard to what records are kept and where.

Action: The Chair of the Board to discuss GDPR with the Principal.

ii) Internal Audit reports and whether these should be confidential to the college. The proposal is for the annual Audit Committee Report, annual Internal Audit report and External Audit reports being provided on the website as now, but not individual internal audits.

Action: The Secretary to the Board to investigate further regarding internal audit reports and get a view from RSM.

Board of Management

Minute of the Meeting of the Audit Committee of the Board of Management of Dumfries and Galloway College held on 15 May 2017 at 2 pm in Room 1074b

Present:	Hugh Carr (Chair) Stuart Martin	Pat Kirby
In attendance:	Carol Turnbull, Principal Philip Church (RSM)	Karen Hunter, Finance Manager Georgina Philp (Scott-Moncrieff)

Minute Taker Heather Tinning, (Executive Team Assistant),

1 Apologies

The Chair welcomed members to the meeting. Apologies for absence were intimated on behalf of Delia Holland, Naomi Johnson, Ann Walsh and Brian Johnstone who had been invited by the Chair to attend.

The Executive Team Assistant confirmed the meeting was quorate with enough members present to allow decisions to be made.

2 Declaration of Interest

Members agreed to indicate declarations of interest as appropriate throughout the meeting.

3 Minute of Meeting of 21 February 2017

The Minute of the meeting of 21st February 2017 was approved.

4 Matters Arising

Matters arising are covered within the Agenda.

5 Internal Audit Reports

5.1 Follow up on Previous Recommendations

Philip Church spoke to the report which had been issued, advising that the report provides assurance to the Committee and College Management that recommendations have been implemented.

Members noted the report and were content that the college is making satisfactory progress towards the recommendations.

5.1.1 Action Tracking Spreadsheet

The Finance Manager spoke to the Action Tracking Spreadsheet, which had been issued to the Committee to summarise the implementation status of previous audit recommendations. The Finance Manager asked the Committee for review and comment on the format of the Spreadsheet.

Members agreed the format and content of the Action Tracking Spreadsheet.

5.2 Cyber Security

Philip Church spoke to the Cyber Security Review, following an Internal Review for 2016/17 undertaken by one of RSM's IT Specialists, which involved looking at Software, Risk Assessments and Policies in place. He advised that 2 Medium and 3 Low recommendations had been implemented, providing a reasonable assurance that adequate policies and procedures are in place to prevent a cyber attack. Also staff and students have been given sufficient awareness in terms of safeguarding.

The Principal reported that following the Cyber Attacks on the NHS at the weekend, the College's IT Manager advised that the College's system had been checked over and that there were no issues with the software and the filters. He has since issued an e-mail reminding staff not to open suspicious e-mails. The Principal reported that the college has had one failed previous attempt by Hackers. Members discussed the GDPR, a new legal framework, which will apply in the UK from 25 May 2018.

Decision: The Principal to discuss the GDPR (General Data Protection Regulation) with the Student Records Manager in terms of the Data Protection Rules

Members noted the Cyber Security Audit Review and agreed that taking account of recommendations made, they were re-assured that adequate measures were in place to prevent a cyber attack

5.3 Income Generation

Philip Church spoke to the Income Generation Audit report, following a review on the income generation activities at both Dumfries and Stranraer campuses. The Zest Restaurant and the Hair and Beauty Salons were reviewed in terms of cash transactions, marketing strategy and stock control. As part of the review 4 recommendations were made. In terms of the products used in the Hair and Beauty Salons, the Principal advised that they are bought in bulk, using APUC. She advised that a stock control system is in place with the Technician in terms of monitoring stock, and that open bottles of products are sold to students and staff at the end of term. Members discussed setting contribution targets in terms of income generation, to provide the students with a commercial focus.

Decision: The Principal and Finance Manager to look at an aspirational target

Members noted the Income Generation Audit Report

5.4 Internal Audit Plan 2017-20

Philip Church spoke to the Internal Audit Plan 2017-20, looking at this year's plan, the College Risk Register and activities in the Sector going forward. In response to a question from a Committee Member regarding the Audit Fee, Philip confirmed that the daily rate is the same as last year. He reported on the Audit Committee requirements, including the impact on student attainment and recruitment. In terms of Risks to the College, members discussed the ongoing EIS dispute over terms and conditions.

Members noted the Final Internal Audit Strategy for 2017-20.

5.5 Progress Report

Philip Church spoke to the Internal Audit Progress Report, providing members of current progress against the 2016/17 Internal Audit Plan which had been approved by the Audit Committee on 10th May 2016.

Members noted the Internal Audit Progress Report and the assurance given that the Audit Plan for 2016/17 has been delivered by the end of the Academic Year.

6 External Audit

6.1 Wider Scope Audit Questionnaire

The Finance Manager asked the Committee to note the commentary and evidence available to the External Auditors, in response to their questions set out in the 'wider scope' paper which is part of Scott Moncrieff's planning work. Georgina spoke to the Wider Scope Audit Questionnaire, advising that the Audit Fee is set by Audit Scotland.

Members noted the Wider Scope Audit Questionnaire and were assured with the evidence that shows procedures and controls are in place.

6.2 External Audit Plan 2016-17

Georgina Philp spoke to the External Audit Plan for 2016-17 advising that the Plan highlights the work that the Auditors propose to undertake this year, including the work plan of 2016/17. She advised that the work will be focused around key areas, including Financial Sustainability. Georgina directed members to the survey monkey on page 4 of the report and encouraged members to comment on the quality of work and the report.

Members noted the External Audit Plan for 2016-17.

7 Strategic Risk Register

The Principal spoke to the Strategic Risk Register, reporting on the amended risks and revised ratings. In terms of Risk number 5, Review of Property and Provision in Dumfries, the Principal advised that she had attended a recent meeting with the University of the West of Scotland and that UWS were still working on a review of their Portfolios.

Following discussion on the recent Cyber Attacks and taking into account recommendations included in the Cyber Audit, members agreed that no further action is deemed necessary at this time.

Members noted that no new risks had been added.

8 Any other business

None.

9 Date and Time of Next Meeting

The next meeting of the committee is to take place on Tuesday 19 September 2017, at 2 pm.

DUMFRIES AND GALLOWAY COLLEGE

Annual Internal Audit Report - Year ended 31 July 2017

Presented at the Audit Committee meeting of: 19th September 2017

RSM

CONTENTS

1 THE ANNUAL INTERNAL AUDIT OPINION

This report provides an annual internal audit opinion, based upon and limited to the work performed, on the overall adequacy and effectiveness of the organisation's risk management, control and governance processes. The opinion should contribute to the organisation's annual governance reporting.

1.1 The opinion

For the 12 months ended 31 July 2017, the head of internal audit opinion for Dumfries and Galloway College is as follows:

Head of internal audit opinion 2016/2017
The College has an adequate and effective framework for risk management, governance, internal control and value for money. **However, our work has identified further improvements to the framework of risk management, governance, internal control and value for money to ensure that it remains adequate and effective.**

Please see appendix A for the full range of annual opinions available to us in preparing this report and opinion.

1.2 Scope of our work

The formation of our opinion is achieved through a risk-based plan of work, agreed with management and approved by the Audit Committee, which should provide a reasonable level of assurance, subject to the inherent limitations described below.

The opinion does not imply that internal audit has reviewed all risks and assurances relating to the College. The opinion is substantially derived from the conduct of risk-based plans generated from a robust and organisation-led assurance framework. As such, the assurance framework is one component that the Board takes into account in completing its annual governance reporting.

1.3 Factors and findings which have informed our opinion

We have updated management and the Audit Committee on the implications of the reports presented during the year on the systems of internal control, governance, risk management and value for money.

Governance

To inform our governance opinion for 2016 / 2017, we have taken in to consideration the governance and oversight related elements of each of the reviews undertaken as part of the 2016 / 2017 Internal Audit Plan. In particular, our reviews of Income Generation, Marketing and Communication, and Safeguarding including the Prevent Agenda included an assessment of the governance structure in place. In each review, we confirmed sufficient reporting arrangements were in place and we have concluded that the governance arrangements in place for the College were adequate and effective.

Risk Management

Our risk management opinion was informed by the assessment of the risk mitigation procedures undertaken in the areas covered by our risk-based reviews in the following areas:

- **Student Activity Data -** Unable to achieve credit (activity) target
- **Student Support Fund -** Imbalance between demand for student support fund/bursaries and funds available
- **Safeguarding including the Prevent Agenda -** Prevent Duty – disruption due to threat of extremism / risk of external influences

Our reviews of Student Activity Data, Student Support Fund and Safeguarding including the Prevent Agenda resulted in substantial assurance opinions and we did not identify any significant weaknesses in the design or application of the control frameworks.

Control

We undertook seven audits of the control environment that resulted in formal assurance opinions. Six reviews resulted in positive assurance opinions: three reviews resulted in substantial assurance opinions and three reviews resulted in reasonable assurance opinions. We also issued one partial assurance opinion that the College should consider when completing their annual statement of corporate governance and internal control.

Furthermore, the implementation of agreed management actions raised during the course of the year are an important contributing factor when assessing the overall opinion on control. We have performed a follow up review during the year which concluded reasonable progress had been made towards the implementation of internal audit management actions.

Value for money

The Scottish Further and Higher Education Funding Council requires internal audit to provide an appraisal each year on the Colleges arrangements for value for money.

We did not perform a specific value for money review at the College, we considered the value for money arrangements as part of our Income Generation and Estates Management – Reactive Maintenance reviews. Both reviews resulted in reasonable assurance opinions and management actions were raised to improve the control framework.

A summary of internal audit work undertaken, and the resulting conclusions, is provided at appendix B.

1.4 Topics judged relevant for consideration as part of your annual governance reporting

Colleges are required to include a Statement of Corporate Governance and Internal Control within their financial statements. As your internal audit provider, the assignment opinions and advisory reviews that we undertake and report on during the year are part of the framework of assurances that assist the Board (through the Audit Committee) prepare an informed statement and provide the opinions required. Our overall opinion may be used by the Board in the preparation of the 2016/2017 Statement.

The matters raised in this report are only those which came to our attention during our internal audit work and are not necessarily a comprehensive statement of all the weaknesses that exist, or of all the improvements that may be required. This report is prepared solely for the use of the Board and senior management of Dumfries and Galloway College.

