

Paul Johnston
Director - General Learning and Justice
Scottish Government
St Andrew's House
Regent Road
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EH1 3DG

5 May 2017

Dear Paul

I have pleasure in enclosing the clearance draft of our report Scotland's colleges 2017. The report reviews how colleges have performed in terms of learning provision and provides an update on the sector's finances.

I would be grateful if you could confirm by 25 May that you are satisfied with the factual accuracy of the report, including all the data and information provided by or relating to your organisation.

During the course of the audit, our contact from the Scottish Government was [REDACTED]

We are also providing John Kemp, Interim Chief Executive, the Scottish Funding Council, with a copy of the report today seeking his comments.

We are currently seeking the views of the sector regarding our financial analysis detailed in exhibits 5, 9 and 10. As such, the figures presented here may be subject to change.

If you have any comments on the report, or if there are any significant issues that require review, it would be extremely helpful if your office could liaise with [REDACTED] before 25 May. The audit team would be happy to meet with you during the clearance period, if this would be helpful.

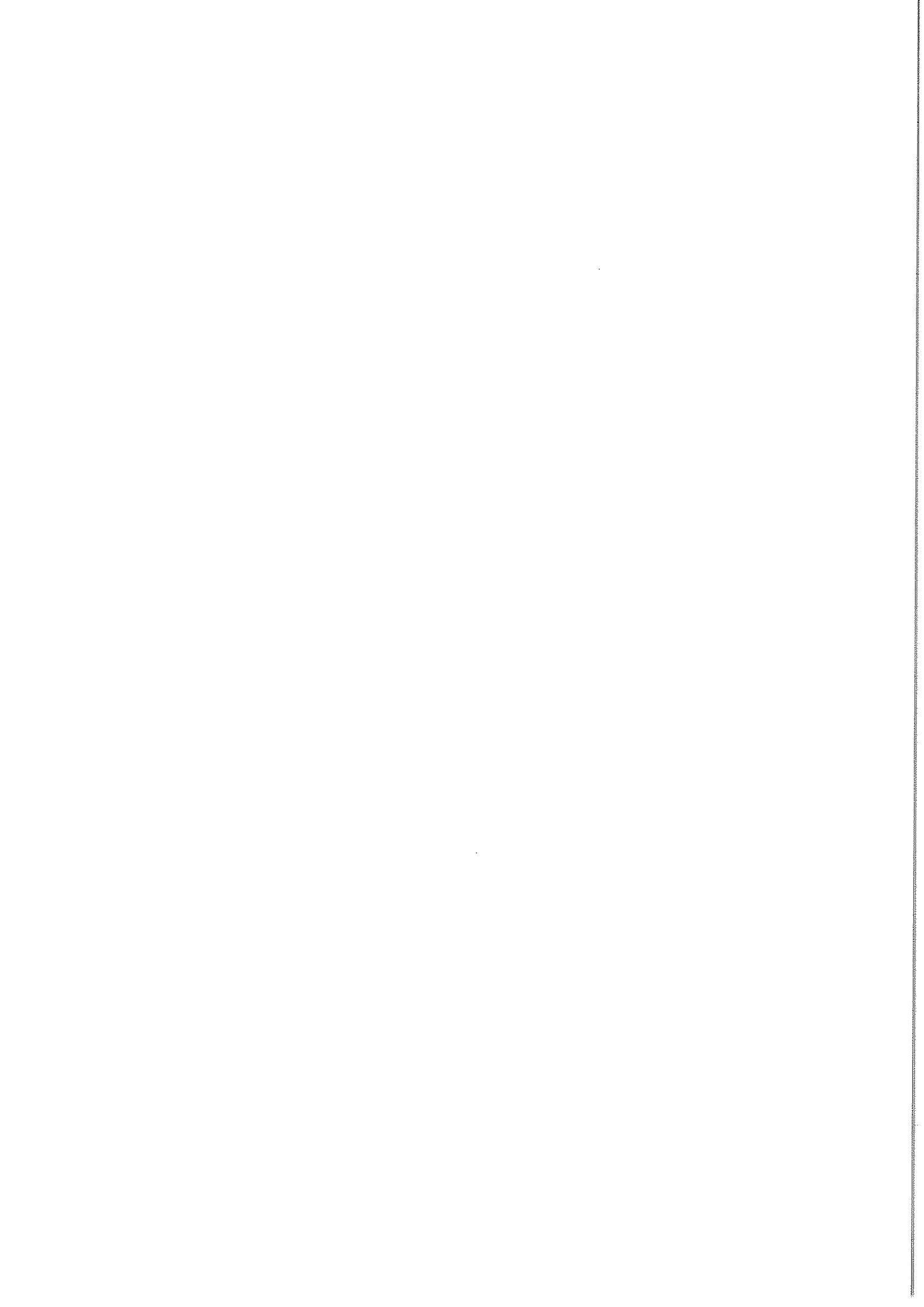
You may wish to refer to our formal protocol if you require clarification of this process.
(<http://www.scotland.gov.uk/Topics/Government/Finance/spfm/agsappendixB>)

The intended publication date for this report is 22 June. I will present the report to the Public Audit Committee in due course.

Yours sincerely



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Scotland's Colleges 2017

24 May 2017

Dear Caroline

Thank you for advance sight of the draft report for clearance on Scotland's Colleges 2017.

I appreciate the regular flow of communication that has underpinned the compilation of this year's report which has undoubtedly helped in the drafting of the final report.

There has been good progress made in a number of areas highlighted in Scotland's Colleges 2016 including: public reporting by the Scottish Funding Council of the impact and success of the programme of college mergers in Scotland; commissioning of a national college estate condition survey to use as a basis to prioritise future capital investment; and improving accountability and transparency through additional guidance to colleges detailing the process colleges now have to follow if they incur a deficit as a result of spending net depreciation funds.

