AUDITOR GENERAL

OVERVIEW REPORT

Overview of further education colleges in Scotland 1999/2000

PREPARED BY AUDIT SCOTLAND

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Contents

AGS/2001/8

Overview of further education colleges in Scotland 1999/2000

A report to the Scottish Parliament by the Auditor General for Scotland

Auditor General for Scotland

The Auditor General for Scotland is the Parliament's watchdog for ensuring propriety and value for money in the spending of public funds.

He is responsible for investigating whether public spending bodies achieve the best possible value for money and adhere to the highest standards of financial management.

He is independent and not subject to the control of any member of the Scottish Executive or the Parliament.

The Auditor General is responsible for securing the audit of the Scottish Executive and most other public sector bodies except local authorities and fire and police boards.

The following bodies fall within the remit of the Auditor General:
- departments of the Scottish Executive eg the Department of Health
- executive agencies eg the Prison Service, Historic Scotland
- NHS boards and trusts
- further education colleges
- water authorities
- NDPBs and others eg Scottish Enterprise.

Audit Scotland

Audit Scotland is a statutory body set up in April 2000, under the Public Finance and Accountability (Scotland) Act 2000. It provides services to both the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Executive and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

Executive summary

Introduction

1. Under the Further and Higher Education (Scotland) Act 1992 (the 1992 Act), most further education colleges in Scotland were transferred from local education authority control on 1 April 1993. Forty-three colleges were incorporated as independent corporate bodies, each governed by a board of management, and assumed ownership and control of all their assets and liabilities at the date of transfer. They have a combined income of around £550 million per annum about three-quarters of which is grant-in-aid payments provided by the Scottish Executive Enterprise and Lifelong Learning Department (the Department) via the Scottish Further Education Funding Council (SFEFC). Roles and responsibilities in the further education sector in Scotland are shown at Exhibit 1.

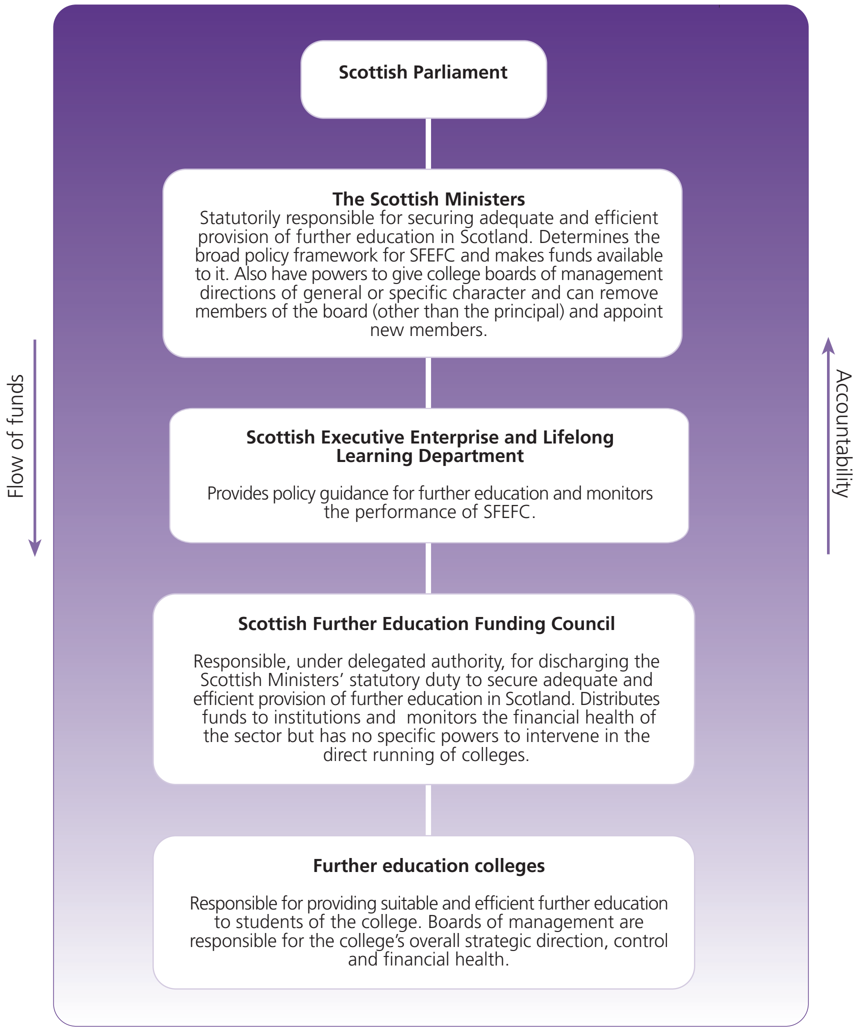
2. Under the terms of the Public Finance and Accountability (Scotland) Act 2000 (the 2000 Act) responsibility for securing the audit of the 43 incorporated further education colleges in Scotland transferred from the college boards to the Auditor General for Scotland with effect from 1 April 2000. Transitional arrangements applied to the audit of 1999/2000 accounts. The audits of further education colleges, which had been commissioned in advance by the colleges themselves, and carried out in accordance with guidance first issued in 1996 by the Scottish Office Education and Industry Department, were reported to the Auditor General after their completion. The colleges appointed commercial accountancy firms to conduct the 1999/2000 audits. Auditors also reported to and agreed findings with individual colleges and provided copies of their management letters to SFEFC.