2 THE BASIS OF OUR INTERNAL AUDIT OPINION

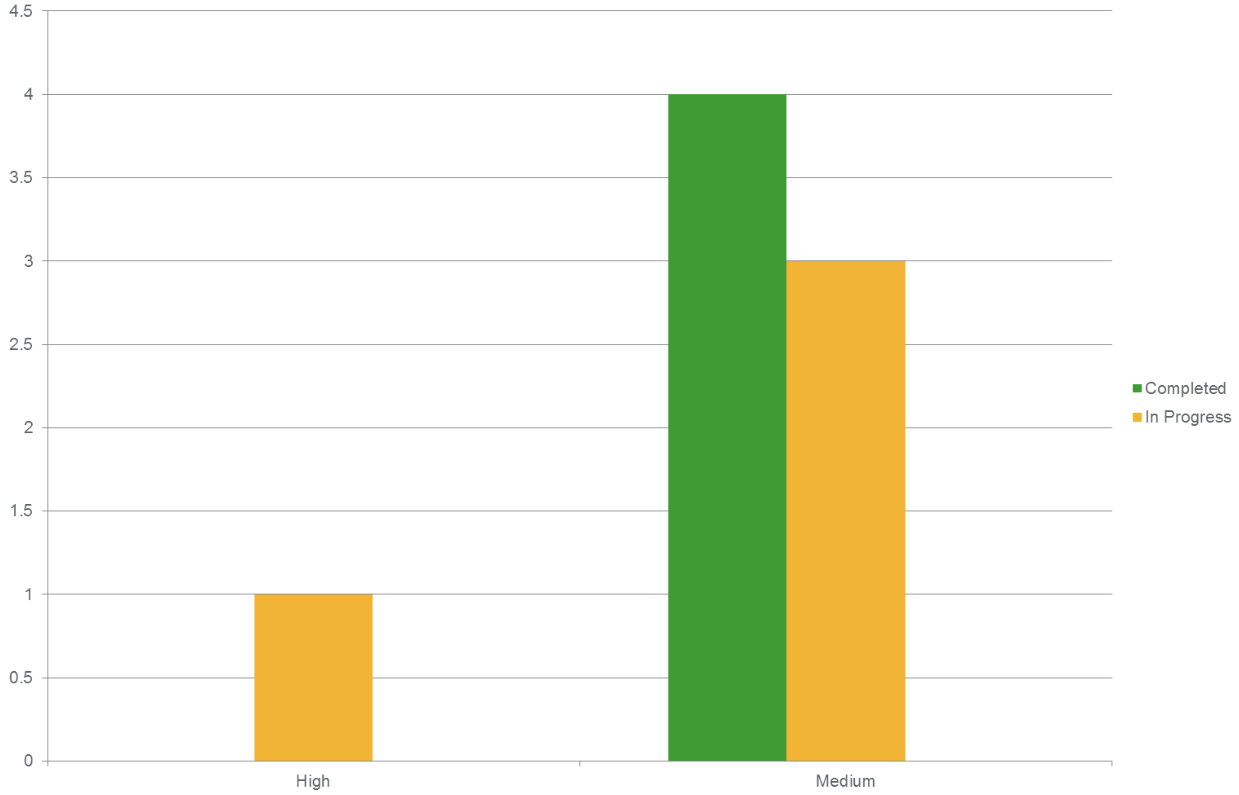
As well as those headlines discussed at paragraph 1.3, the following areas have helped to inform our opinion. A summary of internal audit work undertaken, and the resulting conclusions, is provided at appendix B.

2.1 Acceptance of internal audit management actions

Management have agreed actions to address all of the findings reported by the internal audit service during 2016/2017.

2.2 Implementation of internal audit management actions

Our follow up of the actions agreed to address previous years' internal audit findings shows that the organisation had made **reasonable progress** in implementing the agreed actions.



During 2016 / 2017, we identified one high and three medium actions were in the process of being implemented. Three of the recommendations, one high and two medium, related to a previous audit on Institution Sustainability and due to changes in the sector these recommendations had not been fully implemented.

2.3 Working with other assurance providers

In forming our opinion we have not placed any direct reliance on other assurance providers.

3 OUR PERFORMANCE

3.1 Wider value adding delivery

As part of our client service commitment, during 2016 / 2017 we have added value in the following areas:

Area	How this has added value
Sector briefings and emerging issues	In undertaking an analysis of all high priority management actions agreed with our internal audit further education clients in 2015/2016 our briefing highlighted what we, and our clients, considered to be the most important matters to be addressed and allowed the college to gain an insight into those key themes arising from our reviews. During the year we have also provided information on those key issues affecting the sector and details of recent developments in this regard that are of interest to the college. This included briefing papers on gender pay gap reporting legislation and subsequent requirements and the apprenticeship levy.
The Icarus effect: Tackling cybercrime complacency	Our research has shown that 40 per cent of people say their organisations had been a victim of cybercrime yet 21 per cent of those claimed no action had been taken to prevent it happening again. Following a cross sector survey, our report provides key information on the vital steps to protect the organisation and its workforce and considers potential evolving threats in the future.

3.2 Conflicts of interest

RSM has not undertaken any work or activity during 2016 / 2017 that would lead us to declare any conflict of interests.

3.3 Conformance with internal auditing standards

RSM affirms that our internal audit services are designed to conform to the International Standards for the Professional Practice of Internal Auditing and the International Professional Practices Framework (IPPF) as published by the Global Institute of Internal Auditors (IIA).

Under the standards, internal audit services are required to have an external quality assessment every five years. Our Risk Assurance service line commissioned an external independent review of our internal audit services in 2016 to provide assurance whether our approach meets the requirements of the IPPF.

The external review concluded that “there is a robust approach to the annual and assignment planning processes and the documentation reviewed was thorough in both terms of reports provided to audit committee and the supporting working papers.” RSM was found to have an excellent level of conformance with the IIA’s professional standards.

3.4 Performance indicators

A number of performance indicators were agreed with the Audit Committee. Our performance against those indicators is as follows:

Delivery			Quality		
	Target	**Actual**		**Target**	**Actual**
Audits commenced in line with original timescales	Yes	*Yes*	Conformance with PSIAS and IIA Standards	Yes	*Yes*
Draft reports issued within 10 days of debrief meeting	10 days	*9 days (average)*	Liaison with external audit to allow, where appropriate and required, the external auditor to place reliance on the work of internal audit	Yes	*As and when required*
			% of staff with CCAB/CMIIA qualifications	>50%	*67%*
Final report issued within 3 days of management response	3 days	*1 day (average)*	Turnover rate of staff	<10%	*No staff turnover in 2016 / 2017*
			Response time for all general enquiries for assistance	2 working days	*2 days (average)*
High and Medium recommendations followed up	Yes	*Yes*	Response for emergencies and potential fraud	1 working days	*N/A*

APPENDIX A: ANNUAL OPINIONS

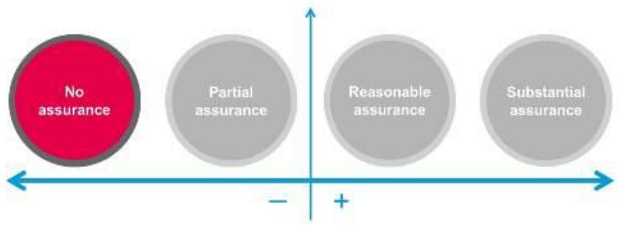
The following shows the full range of opinions available to us within our internal audit methodology to provide you with context regarding your annual internal audit opinion.

Head of internal audit opinion 2016/2017
The college has an adequate and effective framework for risk management, governance, internal control and value for money.
The college has an adequate and effective framework for risk management, governance and internal control. **However, our work has identified further improvements to the framework of risk management, governance, internal control and value for money to ensure that it remains adequate and effective.**
There are weaknesses in the framework of governance, risk management, control and value for money such that it could be, or could become, inadequate and ineffective.
The college does not have an adequate framework of risk management, governance, internal control or value for money.

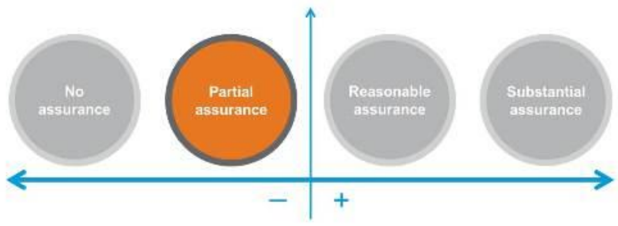
APPENDIX B: SUMMARY OF INTERNAL AUDIT WORK COMPLETED 2016 / 2017

Assignment	Assurance level	Actions agreed		
		H	M	L
Income Generation	Reasonable assurance	0	4	1
Follow Up of Previous Internal Audit Recommendations	Reasonable progress	1	2	1
IT Cyber Security	Reasonable assurance	0	2	3
Estates Management – Reactive Maintenance	Reasonable assurance	0	5	2
Student Support Fund	Substantial assurance	0	1	0
Student Activity Data	Substantial assurance	0	0	0
Safeguarding including the Prevent Agenda	Substantial assurance	0	1	2
Marketing and Communication	Partial assurance	2	2	2

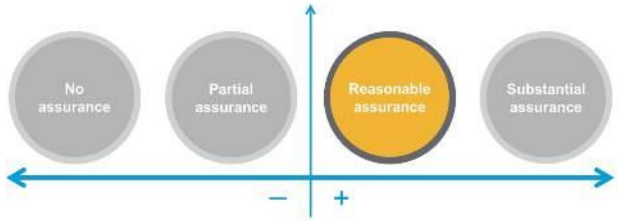
We use the following levels of opinion classification within our internal audit reports. Reflecting the level of assurance the board can take:



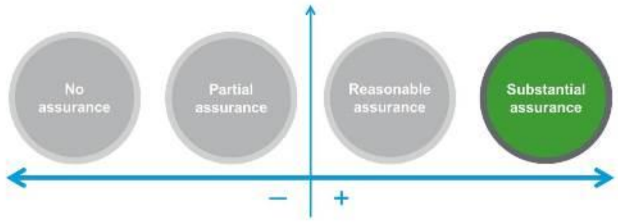
Taking account of the issues identified, the Board **cannot take assurance** that the controls upon which the organisation relies to manage this risk are suitably designed, consistently applied or effective.
Urgent action is needed to strengthen the control framework to manage the identified risk.



Taking account of the issues identified, the Board can take **partial assurance** that the controls to manage this risk are suitably designed and consistently applied. Action is needed to strengthen the control framework to manage the identified risk.



Taking account of the issues identified, the Board can take **reasonable assurance** that the controls in place to manage this risk are suitably designed and consistently applied.
However, we have identified issues that need to be addressed in order to ensure that the control framework is effective in managing the identified risk.



Taking account of the issues identified, the Board can take **substantial assurance** that the controls upon which the organisation relies to manage the identified risk are suitably designed, consistently applied and operating effectively.

FOR FURTHER INFORMATION CONTACT

Rob Barnett, Head of Internal Audit

Robert.Barnett@rsmuk.com

Tel: 07791 237658

Philip Church, Client Manager

Philip.Church@rsmuk.com

Tel: 07528 970082

The 2015/16 audit of Edinburgh College

Prepared for the Public Audit and Post Legislative Scrutiny Committee by the Auditor General for Scotland

Made under section 22 of the Public Finance and Accountability (Scotland) Act 2000

March 2017

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Introduction

1. I have received the audited accounts and the independent auditor's report for Edinburgh College for 2015/16. I am submitting these financial statements and the independent auditor's report under section 22(4) of the Public Finance and Accountability (Scotland) Act 2000, together with this report that I have prepared under section 22(3) of the Act.

2. The purpose of this report is to draw Parliament's attention to concerns about the financial sustainability of Edinburgh College, and to report to Parliament on progress with issues raised in my 2014/15 section 22 report on Edinburgh College. My report is based on information provided through the 2015/16 audit of Edinburgh College and additional work undertaken by the auditor and Audit Scotland.

The auditor's opinion

3. The auditor issued an unqualified opinion on Edinburgh College's financial statements for 2015/16. However, in his report, he highlighted concerns about the college's current financial position and future sustainability. The college reported a deficit of £7.0 million for 2015/16 and was reliant on additional support from the Scottish Funding Council (SFC) in order to meet its liabilities. 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. After excluding these items the underlying position for 2015/16 was a £3.6 million deficit. The auditor also highlighted that, at the time of reporting, the college's delivery of credits was behind its activity target for 2016/17. The auditor concluded that the future financial sustainability of the college is dependant on successful delivery of its transformation plan, but that it was too early in the implementation of the transformation plan to make a judgement about whether it will be successful.