An initial meeting was held between Scottish Government, Scottish Funding Council and Audit Scotland officials on 17 May 2017 to discuss the 2017 report. My colleagues highlighted a small number of areas where it is felt that the tone of the report could be more balanced as well as the reference point for statistical comparisons. The report compares data as far back to 2008 when perhaps a more relevant reference point could be used to more fairly reflect recent changes in the sector i.e. the college merger programme from 2012 onwards.

I note your assessment that the financial health of the sector remains relatively stable but has deteriorated since 2014-15. You will of course be aware of the increased funding (capital and revenue) made available to the FE sector in the 2017/18 budget which should improve the financial outlook.

I have provided an initial reply to your key messages and recommendations in Annex A.

I would be more than happy to have a further discussion on the report contents prior to publication.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Paul Johnston', written in a cursive style.

Paul Johnston
Director General Learning and Justice

Key Messages

Key Message	Scottish Government Position
<p>The sector has continued to exceed the national target for learning but delivered less activity than in 2014-15. Two regions failed to meet their target resulting in a reduction in funding for one college. Highlands and Islands region met its overall target but two colleges within the region failed to meet their targets. Changes in demography and in school leaver destinations will make it harder for the sector to continue to achieve the national target.</p>	<p>The position in Highlands and Islands relate to Lews Castle College and Moray College. Both Colleges are subject to Section 22 reports and are very high risk in the SFC intervention list. Overall the UHI Region met the target however we will continue to work with the SFC to ensure the appropriateness of targets set for individual colleges.</p>
<p>The number of college students has continued to fall and is at its lowest level since 2008. 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 national level, so it is not possible to say whether the decreases reflect a fall in demand.</p>	<p>It is noted that whilst student numbers are falling in terms of headcount the FTE places remain stable, although it is agreed that the 116k FTE places target continues to stretch the colleges. The reduction in headcount could be attributed to fewer part-time courses and more full time courses that are still helping to achieve the FTE target.</p>
<p>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 66 per cent) and is now at the same level as that achieved in 2013-14. Most students continue to be satisfied with their college experience and go on to a positive destination, such as further study, training or employment.</p>	<p>Welcome the increases highlighted by the report.</p> <p>The Minister for Further Education, Higher Education Science also announced an improvement project on 31 March 2017 to look specifically at applying improvement science techniques in Scotland's colleges to improve attainment and retention rates over the next two academic years.</p>
<p>The financial health of the college sector remains relatively stable but has deteriorated since 2014-15. The underlying deficit has increased to £8 million, net assets have decreased by £48</p>	<p>As suggested to Audit Scotland officials, it is perhaps more informative to explain this paragraph in the cash principle adjustment of the deficit as noted in Exhibit 7 on page 16/17 of the</p>

<p>million and colleges hold £12 million less cash than in 2014-15. Four colleges face particular challenges to their financial sustainability.</p>	<p>report.</p>
<p>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.</p>	<p>Costs as a proportion are up and staff numbers have increased for the second year in a row - headcount is up 600 over 2 years to 10,898. One of the reasons for this could be that functions previously out-sourced had been brought back in or changes to the curriculum impacting on staff numbers.</p>
<p>Scottish Government funding to the sector will increase by five per cent in 2017/18 but colleges still face a number of financial challenges. The most significant challenge is national bargaining which involves harmonising pay and conditions for all college employees in Scotland. A national estates condition survey is under way to inform the preparation of a sector capital plan. The sector has still to develop longer-term financial planning in order to address these issues.</p>	<p>Likely to remain as an increasing cost based on harmonisation and the result of the current negotiations. Staffing requirements might have an impact due to future student headcount numbers changing. For the national estates condition survey it is important that ahead of the conclusion of the survey, SFC provide a mechanism for the priority of spend in terms of critical estate requirements.</p>

Recommendations

<p>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</p> <p>Complete the national estate condition survey and use this as a basis to prioritise future capital investment</p>	<p>The SFC will provide further information about the regional demographic model and how it supports the sector.</p> <p>The National Estate Survey is underway and will be completed in July 2017.</p>
<p>The SFC and colleges should: Assess demand for college courses across Scotland, in accordance with our recommendation last year, in order to plan future education provision</p> <p>Agree the adjustments that should be made to the financial position reported in college accounts, taking account of the approach we have taken in this report, in order to reach an 'underlying financial position' that reflects the immediate financial health of the college</p> <p>Agree common assumptions to be used by colleges when developing longer term financial plans</p>	<p>The SFC will respond to this recommendation in terms of the regional demographic model that is used. The SFC (and the Scottish Government) would welcome further detail from Audit Scotland on the expectations and likely outputs to satisfy this recommendation.</p> <p>It should also be noted that there is work being done through the Learner Journey project on a Common Application Process which may go some way to addressing this recommendation.</p>
<p>The SFC should: Require each college to include, within its accounts, an 'underlying financial position' that reflects the immediate financial health of the college, in line with our approach in this report</p>	<p>The SFC are currently considering their response to this point and will advise.</p>
<p>Colleges should: Prepare longer term financial plans, as we recommended last year, in order to set out how financial challenges will be addressed and ensure that their future budgets are in line with</p>	<p>The SFC are working with Colleges Scotland by end May 2017 to develop an approach to long-term financial plans, building on existing financial forecast return requirements. The college sector</p>

likely funding

Calculate the cost of harmonising staff pay, terms and conditions

Finance Network is working on an approach, with support from the SFC, especially in relation to the use of common planning assumptions.