3. This report, which I present under section 23 of the 2000 Act, is my first overview report on the further education sector. The report has been prepared principally from information contained in reports prepared by the colleges' appointed auditors at the conclusion of their audits. Where appropriate, I have supplemented this with other relevant, contextual information including SFEFC's own work in monitoring the financial health of the sector. My report covers all the significant issues arising out of the 1999/2000 audits of incorporated further education colleges.

4. Overall, auditors' reports provide assurance of sound financial stewardship in the FE sector in Scotland. However, my report on governance and financial management at Moray College shows how a failure to maintain the highest standards can result in serious difficulties.

5. The audit results also highlight the extent to which colleges are experiencing severe financial difficulties. Audited accounts for the period to 31 July 2000 showed that a total of 34 colleges reported an operating deficit for the accounting period and auditors' opinions on the financial statements of five colleges noted that the colleges only remained going concerns on the understanding that financial support from SFEFC or the college's bankers would continue. Furthermore SFEFC have required 12 colleges to prepare financial recovery plans to address deficits accumulated over a number of years. My report therefore comments on continuing risks to financial health and on SFEFC's considerable efforts to improve the financial health of the sector.

Exhibit 1: Roles and responsibilities in the Scottish further education sector



Source: Audit Scotland

Audit results

Completion of accounts and audits

6. Section 22 (5) of the Public Finance and Accountability (Scotland) Act 2000 (the PFA Act) requires Scottish Ministers to lay before Parliament a copy of every account and report sent to them via the Auditor General not later than nine months after the end of the financial period to which the account relates. The completion of the audit of four colleges was delayed beyond the nine-month targets for a variety of reasons. It is disappointing that such relatively generous reporting timetables could not be met. To ensure that compliance with deadlines can be achieved in future years it is essential that:

- a timetable for the conduct and completion of the audit should be agreed in advance and the accounts and supporting working papers should be made to the auditors in accordance with that timetable
- any changes to the guidance and directions on the form and content of the annual accounts should be notified by SFEFC well in advance of the point at which college accounts are being prepared
- in the event that completion of the audit will be delayed, early dialogue is entered into with Audit Scotland so that revised deadlines can be agreed.

7. Auditors provided unqualified opinions on the 1999/2000 accounts of 42 colleges. In the remaining college the auditor provided a technical qualification on the basis of limitation of scope in that the college had not complied fully with the provisions of Financial Reporting Standard 15, Accounting for Tangible Fixed Assets. In a further five colleges, while auditors did not qualify their opinion on the financial statements, attention was drawn to the financial circumstances of the college.

8. In August 2000 the Accounting Standards Board issued a Statement Of Recommended Practice (SORP) Accounting for Further and Higher Education. The SORP is applicable to all further and higher education institutions in the United Kingdom for accounting periods commencing on or after 1 August 1999. Although the SORP is not strictly applicable to the accounts of 1999/2000, SFEFC reviewed individual college's financial statements to gauge the level of compliance with disclosure requirements of the SORP. SFEFC concluded colleges mostly complied with the requirements of the SORP but, equally, every college could improve its compliance.

9. The SORP was issued so that, as far as possible, the financial statements of institutions should be prepared on a comparable and consistent basis. The further education sector in Scotland has made good progress in applying the SORP but it is essential that it builds on this good start to ensure full compliance in future accounts.

Risks to future financial health of colleges

10. Auditors' reports to college boards of management regularly drew attention to two specific factors which could have a significant affect on the future financial health of the colleges.

European funding issues

11. In 1999/2000 40 colleges recorded income from EU grants, nine colleges recorded EU grant income in excess of £1 million and in five colleges European grants contributed over 10% of total college income. New programmes of EU grants became effective from April 2000. Auditors of a number of colleges commented in their reports to college boards of management on the potential impact of the new programmes on future income streams and recommended the need to monitor developments so that colleges can maximise funding and manage effectively the associated costs from this source in the future.