Background

4. This is the second consecutive year in which I have reported on Edinburgh College. In my previous report, published in March 2016, I highlighted concerns raised in the auditor's annual report about the college's financial position. The auditor noted that the college experienced financial difficulties in 2014/15, and faced a reduction in forecast cash resources of £3.3 million in 2015/16. As a result the college sought additional financial support from the SFC. In my 2016 report, I highlighted the issues arising from the college's failure to meet its targets for student activity, and concluded that the college would face extreme difficulties without further financial support. I asked the auditor to keep the position under review and also asked Audit Scotland to undertake further work to examine the action being taken by the college to address these concerns.

5. Edinburgh College was formed in October 2012 by the merger of Jewel and Esk, Telford and Stevenson colleges. Edinburgh College is an independent legal body with charitable status as defined by the Further and Higher Education (Scotland) Act 1992 (the 1992 Act). It is governed by a board which is responsible for determining the overall strategy of the college and the proper use of public funds, the quality of provision and appointing the Principal and

other senior staff. In 2015/16, the college had 17,898 registered students and employed 1,164 full-time equivalent members of staff.

6. The college receives approximately 75 per cent of its annual income from the SFC. The majority of this funding is allocated on the basis of the college achieving an agreed target rate of student activity. This activity target is measured in 'credits'.[1] The SFC can seek to recover money from a college if the activity target is not met.

7. The SFC issued revised funding guidance in July 2014. The guidance included a change that set a limit on the use of additionality.[2] Additionality (also referred to as '1+' activity) is the provision of extra learning to students who are already enrolled at the college, such as students completing extra units that better prepare them for the workplace. The change in SFC funding guidance tightened the rules covering the volume of additionality for which a college could claim funding. The practice is now only permitted to specified levels and anything above these levels must be agreed in advance with the SFC.

8. The SFC had previously noted high levels of additionality at Edinburgh College, and the SFC raised its concerns with the college in November 2014, when the college's quarterly data return to the SFC showed a higher level of 1+ activity than was allowed. Despite the new guidance, and the SFC’s efforts to highlight its concerns, the college again reported high levels of additionality in 2014/15.

9. In October 2015, the SFC notified the college that it was likely to recover funds (£0.8 million) as a result of the college failing to reach its activity target for 2014/15. This failure occurred largely because of the college's reliance on 'additionality' to meet its activity targets.

10. Having realised the extent of the college's problems with student numbers, the current Principal, in post since May 2015, approached the SFC to rebase the college's activity target. In December 2015, the SFC wrote to the college, agreeing a six per cent reduction in its target for 2015/16, from 200,258[3] to 186,258. These credits were removed in-year and the associated reduction in funding of £2.8 million, plus a further £0.66 million reduction in European Social Fund funding, placed the college in severe financial difficulty.

11. In December 2015, the college Board of Management approved a 16-point action plan to form the basis of a new transformation plan (referred to in my 2016 report as a "recovery plan").

[1] Prior to 2015/16, 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, e.g. engineering courses cost more than social studies courses. The adjusted units were referred to as weighted SUMs (WSUMs). The new funding model removes the weightings applied under WSUMs and instead categorises courses in five price groups. Each group has a credit value attached to it. 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.

[2] While the SFC guidance specified a limit on additionality of no more than 2.5 per cent of activity, the guidance also indicated that higher levels of additionality might be accepted, but only if colleges agreed those levels with the SFC in advance.

[3] This includes a core credit target of 195,452 and 4,806 additional credits for delivery of programmes supported by the European Social Fund.

The final version of the transformation plan was agreed by the SFC in March 2016, and it was published in April 2016. In February 2016, the SFC notified the college that the Scottish Government had agreed that the college could retain the £0.8 million that the SFC was due to recover, as part of a special payment to support implementation of the transformation plan and on condition that the college implement the plan.

Action taken since the 2014/15 report

Additionality

12. The problems with additionality, and the associated decision by the SFC to pursue recovery of funding, led the new Principal to carry out a detailed review, beginning in November 2015, in order to better understand the reasons for the college's failure to meet its activity targets. The Principal reported to the Board on her findings in February 2016, with a final report presented to the Audit and Risk Assurance Committee in June 2016. On the specific issue of additionality, the Principal's review highlighted that there were problems arising from having two Vice Principals with responsibility for curriculum. Due to a lack of effective joint working within the college, and a potential for blurring of the lines of responsibility between the Vice Principal Curriculum and the Vice Principal Quality, there was a lack of clarity about who was ultimately responsible for making changes to the curriculum. The Principal confirmed that there were problems with lines of accountability at the meeting of the Public Audit and Post-Legislative Scrutiny Committee (PAPLSC) on 17 November 2016.

13. The SFC raised concerns about the college's use of additionality with the then Depute Principal and both the Vice Principal (VP) Curriculum and the VP Quality on numerous occasions, beginning in August 2014. The Principal concluded that the SFC's concerns about the use of additionality were not adequately addressed, but noted that other members of the Executive Team reported that that they had assumed the matter had been dealt with. The current Chief Operating Officer was the Director of Finance during 2014/15. In evidence to the PAPLSC, he stated that, although he was aware of the change in SFC guidance, neither of the two Vice Principals had raised any concerns with him. He indicated that, as far as he was aware, the levels of additionality had been agreed with the SFC. In her report, the Principal acknowledged that part of the problem arose from the lack of follow-up action from the wider Executive Team to address problems raised with the use of additionality, and underlying problems with the curriculum.

14. The two Vice Principal posts for curriculum and quality were merged in May 2015, as part of a management restructuring exercise, creating a new post of Vice Principal Curriculum and Quality. The then VP Curriculum was matched into the new role. Following the restructuring, the VP Quality applied for and was granted voluntary severance, with a severance payment in line with the terms of the scheme. For the six months between her post being deleted and taking severance, she worked as Director of Strategic Projects until leaving the college in November 2015.

15. On completing her review, the Principal concluded that the primary responsibility for developing the curriculum, and making sure the curriculum frameworks were updated and

compliant with SFC guidance during 2014/15 lay with the then VP Curriculum. In February 2016, the Board agreed that the now VP Curriculum and Quality would undergo a competency hearing to determine if disciplinary action was required. Before the competency hearing was initiated, the VP Curriculum and Quality resigned and left the college in May 2016. He did not receive any severance payment or any other additional payment.

16. Our assessment of all the investigatory material reviewed by the Principal concurs with her findings. We found evidence of concerns and differences of opinion between Management Information Systems (MIS) staff and Heads of Centre over the reliability and robustness of the data being reported to the SFC. Correspondence in October 2014 and March 2015 shows that MIS staff raised concerns with Heads of Centre and with the VP Curriculum about the high levels of additionality. There was evidence of confusion over target and planned activity levels in each of the curriculum areas and a lack of understanding from Heads of Centre about how this information was recorded.

Wider problems with curriculum and recruitment

17. The Principal's review found that the college's over-reliance on additionality was indicative of broader underlying and long-standing problems with the college’s curriculum, linked to difficulties in both recruiting and retaining students. While the college had been aware of some of these issues for a number of years, the college’s efforts to address the problems were inadequate. The Principal noted that both a 2014 curriculum review and a 2015 curriculum 'health-check' had highlighted problems with student numbers and retention, but the college did not take appropriate action to address the problems. The Principal concluded that there was a lack of leadership on curriculum issues, with no-one at the college taking responsibility for ensuring that the curriculum was updated and compliant with SFC guidance.

18. Our assessment of the evidence concurs with the Principal's conclusion that the college's breach of the SFC's guidance on additionality was symptomatic of deeper issues. The evidence indicates that, while management recognised that the curriculum frameworks needed to be fully reviewed and updated following the merger, the college had not taken effective action to do so.

19. At the PAPLSC meeting on 17 November 2016, the Principal accepted that the college was responsible for the underlying problems. Corporately, the college focused on increasing activity per student as a short-term fix, without addressing the deeper issues with student recruitment and retention.

20. As well as putting the transformation plan in place, the college has now completed a full restructuring of the senior management team to improve lines of accountability. With the exception of the Principal, who joined in May 2015, the current Chief Operating Officer is the only remaining member of the senior team that was in place during 2014/15. The executive team is now smaller, with the Chief Operating Officer and one Depute Principal sitting below the Principal, supported by three Assistant Principals.

Progress with the transformation plan

21. The college developed its transformation plan to help it move to a sustainable financial position, by improving operations and the delivery of core activity. It consists of 19 projects, forming four overarching programmes of work:

- financial sustainability: priority-based budgeting, resource management and estates strategy
- curriculum relevance, regional and coherence with community planning partnerships
- workforce development and structure
- recruitment, retention and productivity.

22. The SFC was supportive of the broad direction of the plan but raised concerns about the volume of work to be undertaken and requested prioritisation of work relating to the core curriculum and financial health issues. In July 2016, the college's internal auditor was jointly commissioned by the SFC and the college Board to undertake a detailed review of the plan. The aim of this review was to assess whether the plan was fit for purpose, and to provide assurance to the SFC and the Board on the extent to which the plan was likely to achieve its objectives.

23. The review was completed in September 2016. The internal auditor concluded that, overall, the plan set out the key challenges facing the college and the improvements the college needed to make to address them. It found that the college had made good progress with certain key areas of the plan, specifically with student recruitment and curriculum planning. However, the review also made 12 recommendations, highlighting areas where there was scope for improvement, particularly in relation to the prioritisation of projects, setting SMART objectives and putting in place more robust and consistent project management processes. It also recommended that the financial plan be regularly refreshed and forecasts shown on a monthly basis. The recommendations were accepted by the college and the Board of Management.

24. A Strategic Programme Board, chaired by the Principal, meets every eight weeks. The Depute Principal acts as the Depute Chair and the Programme leads also sit on the Strategic Programme Board. The Strategic Programme Board provides high level governance of the transformation plan. There are also programme boards for the four transformation plan programmes, each chaired by a senior manager. The programme boards meet between every one to two months, depending on progress with the particular programme. The Policy and Resources Committee provides governance of the transformation plan on behalf of the college's Board of Management, and considers progress reports at every committee meeting. A paper presented to the committee in January 2017 reported that the college was making progress across all four transformation programmes.

25. Following the review of the transformation plan, the college has taken positive steps to act on the internal auditor's recommendations to improve governance and project management processes. It appointed a Head of Corporate Development in November 2016, whose role is to set up and run a Programme Management Office (PMO). The college is in the process of

recruiting further staff for the PMO. The Head of Corporate Development has developed a portfolio improvement plan. This is a high-level action plan, incorporating the internal auditor's recommendations. The college is also refreshing the transformation plan to incorporate the internal auditor's recommendations. It is too early to make an assessment of the impact of the PMO, but the external auditor will continue to monitor progress.

Monitoring and reporting

26. The SFC has put in place effective monitoring arrangements, meeting with the college on a monthly basis to monitor progress. The SFC also attends meetings of the Policy and Resources Committee. At these meetings, the college provides updates on progress with the transformation plan on student activity, curriculum planning, staffing issues and the financial position. The SFC believes the college is making progress, particularly with its approach to curriculum planning. It has required the college to provide more robust evidence to support its reporting on progress, including a weekly update on student activity. Based on regular engagement with the college to secure assurances, the SFC is confident that the college will meet, or slightly exceed, its activity target for 2016/17.

27. The SFC is satisfied that the college has improved its financial forecasting and our review of the management accounts supports this view. The finance report which goes to the executive team and the Board every month provides a good level of detail, with narrative to support forecasts and updates to explain movement and variance.

28. Board members told us that, during 2013/14, it became clear that there were financial problems at the college, but that the root cause of the problems was not clear from the information provided to the Board. Although there was no indication that the financial data being provided to the Board was unreliable, it did not explain why the college was not meeting its credit targets. Board minutes show that during 2014/15, the Board was provided with assurances by the executive team that the college would achieve its student activity target. Minutes during this period also show that the Board raised the need for the development of management information to allow for more effective monitoring of application and enrolment data.

29. The auditor found that the quality of information provided to the Board during 2015/16 had improved, particularly in relation to the management accounts and on student recruitment. Board members told us that they are now more confident that the Board and committees are getting the right information to allow them to assess progress, and that the information provided by the management team is more robust.

30. The college has developed a new approach to curriculum planning. Each department within a faculty is set a credit target based on past performance and projected future demand, and credits by department are monitored and reported on. The Assistant Principal for Curriculum told us that previously, projections were more arbitrary, as it was not possible to work out whether a course was efficient or not. The college has taken steps to better understand the relative value of individual courses under the SFC's funding formula.

31. The college has developed a new curriculum planning tool, which is enabling improved monitoring and analysis. For each course, the planner includes information on:

- projected and actual enrolments
- delivery hours
- credit target
- SFC funding
- FTE staff required
- current staff numbers.

32. The curriculum planning tool provides the college with better information on activity across departments and individual courses, allowing the college to monitor and respond to changes in activity and costs, for example by removing inefficient courses from the curriculum. The staffing information also enables the college to assess which areas should be targeted for the third phase of voluntary severance. The auditor will continue to monitor progress with implementation of the revised curriculum.

33. In January 2017, it was reported to the Policy and Resources committee that the early withdrawal rate is currently at 4.3 per cent, compared to 5.2 per cent in 2015/16.

Current financial position and future sustainability

Financial position and SFC support

34. The college's financial position was weak and worsening by the end of 2015/16. The college reported a deficit of £7.0 million in 2015/16 (compared to £5.6 million in 2014/15), which equates to approximately 11 per cent of the college's total income for the year. After excluding pension accounting adjustments, the underlying position for 2015/16 was a £3.6 million deficit (paragraph 3). The college is forecasting a deficit of £3.814 million for 2016/17, a deficit of £0.546 million for 2017/18, and a small surplus for 2018/19.

35. The college was heavily dependant on SFC support in 2015/16 in order to meet its liabilities, and will continue to be so until at least 2018/19. The SFC has agreed to provide a range of support to the college (Exhibit 1). This includes funding to support the voluntary severance schemes (paragraphs 40-41) and a cash advance of up to £2.9 million to support implementation of the transformation plan. The SFC expects the college to repay this advance. Details of the repayment have not been formally agreed, but the college's financial plan for 2015-19 forecasts a three-year repayment period to 2019/20, subject to affordability.

36. The SFC has acknowledged the scale of change required by the transformation plan and the fact that the college may require further support to meet operating and transformation costs. In November 2016, the SFC provided written assurances to the college that it will continue to support the college through to 2018/19, when the transformation plan is due to be fully implemented.

Exhibit 1

Additional support provided to Edinburgh College by the SFC

Nature of support	Value £ million	Timing of receipt	Subject to future repayment
Additional transformation funding	£1.1m	2015/16	No
Additional transformation funding	£0.8m	2015/16	No
Voluntary severance 1	£0.65m	2015/16	No
Total 2015/16	**£2.55m**		
Cash advance funding	£2.9m	2016/17	Yes
Voluntary severance 2	£0.6m	2016/17	No
Voluntary severance 3 (not yet confirmed)	£1.8m	2016/17	No
Total 2016/17	**£5.3m**		
Voluntary severance 4 (not yet confirmed)	£0.25m	2017/18	No
Total 2017/18	**£0.25m**		
Total non-repayable funding	**£5.2m**		
Total	**£8.10m**		

Source: Edinburgh College Annual Audit Report 2015/16

Performance against activity targets

37. The financial sustainability of Edinburgh College is primarily dependent on its ability to deliver its annual activity target and on the outcome of a series of voluntary severance schemes. The college must also effectively monitor its income, expenditure and cash flows, to ensure its financial forecasts remain on track to achieve a small surplus in 2018/19.

38. The college's rebased activity target for 2015/16 was 186,258 credits (paragraph 10). Subsequently the college missed this target, delivering a total of 180,144 credits. The shortfall of 6,114 credits for 2015/16 amounted to £1.1 million in SFC funding. The SFC clawed back this funding and then re-issued it to the college as non-repayable transformation funding. In addition to the £0.8 million re-issued to the college to replace the clawback for 2014/15, this amounts to a total of £1.9 million of transformation funding in 2015/16.

39. The SFC and the college agreed a core activity target of 184,028 credits for 2016/17, plus 2,000 European Social Fund credits. As at 14 March 2017, the college reports that it had delivered 185,074 credits and that it is on track to meet its 2016/17 target. The college is likely to retain the same credit target in 2017/18, based on the SFC's indicative allocations. The college plans to seek modest increases to this target from 2018/19 onwards. Growth will be dependent on the availability of funding from the SFC and on successful delivery of the college's new curriculum.

Voluntary severance schemes

40. The college has planned for four voluntary severance schemes from 2015/16 to 2017/18, with a target reduction in FTE staff of around 134. The college anticipates that, in total, these schemes will deliver recurring savings of £4.6 million by the end of 2018/19 (summarised in Exhibit 2). The SFC is providing £3.3 million of support for these schemes.

41. Phases one and two involved mainly administrative support staff. Phase three, which opens in April 2017, will target academic staff following the curriculum redesign. This will be the most challenging scheme to date. The college is aiming to target specific subject areas as far as possible, but, as it is an open scheme, there is a risk that this phase of voluntary severance may not deliver the staff profile required and the associated savings.

Exhibit 2

Voluntary severance schemes

Dates	Number of staff	SFC funding £ million	Cost £ million	Expected savings £ million
May-June 2016	41	£0.65m	£1.14m	£1.12m (audited)
October-November 2016	26	£0.56m	£0.620m	£0.77m
April-May 2017	c.51	£1.85m	tbc	£2.46m
Feb-March 2018	tbc	£0.25m	tbc	£0.35m
Total	**c. 134**	**£3.31m**	**tbc**	**c.£4.7m**

Source: Edinburgh College Financial Plan

Financial monitoring

42. College financial forecasts are based on a number of assumptions underpinning the success of the transformation plan including the adoption of Priority Based Budgeting to align curriculum and staff planning. Cash flow management is a critical component with efforts required to address cost areas where the college has limited control such as pension and energy costs and the outcome from national bargaining. The college is looking for cost savings beyond those from voluntary severance, and its unaudited management accounts at the end of December 2016 report some success so far in 2016/17, with savings on staff vacancy churn and delayed recruitment, professional fees and catering overheads. Looking further ahead, the college plans to make savings in estate management across the four campuses.

43. Management accounts at the end of December 2016 show that year-to-date performance has reduced the projected deficit for 2016/17 by £0.4 million to £3.417 million. Cash flows are dependent on full draw-down of SFC funding of £2.9 million between March and April 2017, with a forecast year-end cash balance of £0.7 million. Finance staff have carried out high-level sensitivity analysis on the budgeted forecasts for the year to determine the potential impact of various events such as reduced income, increased expenditure in the year, or the timing of voluntary severance acceptances by staff. These demonstrate the vulnerability of the college's finances. Any fluctuation in income or expenditure will affect the size of the deficit and may result in the college requiring further financial support from the SFC.

Conclusion

44. The college now understands the underlying issues which led to its current financial position and is making progress to address these through its transformation plan. It has put in place more robust governance arrangements, which should lead to better and more consistent programme and project management, as well as better monitoring and reporting to both the Board and the SFC. The college reports that it has improved performance against activity targets and is on track to achieve its target for 2016/17.

45. While there is an overall picture of progress and improvement, the college's financial position remains challenging and continued progress is dependant on the college fully implementing its curriculum review in time for the 2017/18 academic year. The college is also heavily reliant on voluntary severance to make savings.

46. The SFC has provided written assurances to the college that it will continue to support the college through the implementation of the transformation plan, and made clear that further support is conditional on the continued delivery of the transformation plan. Any adverse fluctuation in income or costs could affect the college's ability to repay the £2.9 million transformation funding to the SFC, and the college could require further support.

47. The auditor will continue to monitor progress.

Appendix 1

Timeline

Date	Event
22 July 2014	SFC issue 2014/15 funding and activity guidance to colleges
August 2014 -October 2015	College monitors and reports on activity to both the SFC and the Board, providing assurances to the Board that targets would be met
November 2014 - April 2015	Interim Principal in post - puts initial development plan in place
May 2015	New college Principal and Chief Executive takes up post
May 2015	VP Curriculum and VP Quality posts merged
10 October 2015	Deadline for submission of 2014/15 data return for funding purposes by the college to SFC. Accompanying audit certificate and report provided by internal audit
Mid-late October 2015	College notified by SFC that it failed to deliver its agreed activity target and that SFC will seek to recover £0.8 million
November 2015	VP Quality leaves the college on voluntary severance
November 2015	Principal initiates review of the college’s activity targets from the point of merger
November 2015	Principal approached the SFC to request rebasing the college's 2015/16 activity target
December 2015	Board agree 16 point action plan that will form basis of transformation plan
December 2015	SFC writes to the college to agree Principal's request to rebase 2015/16 activity target
February 2016	SFC notify the college that it can retain £0.8 million, that it had originally intended to claw back due to failure to deliver agreed activity target
February 2016	Principal reports to the Board on the outcome of her review of the college's activity targets
March 2016	Final version of transformation plan submitted to SFC
April 2016	College formally publish transformation plan
May 2016	VP Curriculum and Quality (former VP Curriculum) resigns and

Date	Event
	leaves the college
June 2016	Report on Principal's review of activity targets presented to the Audit and Risk Assurance Committee
1 July 2016	New senior management structure in place
September 2016	Internal auditor completes review of the transformation plan, commissioned jointly by the college and the SFC

The 2015/16 audit of Lews Castle College

AUDIT SCOTLAND

Prepared for the Public Audit and Post Legislative Scrutiny Committee by the Auditor General for Scotland

Made under section 22 of the Public Finance and Accountability (Scotland) Act 2000

March 2017

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Introduction

1. I have received the audited financial statements and the auditor's report for Lews Castle College for 2015/16. I am submitting these financial statements and the independent auditor's report under section 22(4) of the Public Finance and Accountability (Scotland) Act 2000, together with this report that I have prepared under section 22(3) of the Act.

2. The purpose of this report is to draw Parliament's attention to concerns about an inability to achieve activity targets at Lews Castle College during 2015/16 and the potential impact on financial sustainability in the longer term.

The auditor’s opinion

3. The auditor gave an unqualified opinion on Lews Castle College's financial statements for 2015/16 but, in his audit report, he highlighted concerns about financial sustainability arising from the college not achieving student activity targets. The auditor also highlighted that delays in appointing board members had a significant impact on governance arrangements and committee meetings in 2015/16.

Background

4. Lews Castle College is an independent legal body with charitable status as defined by the Further and Higher Education (Scotland) Act 1992 (the 1992 Act). It is governed by a board which is responsible for determining the overall strategy of the college and the proper use of public funds, the quality of provision and appointing the Principal and other senior staff. In 2015/16, the college had 2,016 registered students and employed 111 FTE members of staff.