Provisions for pensions and early requirements

12. Since incorporation many colleges have undergone a process of restructuring with consequent job losses and staff early retirements. Where employees retire early, standard accounting practice requires colleges to establish provisions in the balance sheet to meet the cost of enhanced pensions. The annual cost of pension enhancement is funded from the provision the level of which is maintained by an annual charge in the income and expenditure account. At 31 July 2000 all but one college had established a provision for enhanced pension liability and the total of the provision amounted to £36 million.

13. Doubts about the level of continued access to European grants available to further education colleges in future years and the continuing liability arising from enhanced pension payments resulting from college restructuring both pose potential risks to the future financial health of colleges. It is essential that colleges and SFEFC monitor the impact of both these factors and take appropriate action to ensure the provision of further education is not put at risk.

Value for money issues

14. In September 1999 and January 2000 the Scottish Parliament's Audit Committee examined the financial health of the sector and ways of improving colleges' performance. The Committee took evidence from the accountable officers of the Department and of SFEFC. The Audit Committee's report, published in March 2000, found that the further education sector in Scotland was in poor financial health and recommended that SFEFC complete various reviews which had been referred to in evidence to them and to report back to them on progress.

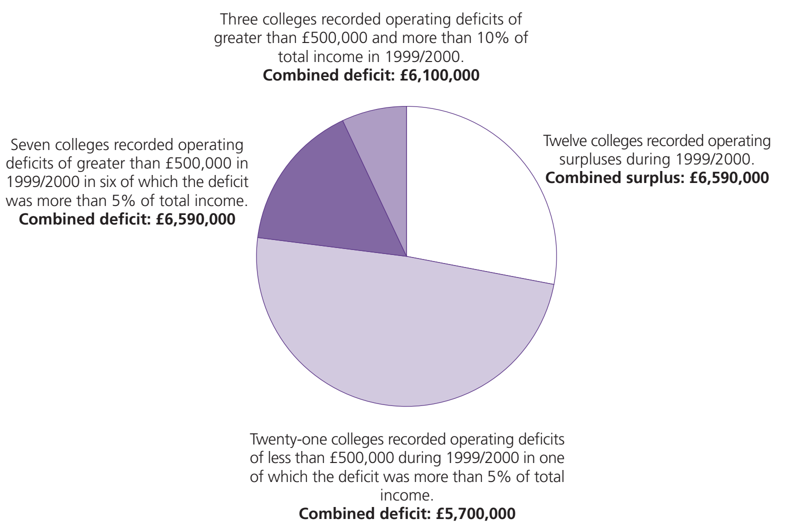
15. In December 2000 SFEFC provided a progress report against each of the reviews noted in the Committee's recommendation. SFEFC noted, however, that in recognition of the scale of its root and branch review of the sector, the timetable for colleges to produce action plans to implement improvements had been extended. SFEFC intend to produce a further progress report to the Committee in October 2001.

Financial health of the further education sector

Financial performance

16. Since incorporation in 1993/94, colleges have improved efficiency and reduced unit costs but the financial results of the sector have been poor. Colleges have recorded an overall operating deficit each year since 1994/95, reaching a peak of £23 million in 1998/99. The total operating deficit for 1999/2000 fell to £16 million but this still resulted in 34 individual colleges returning an operating deficit. For those colleges recording deficits the total operating deficit amounted to £18 million. Altogether, nine colleges returned operating deficits which were in excess of £0.5 million and more than 5% of total income in 1999/2000 (Exhibit 2).

Exhibit 2: Colleges operating surpluses/(deficits) 1999/2000



Source: Audit Scotland

17. Although an operating deficit for the sector as a whole was experienced in 1999/2000, the accumulated deficit fell £2.4 million to £15 million as a consequence of the accounting treatment for the depreciation of fixed assets. By 31 July 2000 some 21 colleges had accumulated deficits with nine colleges having accumulated deficits in excess of £1 million.

18. The full financial position of the colleges for the year ended 31 July 2001 will not be known until the audit process is complete in early 2002. On the basis of colleges' financial forecasts covering the period up to June 2001, 37 colleges are expected to record operating deficits in 2000/01 with the overall operating deficit for the sector likely to be around £14.2 million for the year. SFEFC expects the number of colleges recording operating deficits will fall to 24 by 2003/04.