5. Colleges are organised into 13 college regions. Ten of the regions contain a single college, while three are multi-college regions (Glasgow, Highlands and Islands and Lanarkshire). In each multi-college region, there is a regional strategic body which is responsible for planning and funding delivery of learning across all of the colleges in the region. The regional body is also responsible for working with the Scottish Funding Council (SFC) to determine and agree the priorities for the region. Lews Castle College is part of the Highlands and Islands Region, and the associated regional strategic body is the University of the Highlands and Islands (UHI). UHI took on its regional strategic body responsibilities from August 2014.

6. The college's total income in 2015/16 was £5.7 million. The college reported a deficit of £274,000 (five per cent of income). After excluding items that do not reflect in-year financial payments but instead relate to longer-term considerations (that is, depreciation and pension accounting adjustments), and adjusting for the final instalment of short-term strategic funding from the SFC, the finances showed a break-even position.[1]

[1] The SFC provided strategic funding to support a review of the college's processes and procedures for assessing, processing and claiming extended learning support (ELS). ELS is provided for individual students with particular educational support needs who are studying on a mainstream programme.

7. While the college is not in immediate financial difficulty, it failed to achieve its learning activity target in 2015/16. The college has missed its target persistently over an extended period, and the margin by which it missed the target in 2015/16 was significantly higher than in previous years (Exhibit 1). The college sector has experienced significant change over this period. Changes in national policy focus, reductions in funding, the reclassification of colleges as public bodies and changes in regional governance arrangements have created a challenging environment for the sector. Continued under-delivery could result in both a reduction in funding and recovery of funding for activity not delivered.

Performance and financial sustainability

8. The SFC allocates funding to the 13 college regions in Scotland in exchange for each region delivering an agreed volume of student activity. Student activity is measured in 'credits'. In multi-college regions, the SFC provides funding to the regional body for each region. The regional body is then responsible for agreeing activity levels with, and allocating funding to, the colleges in the region. Lews Castle College, like other colleges in the Highlands and Islands region, contributes to the regional target. This means that under-delivery in one college in the region can be off-set by over-delivery in another college.

9. The SFC can seek to recover funding from a region where the target is not met. Any decision by the SFC to recover funding would depend on the wider Highlands and Islands regional performance and the approach taken by UHI.

10. UHI provided Lews Castle College with £3.8 million of funding in 2015/16, of which £2.29 million was for further education activity. The college agreed to deliver 6,376 units ('credits') of further education activity. The college delivered only 5,131 credits, over 19 per cent short of the target. The region, overall, exceeded its target and the SFC did not seek recovery of funding. UHI did not seek any recovery from the college.

11. Historically, the SFC allowed colleges a degree of leeway in achievement of their targets. This was intended to reflect the fact that the circumstances under which some students leave a college are beyond the immediate control of the college. If targets were adjusted to reflect this leeway, the college would have missed the adjusted target in three of the four years in which a leeway applied.[2] The degree by which the college has missed its target has increased significantly since 2012/13 (Exhibit 1). The credits target for 2016/17 remains at 6,376 and will be challenging for the college to achieve.

[2] The SFC leeway was no longer applicable from 2012/13. This was the first year of regional outcome agreements, which incorporate a wider range of measures. The level of funded activity is one of the measures.

Exhibit 1

The college has persistently failed to meet its activity target over a long period of time

The proportion of the target achieved has decreased by 12 per cent since 2012/13.

Accounting Year	Measure	Target	Achieved	Over/(under) (%)	SFC leeway (%)	Achieved within leeway
2008/09	WSUMs	8,935	7,020	(21.4)	2	No
2009/10	WSUMs	8,935	8,333	(6.7)	2	No
2010/11	WSUMs	9,067	8,841	(2.5)	2	No
2011/12	WSUMs	8,699	8,430	(3.1)	5	Yes
2012/13	WSUMs	8,427	7,803	(7.4)	n/a	n/a
2013/14	WSUMs	8,994	8,336	(7.3)	n/a	n/a
2014/15	WSUMs	8,994	8,082	(10.1)	n/a	n/a
2015/16	Credits	6,376	5,131	(19.5)	n/a	n/a

Notes: Prior to 2015/16, learning activity was measured in 'weighted student units of measurement' (WSUMs). The SFC changed the measure to credits from 2015/16.

Source: Scottish Funding Council and Lews Castle College accounts

12. While the SFC did recover funding for under-delivery against target in 2008/09, neither it nor UHI has sought to recover funding from the college in any of the subsequent years. The auditor has highlighted the risk that continued under-achievement could result in reductions in future funding settlements. SFC funding accounts for around two-thirds of the college's total income, and any reduction or recovery could have a significantly detrimental effect on the college's financial sustainability. The current situation also means that the college was funded in excess of what it needed to deliver its levels of activity. In effect, other colleges in the region subsidised Lews Castle College..

Reasons for under-delivery

13. The college has indicated that the national policy focus on full-time courses leading to employment (introduced in 2009) and on provision for young people (2011) affected the college's ability to meet targets. The college previously catered for a larger proportion of part-time learners and older (over 24 years of age) learners. The college has also indicated that a changing local demography, particularly a reduction in the number of young people, has contributed to the college's difficulty in delivering the target. The board and its committees did consider performance regularly, including the risks associated with under-delivery, but there is little evidence of the board taking effective action to adjust the college's operations to address these risks and the changes described above. The college did develop new marketing, employer engagement and curriculum strategies from 2014, but these have not delivered intended increases in student numbers.

14. The SFC began to introduce a new funding model for the college sector in 2015/16.[3] Both the college and UHI have acknowledged that delays in them fully understanding the effects of this change led to difficulties in applying a revised approach to the allocations made by UHI for 2015/16. Instead, UHI based the 2015/16 allocations, of both funding and targets, on 2014/15 figures, and the college cites this as a significant factor in the disparity between its performance and its target in 2015/16. Essentially, it considers the target was higher than it should have been. UHI is working with colleges in the region during 2016/17 to review and, where necessary, adjust the targets to reflect the change in the funding model. UHI plans to implement a new allocation approach in 2017/18. Lews Castle College expects this work to result in its activity target reducing significantly, with the revised target likely to mirror current activity.

15. The prospects of the college successfully resolving issues relating to under-delivery will be dependent on the outcome of the UHI review described at paragraph 14. A significant reduction in target will have implications for the college's funding allocation. Given the relatively small size of the college, and the area it covers, any significant reduction in funding would be a challenge. The college is currently considering the cost reduction measures that might be necessary to accommodate the reduction in funding.

Governance

16. Delays in board appointments significantly affected governance arrangements during 2015/16. Seven experienced independent members left during the year, including the Chair.[4] The Board's standing committees did not meet between December 2015 and October 2016. During that period all committee business, other than that of the audit committee, had to be considered by the Board in full at its meetings in March, June and September 2016.

17. New Board members are now in place. Of the 13 current members, six had served on the board in the years immediately prior to 2015/16 and one served on the Board in a previous period. At the time of the annual audit, a full induction process had not been completed for new members. However, by the time this report was prepared, all but one new board member had received induction training. While there is no indication that the absence of standing

[3] Prior to 2015/16, 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). The new funding model removes the weightings applied under WSUMs and instead categorises courses in five price groups. Each group has a credit value attached to it. 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.

[4] This high turnover reflects the fact that a new board was established at the point of regionalisation, following implementation of the Post-16 Education (Scotland) Act. Many of the departing members' appointment terms ended during 2015/16.

committees affected delivery targets, the new board will play a key role in implementing necessary changes to the college's activity target and to its cost base.

Conclusion

18. Lews Castle College is not in immediate financial difficulty but its failure to effectively address underlying problems with its activity target places the college at risk of financial penalty and funding reductions. It needs to take steps now to agree an appropriate activity target with UHI, and to make adjustments to its cost base to match this. I note that the college is working with UHI to address this and I have asked the auditor to keep the position under review.

The 2015/16 audit of Moray College

Prepared for the Public Audit and Post Legislative Scrutiny Committee by the Auditor General for Scotland

Made under section 22 of the Public Finance and Accountability (Scotland) Act 2000

March 2017

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Introduction

1. I have received the audited financial statements and the auditor's report for Moray College for 2015/16. I am submitting these financial statements and the independent auditor's report under section 22(4) of the Public Finance and Accountability (Scotland) Act 2000, together with this report that I have prepared under section 22(3) of the Act.

2. The purpose of this report is to draw Parliament's attention to concerns about financial management and sustainability at Moray College.

The auditor’s opinion

3. The auditor gave an unqualified opinion on Moray College's financial statements for 2015/16 but, in her audit report, highlighted concerns relating to the financial position. During the year, the college needed to urgently draw down an advance on its funding allocation for 2016/17 from the University of the Highlands and Islands (UHI) as it did not have enough money to meet its operational costs. The auditor concluded that the current financial position was not sustainable and that the college needs to take action to achieve financial balance. The college's recovery plan has been submitted to UHI and the Scottish Funding Council (SFC).

Background

4. Moray College is an independent legal body with charitable status as defined by the Further and Higher Education (Scotland) Act 1992 (the 1992 Act). It is governed by a Board which is responsible for determining the overall strategy of the college and the proper use of public funds, the quality of provision and appointing the Principal and other senior staff. In 2015-16, the college had 4,184 registered students and employed 249 FTE members of staff.

5. Colleges are organised into 13 college regions. Ten of the regions contain a single college, while three are multi-college regions (Glasgow, Highlands and Islands and Lanarkshire). In each multi-college region, there is a regional strategic body which is responsible for planning and funding delivery of learning across all of the colleges in the region. The regional body is also responsible for working with the Scottish Funding Council, to determine and agree the priorities for the region. Moray College is part of the Highlands and Islands Region, and the associated regional strategic body is the University of the Highlands and Islands. UHI took on its regional strategic body responsibilities from August 2014. Moray College received 72 per cent of its 2015/16 income from the Scottish Funding Council (SFC). These grants were allocated by UHI as the regional strategic body. The college also received income from course fees, research grants and contracts.

6. The college's total income in 2015/16 was £12.1 million. The college reported a deficit of £876,000 (seven per cent of income). After excluding items that do not reflect in-year financial payments but instead relate to longer-term considerations (that is, depreciation and pension accounting adjustments), the underlying deficit would be £158,000.

Financial management and reporting

7. In my report, *Scotland's colleges 2016*, I highlighted that the college had received a cash advance of £568,000 from UHI during 2014/15. This was required to meet immediate commitments, following a failure by the college to adjust its budget to reflect changes in higher education funding. The college repaid this in full by the end of October 2015. However, the college had to make another request for funding in 2015/16, requesting £697,000 of advance funding (six per cent of income) in June 2016.

8. In 2014/15 the auditor stated that Board and committee minutes did not evidence decisions or agreed actions to address the college's financial challenges and concluded that there needed to be clearer evidence of the decisions taken by the Board and its committees following their consideration of the financial position. While the college took steps to address concerns raised by the auditor in 2014/15, these were not sufficient.

9. The college was forecasting an end-year surplus of £145,000 in January 2016. By April 2016, this had changed to a forecast deficit of £499,000. The auditor found that the management accounts analysed the areas of overspend but did not provide explanations for variances between budgets and forecasts. Neither did they indicate why the issues were not identified earlier so alternative action could have been considered. In addition, there was a lack of audit trails to support some budget and forecast figures included in management accounts.

10. The cash advance of £697,000 included the following items:
    - repayment of the outstanding amount of £368,000 in respect of the 2014/15 cash advance
    - an invoice for £46,000 from HMRC following a failed bid for VAT relief during the construction of a major capital project and a remaining payment of £83,000 in connection with the same project
    - a funding claw back of £79,000 for a project review by European Regional Development Fund auditors
    - a backdated amount of £60,000 following implementation of a national pay award
    - delay in the release of European Structural and Investment Fund (ESIF) grant income to the college of £39,000.

11. The college's 2015/16 budget and cash flow were initially prepared in June 2015 but subsequent revisions were not fully updated to reflect the effect of unplanned amounts on cash flow, for example the backdated national pay award and the delay in ESIF grant income. Consequently, the cash flow position in 2015/16 was lower than the college had been planning for. In April 2016, the Board was advised that the college would be in a cash deficit position by July 2016 and would need a cash advance from UHI.

12. Between April 2015 and February 2016, the college was operating without a permanent Principal. The Director of Finance was on long-term absence from August 2015 until formally retiring on 31 July 2016. The Acting Principal took on the Director of Finance role during this time and day-to-day financial management was provided by the accounts team, led by an

Assistant Accountant. The auditor concluded that the team was competent but that more capacity was needed. The auditor previously flagged concerns about a lack of senior financial expertise in her audit report on the 2014/15 financial statements. Following the appointment of a new Principal in March 2016, an interim Director of Finance was appointed on a part-time basis in June 2016 to develop a financial forecast and plan for the next three years.

Financial sustainability

13. The auditor highlighted a number of contributing factors that are indicative of the difficulties the college faces:

- deficits reported on income and expenditure statements year-to-year
- the net current liability position is increasing each year
- the decision to delay property repairs as a short-term funding solution may lead to increased costs in the future, accelerated deterioration in the value of the assets and an adverse impact on students' learning experiences
- failure to achieve financial targets against resource limits.

14. The current financial position is not sustainable. The college's 2015/16 accounts forecast a deficit of £641,000 in respect of 2016/17 and the college has identified funding shortfalls until 2019. At February 2017, the college reported that its forecast deficit for 2016/17 is £472,000. There is a risk that the college will not secure the necessary efficiencies to meet the estimated shortfall in the longer term. The auditor's report highlights that the college is currently faced with a level of staff costs which appear unsustainable. Staff costs were £9.4 million in 2015/16, and accounted for 72 per cent of gross expenditure. This is higher than the average for Scotland's colleges overall (63 per cent of gross expenditure). In light of the college's restriction on non-pay expenditure in 2016/17, the auditor questioned 'whether more can be saved without impacting on the learning experience'. The auditor concluded that a fundamental change is required to reduce the cost base and deliver a sustainable, balanced budget.

Recovery plan

15. The Principal (appointed in March 2016) has reviewed the college's activities and its associated income and expenditure streams. The college began discussing a recovery plan with UHI in June 2016 and the plan was submitted to the SFC in February 2017. The college has already implemented a temporary freeze on the recruitment of support staff. It is also considering a severance scheme to reduce costs - this is likely to require additional funding from the SFC. The college also identified a need to appoint a senior staff member in the finance team. UHI has appointed a Director of Finance who will be seconded to Moray College for at least two years. Other actions proposed include:

- a review of activity targets, to determine whether a change in allocation is appropriate (this is part of a regional review with UHI)
- increasing income generation.

16. It is clear that the college will have to work closely with both UHI and the SFC in order to implement all of the actions needed to achieve recovery.

Timeline of events

17. A timeline of key events is included at Appendix 1.

Conclusion

18. Moray College had a significant underlying deficit in 2014/15, which I commented on in my report, *Scotland's colleges 2016*. The college has again experienced difficulties in managing its finances within budget in 2015/16. Moray College will continue to face financial difficulties without fundamental changes to its costs and financial management arrangements. The college is taking steps to address its financial difficulties but as yet has to agree its recovery plan with the SFC. The organisations need to agree actions as a matter of urgency. It is important that UHI as the regional body ensures that the college is able to deliver on its priorities within the resources available. The College Board will also have an important role to play in monitoring the college's progress with its agreed recovery plan. I have asked the auditor to keep the position under review.

Appendix 1

Timeline

Date	Event
August 2014	New Principal appointed
March 2015	Principal left by mutual agreement
March 2015 - February 2016	Acting Principal arrangements in place (the Assistant Principal was acting up as Principal)
June 2015	The college needed to draw down £568,000 cash in advance from UHI to meet immediate commitments
By 31 July 2015	£200,000 repaid leaving a balance of £368,000
June - August 2015	Detailed review of Moray College's financial position reported to UHI's Finance and General Purposes Committee
11 August 2015	UHI sent a letter to the Chair of Moray College highlighting serious concerns and requesting a number of urgent actions in return for the short-term funding.
October 2015	The college cleared the balance of £368,000
August 2015 - July 2016	Director of Finance on long-term absence
March 2016	New Principal appointed
31 July 2016	Director of Finance retired
June 2016 to present	Part-time Interim Director of Finance in post to assess the financial position within the college and develop a financial forecast and plan for the next three years
June 2016	The college requested an advance of £697,000 from UHI to meet immediate commitments.
At 31 July 2016	£658,000 of the cash advance still owed at the end of the month.

Date	Event
August 2016	Cash advance fully repaid.
August 2016	Ten non-executive members of the college board (from a total of 18) resigned. Nine new appointments were made. This was part of a national refresh of college boards of management. The refresh was due at the end of 2014/15 but was deferred following the departure of the Principal in March 2015 in order to provide continuity until a new Principal was appointed. Four members (including the Acting Chair) provided continuity during the period of transition between boards.
June 2016 - ongoing	UHI in discussion with Moray College about its recovery plan and possible solutions.
November 2016	Moray College provided an update and position statement on the Recovery Plan to UHI
December 2016	Moray College submitted a formal request to the SFC, through UHI, for approval and funding for a voluntary severance scheme
January 2017	Moray College incorporated UHI and SFC feedback into the final version of the Recovery Plan
2 February 2017	Moray College's board approved the Recovery Plan.
8 February 2017	UHI received Moray College's Recovery Plan without amendment
13 February 2017	UHI submitted the final Recovery Plan to the SFC.

Scotland's colleges 2017

AUDITOR GENERAL

Prepared by Audit Scotland
June 2017

Auditor General for Scotland

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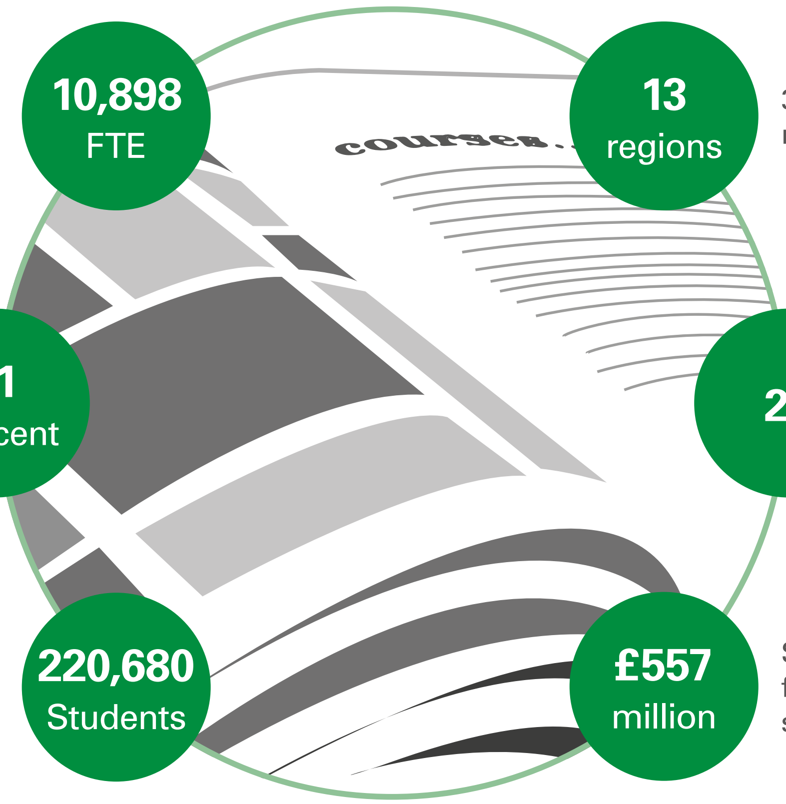


10,898 FTE — Staff in incorporated colleges in 2015-16

13 regions — 3 of which contain more than 1 college

51 per cent — Female students in incorporated colleges in 2015-16

20 — Incorporated colleges

220,680 Students — Studying at incorporated colleges in 2015-16

£557 million — Scottish Government funding to the college sector in 2015/16

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 Board[4]
- 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.

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

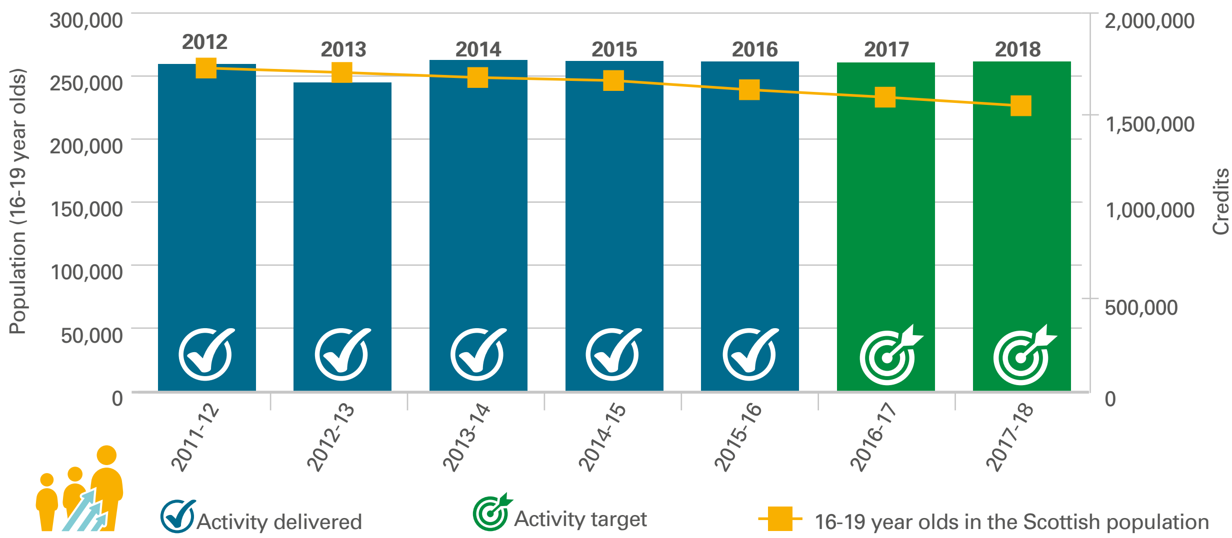
The college sector has continued to exceed the national target for learning activity in 2015-16 but delivered slightly less activity than in 2014-15

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.

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).

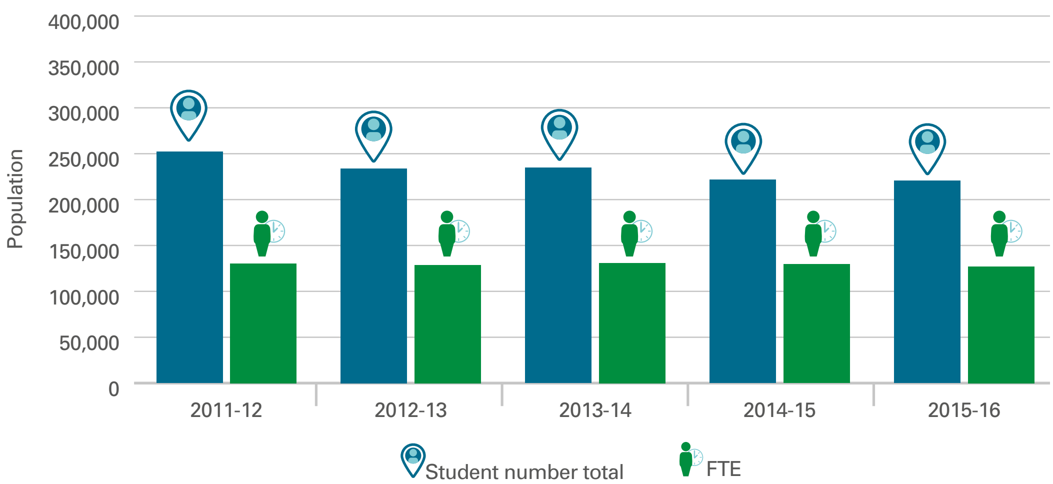
11. The Office for National Statistics' (ONS) Labour Market Statistics indicate that the number of young people (aged 16 to 19) in Scotland is reducing Exhibit 1 (page 9).[7] Data is not readily comparable across all school leaver destinations, but Scottish Government data shows that more young people 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.

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

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.

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]

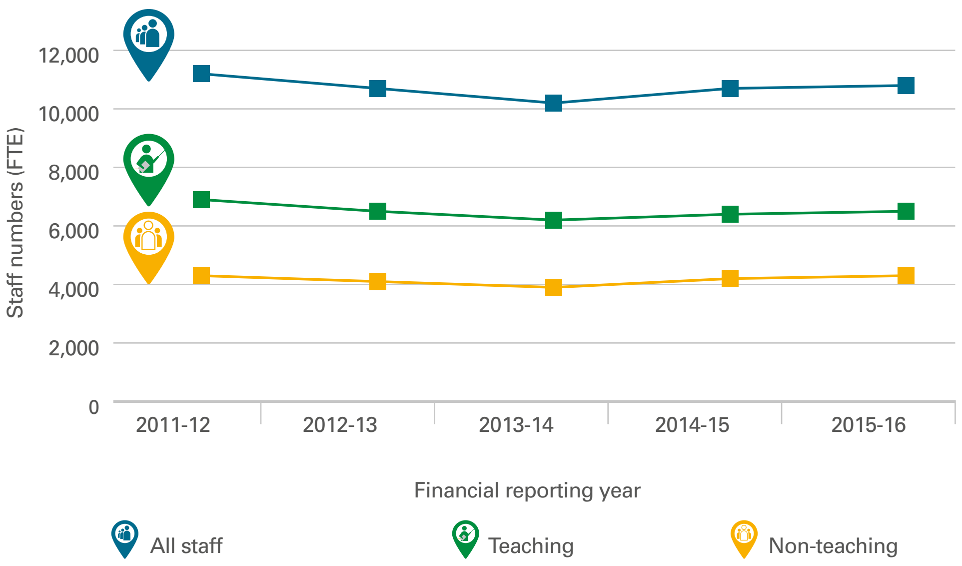
43. Teaching staff numbers have risen by 317 (five per cent) since 2013-14. From discussion with colleges, the main reasons for the increases are increasing credits targets for expanding colleges (including European funded places) and changes in curriculum or service delivery. An element of the increase 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).

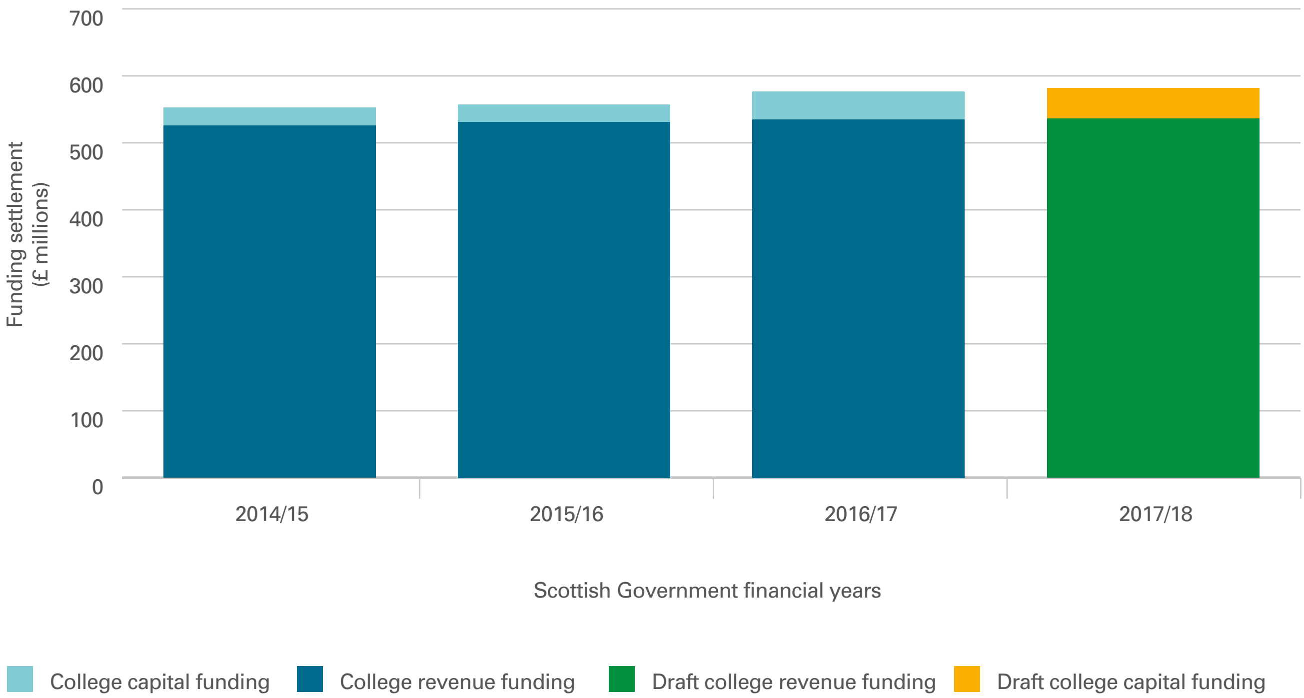
46. The Scottish Government funding allocation to the sector is in two distinct parts. The larger part (95 per cent in 2015/16) is called revenue funding and is used to fund running costs such as paying staff and buying goods and services. The sector is due to receive an increase in revenue funding of £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:

1. 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).
2. 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)

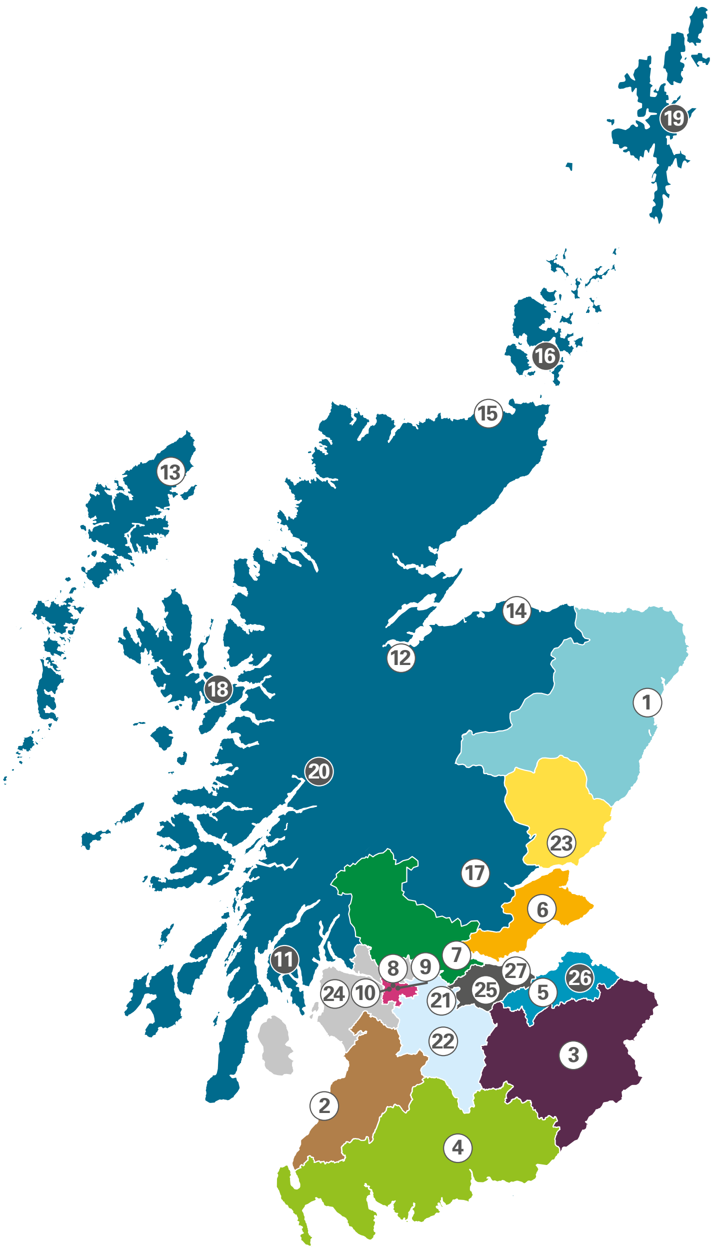
The introduction of the new SORP has led to a significant decrease in college net assets and to five colleges reporting a net liabilities position, where previously there was none. This is because of a change in how government capital grants are presented in college accounts. These grants are shown as 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
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 but counts towards the achievement of the national target for colleges.

Source: Audit Scotland

Scotland's colleges 2017

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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk

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Audit Committee

DRAFT – ANNUAL REPORT OF THE AUDIT COMMITTEE 2016-17

1 PURPOSE OF REPORT

1.1 To advise the Board of Management of the activities and decisions of the Audit Committee during Financial Period 2016-17 and to provide opinions on matters specified by the Code of Audit Practice.

2 BACKGROUND TO REPORT

2.1 It is a requirement of the Code of Audit Practice and the College's Standing Orders and Financial Regulations that the Audit Committee provides the Board with an Annual Report so that all members of the Board can be fully informed of, amongst other things, aspects of the system of Internal Control.

3 ADMINISTRATIVE MATTERS

3.1 The period covered by this report is the twelve month period 1 August 2016 to 31 July 2017.

3.2 The membership of the Committee during the period was:

Hugh Carr, Chair
Delia Holland
Pat Kirby
Stuart Martin

3.3 Other attendees at Audit Committee meetings include:

Carol Turnbull, Principal
Jannette Brown, Vice Principal Corporate Services and Governance
Kay Bird, Secretary to the Board until February 2017
Anne Walsh, Secretary to the board from March 2017
Karen Hunter, Finance Manager
Representative from RSM, Internal Auditors
Representative from Grant Thornton, External Auditors (until December 2016)
Representative from Scott Moncrieff, External Auditors (from January 2017)

3.4 During the relevant period, the Committee's formal meetings were as follows:

Date of Meeting:	Board members present:
20 September 2016	Hugh Carr Delia Holland
21 November 2016	Hugh Carr Pat Kirby Stuart Martin
21 February 2017	Hugh Carr Pat Kirby Stuart Martin
10 May 2016	Hugh Carr Pat Kirby Stuart Martin

There was an average attendance of 2.75 members (69%).

4 INTERNAL AUDIT

4.1 RSM acted as internal auditors throughout the year.

4.2 RSM have provided their Annual Audit Report for 2016-17. The opinion for the 12 months ended 31 July 2017 was as follows:

'***Head of internal audit opinion 2016-17***

The College has an adequate and effective framework for risk management, governance and internal control.

However, our work has identified further enhancements to the framework for risk management, governance and internal control to ensure that it remains adequate and effective.'

A copy of the full report is detailed in RSM's Annual Internal Audit Report - Year ended 31st July 2017.

4.3 A summary of the internal audit undertaken, and the resulting opinions, is provided below:

Assignment	**Assurance level**	**Actions agreed**		
		H	**M**	**L**
Income Generation	Reasonable assurance	0	4	1
Follow of Previous Internal Audit Recommendations	Reasonable progress	1	2	1
IT Cyber Security	Reasonable assurance	0	2	3
Estates Management – Reactive Maintenance	Reasonable assurance	0	5	2
Student Support Fund	Substantial assurance	0	1	0
Student Activity Data	Substantial assurance	0	0	0
Safeguarding including the Prevent Agenda	Substantial Assurance	0	1	2
Marketing and Communication	Partial Assurance	2	2	2
Total (2016/17)		**3**	**17**	**11**
Total (2015/16)		1	9	13

4.4 The recommendations are categorised by the auditors according to the level of priority – High, Medium and Low, and are prioritised to reflect the auditors' assessment of risk associated with the control weaknesses.

In addition, Suggestions may be included as part of the Action Plan reported. These are not formal recommendations that impact the overall audit opinion, but used to highlight a suggestion or idea that management may want to consider.

17 of the recommendations made during the year were categorised as Medium Priority, with 11 categorised as Low Priority.

Three High Priority management actions were made during the year.

4.5 Where a recommendation is not accepted this is documented in the individual audit reports considered by the Audit Committee. In general, recommendations may not be accepted where it is considered that the benefits of implementation are outweighed by the costs.

4.6 Assurance on the adequacy of internal controls within the College arises only from the results of reviews that have been completed during the period in accordance with the programme approved by the Audit Committee. In this context it is important to note that:

- It is management's responsibility to maintain internal controls on an ongoing basis;
- The internal audit function forms part of the overall internal control structure of the Board; and
- Whilst the Internal Auditors have planned their work so that they have a reasonable expectation of detecting significant control weakness, internal audit procedures do not guarantee that fraud will be detected.

It is the responsibility of internal audit to assess the adequacy of the internal control arrangements put in place by management and to perform testing to ensure that these controls were operating for the period under review.

5 EXTERNAL AUDITORS

5.1 The external auditors for the period to 31 July 2016 were Grant Thornton UK LLP, 7 Exchange Crescent, Edinburgh EH3 8AN, which was the final year of their appointment.

5.2 Audit Scotland appointed Scott Moncrieff as external auditors for the five year period 2016-17 to 2020-21.

5.3 The fundamental objective of the planning, approach and execution of the audit is to enable the auditors to express an opinion on whether or not the financial statements, as a whole, give a true and fair view of the activities of the College since the last audit and of its state of affairs as at the Balance Sheet date.

5.4 We confirm that the external auditors have been approved by the Auditor General in accordance with the Code of Audit Practice and the letter from the Auditor General dated 20 April 2000 for provision of external audit services for the financial period 2015-16.

5.5 The external audit of the financial statements for the period ended 31st July 2017 will commence in September 2017, and Scott Moncrieff are expected to issue their external audit report in November.

6 THE FINANCIAL STATEMENTS

6.1 The External Auditors will provide their Annual Report to the Board of Management following completion of their external audit work, as noted above.

7 VALUE FOR MONEY PROGRAMME (VFM)

7.1 RSM did not perform a specific value for money review at the College, but considered the value for money arrangements as part of the Income Generation and Estates Management – Reactive Maintenance reviews.

7.2 Both reviews resulted in reasonable assurance opinions and management actions were raised to improve the control framework.

8 OTHER MATTERS

8.1 There are no matters arising from trusts, joint ventures, subsidiary or associated companies.

8.2 There were no issues of alleged fraud/irregularity investigated during the audit period.

8.3 There are no foreseeable events that will affect the work of the Audit Committee.

9 GOOD GOVERNANCE

9.1 In line with the 'Code of Good Governance for Scotland's Colleges' the College Internal and External Auditors have access to the Audit Committee members to discuss any issues without College staff being present.

9.2 At the Audit Committee meeting held on 20 September 2016, the Chair asked members of the Executive Management Team and Finance Manager to withdraw from the meeting in order for the Committee to meet privately with internal and external auditors. The Chair sought feedback from internal and external auditors on any matters they wished to raise without staff present. Both advised there was no issues with the college and everything was in order with a good risk management policy imbedded

10 OPINION

10.1 The Audit Committee's opinion will be reported for the final report following completion of the Financial Statements audit, when the External Auditors' reports are available.

11 RECOMMENDATION

11.1 It is recommended that the Board take note of the work of the Committee for the period August 2016 to July 2017.

Board of Management

Dumfries and Galloway College

Marketing Strategy 2017-2020

1 Introduction

Dumfries and Galloway College aims to deliver the highest quality learning for our students, to make a positive contribution to the local and national economies and to utilise the expertise of our staff to deliver continuous improvements.

As a service organisation the College recognises that it must maintain a high public profile to promote the courses and services it offers to people in the area it serves.

Good communication is key to improve people's understanding of what the College is and what it can provide.

Marketing in the context of this strategy refers to the whole range of activities involved in establishing and maintaining the College's public image and publicising its services to individuals and organisations. It includes activities, therefore, which are known variously as: publicity, public relations, events management, design, advertising, communication and estates enhancement.

2 Marketing Strategy Aim

The overall aim of the Marketing Strategy is to establish a framework for effective communication with individuals, communities, industry and other organisations about the education and training opportunities offered by the College and to ensure achievement of activity targets.

In working towards this aim the College will continue to develop appropriate regional branded publicity materials, communication and media channels.

3 Marketing Strategy Objectives

- Support the development of the Colleges courses and progression routes in line with identified customer demand and government priorities.
- Promote the College's services and facilities to potential students in order to achieve student recruitment targets.
- Promote the College's services and facilities to businesses and industry partners to foster employer engagement and partnership working
- Promote HNC/HND articulation links between the College and local (and other) universities.
- Provide PR and Communication support.
- Support College activities and events including those of the Student Association.
- Manage and develop the College's online and social media presence and brands.
- Support the College in fostering a climate of equality and diversity for all staff and students.

4 Implementation of the Strategy

Board of Management

4.1 The Marketing Team will support the development of College courses and progression routes by:

- Providing structured information relating to the education and training needs of individuals and organisations to course teams to use during the processes of planning and approving new provision.
- Assisting with liaison between Curriculum teams, partners and other stakeholders to create clear progression routes from school and community services into College and from College into employment or university, taking account of government priorities and identified customer demand.

4.2 The Marketing Team will promote the College's services and facilities to potential students by:

- Developing content for the College website.
- Developing printed marketing materials.
- Maximising use of social media and other digital technologies to advertise college courses, facilities and activities – ensuring effective frequency, media impact, timing and reach across press, print, radio, TV and online media.
- Organising Public Relations activities to increase the profile of the College.
- Direct mail and social network marketing activity.
- Attendance at internal and external events aimed at potential customers.
- Promoting the College through public events – graduations, open days, employer events, exhibitions and end of year shows and celebrations, and other student events.

4.3 The Marketing Team will promote the College's services and facilities to businesses and industry partners to foster employer engagement and partnership working by:

- Supporting Employer engagement events.
- Promote college services and facilities to local businesses and industries.
- Promoting examples of college-employer partnership working in the College's publications and press releases.
- Collating profiles of successful partnership working with employers/industry for use in publications.
- Encouraging and facilitating employers to advertise job vacancies to students using the college website and social media networks as well as internal communication channels.

4.4 The Marketing Team will promote HNC/HND articulation links between the College and local (and other) universities by:

- Liaising with University of Glasgow, UWS, and the Open University to promote articulation opportunities and other link courses.
- Developing appropriate links between College and University web sites.
- Liaising with Universities to update HNC/HND articulation links and produce the progression section in the College's online prospectus and course information.
- Supporting University progression events.
- Promoting University progression in the College's publications and press releases.

4.5 The Marketing Team will provide PR and Communication support by:

- Encouraging Schools/Senior Management/Board members and Cross College personnel to advise of potentially positive or negative news items and establish and maintain a continuous flow of information to the media.
- Liaising with College partners and co-ordinating the distribution of news items to the media that highlight good practice and working partnerships, as required.
- Recording student and staff successes.
- Collating profiles of successful students for use in publications.
- Supporting annual student celebration events and associated PR.

4.6 The Marketing Team will support the College's programme of activities and events including those of the Student Association by:

- Supporting and organising key College events – awards ceremonies, exhibitions, opening events, seminar events with key partners, open days.
- Providing advice to Curriculum and Support Teams in organising course or team-specific events.
- Developing materials for use in course and team-specific events.

4.7 The Marketing Team will manage and develop the College's online and social media presence and brands by:

- Establishing design parameters for the College's website to ensure consistency.
- Agreeing the protocols and processing for approving and uploading contents.
- Creating links to partner and stakeholder websites as required.
- Organising e-marketing campaigns.
- Managing social networking activities by the College

4.8 The Marketing will support the College in fostering a climate of equality and diversity for all staff and students by:

- Ensuring graphics and photographs used in publicity materials promote equality, diversity and inclusiveness, sensitive to the target group.
- Disseminating information that reinforces messages of equality and diversity through public information systems.

5 Responsibility for the Strategy

The Marketing Manager will have overall responsibility for the delivery of this strategy and is accountable to the Principal for the execution of the Strategy.

Status:

Approved by:	Executive Management Team
Date of Version:	August 2017
Responsibility for Strategy:	Principal
Date of Review:	August 2020

Audit Committee

Strategic Risk Register

1. Introduction

1.1 The purpose of this paper is to provide the Audit Committee with the opportunity to review the College's Strategic Risk Register.

2 The Report

2.1 In accordance with the College's Risk Management Policy any risk with an inherent rating of 12 or above must have mitigating controls in place and where the residual rating remains above 12 should be reviewed at least quarterly in order to identify if any further actions could be taken to reduce the residual rating to below 12. For completeness all risks are included in the attached register, in order of high to low ratings.

2.2 The Principal and Executive Management Team routinely review the Strategic Risk Register to reflect the risks the College is facing and the mitigation that will be applied to each risk. There are currently 9 strategic risks, four of which are rated 12 or above.

2.3 No new risks have been added but changes have been made to the following:

- Risk No 6 – 'Failure to achieve attainment targets'. Residual Risk has been increased to 12
- Risk No 3 – 'Governance issues'. Recommendation to remove comments as little funding left in ALF
- Risk No 13 – 'Cyber Attack'. Inherent Risk has been increased to 12
- Risk No 4 – 'Unable to achieve credit (activity) target'. Residual Risk has been increased to 12
- Risk No 10 – 'Imbalance between demand for student support funds/bursaries and funds available'. Propose to remove from Strategic Risk Register

3. Recommendation

3.1 It is recommended that the Audit Committee consider and, if so minded, approve the Strategic Risk Register.