SFEFC's approach to monitoring financial health

19. Key features of SFEFC's approach to monitoring financial health in the further education sector include:

- issuing guidance to assist colleges in managing their financial health including a new financial memorandum between SFEFC and individual colleges, a new code of audit practice setting out SFEFC's mandatory requirements in relation to colleges' audit arrangements and the requirement for colleges to submit to SFEFC for review their annual development plans and financial forecasts for three years ahead.

- introducing a programme of visits to review the effectiveness of colleges' financial management, audit and governance arrangements. Initially SFEFC visited those colleges whose financial health appeared to be of most concern but the programme has now been rolled out so that visits have been undertaken at 42 colleges with the remaining college to be visited in 2001.

- using a risk-based assessment of colleges to drive the monitoring programme based on a system for categorising the financial health of individual colleges. In 1999/2000 SFEFC categorised the financial health of 19 colleges as exhibiting serious concern. SFEFC is looking to refine its financial categorisation system so as to provide a more detailed indication of colleges most at risk.

20. SFEFC's approach to monitoring the financial health of the sector has been to assist and support to colleges to help them recover their deficits whilst, at the same time, recognising that responsibility for achieving financial stability rests with the boards of management of individual colleges. SFEFC has no specific powers to intervene in the direct management of a college facing financial difficulty and must therefore encourage and persuade rather than direct a college towards corrective action. As my examination of Moray College found, this approach is not always successful as there are limitations to the effectiveness of the accountability framework within the further education sector.

Financial recovery plans

21. SFEFC requires colleges to develop robust financial recovery plans if an accumulated deficit on a college's income and expenditure account is unlikely to be cleared within three years of the deficit first appearing. Financial recovery plans are either in place or are at an advanced stage of preparation at 11 of the 19 colleges whose financial health SFEFC assessed as being of most concern. For each of these colleges SFEFC is monitoring the achievement of recovery plans through regular reports and meetings with colleges' management. In the remaining eight colleges no financial recovery plan has been prepared largely because action is already in hand or the financial position is forecast to improve in future years.

22. The financial health of the further education sector has progressively worsened since 1993. The position improved to some extent in 1999/2000 but the scale of deficits at a significant number of colleges continues to cause concern. SFEFC has in hand action to address matters at individual colleges and on a wider front and it is vital that these efforts should continue. Individual colleges, too, must respond positively to the challenges faced and concentrate on implementing those aspects of their financial recovery action plans most likely to lead to financial stability. This is a matter of serious concern and I intend to monitor closely the financial health of the sector in future years.

Recent developments

23. In addition to its efforts to improve the financial health of individual colleges, SFEFC has also introduced a range of further initiatives designed to improve the management of college finances and the effectiveness of expenditure across the sector. These include:

- a review of the management of Scotland's further education colleges which identified scope for: improved strategic and operational planning; development of financial management; and colleges to develop comprehensive estate strategies. Colleges were required to develop management action plans addressing how they intend to respond to the report's findings and to submit these to SFEFC by March 2001. SFEFC has now provided sector-wide feedback and intends to provide feedback to individual colleges on the adequacy of action plans in October 2001.

- a review of the supply and demand for further education in Scotland concluded that on a national basis, provision of college based learning opportunities was broadly adequate. But the review recommended a further examination of the relative adequacy and efficiency of the provision in each area and for key industrial sectors. SFEFC has begun a comprehensive assessment of each geographical area and of key industrial sectors, due to be complete by 31 March 2002.

- an external review commissioned by SFEFC and the Glasgow Colleges' Group on the strategic options for the provision of further education in Glasgow. The review included consideration of the future curricular requirements of Glasgow-based students and employers, the location of further education provision across the city, geographical features of participation and need and the most effective organisational structures and configuration to support such provision. The Glasgow Colleges' Group has established a committee with representation from SFEFC to oversee and co-ordinate consultation with college boards and with other stakeholders. The consultation is now complete and the Glasgow Colleges' Group expect to make the findings public shortly to inform joint consideration of the outcomes.

- a sector wide survey into the overall condition of colleges' estate concluded that £116 million was required to bring colleges' estates up to an operationally acceptable standard excluding any provision for improvement or reconfiguration. £60 million was subsequently made available to colleges over the five years 2003/04 to tackle the most pressing estates needs. The existence of college estates strategies is now a condition of grant funding. Estates strategies are now in place at 41 colleges and SFEFC have agreed a timetable for implementation with the other two colleges.

- in 1998 Ministers announced that an extra £214 million would be made available for further education over the three year period from 1999/2000 to 2001/02. In the Spending Review 2000, Ministers provided an additional £22 million for the sector in 2001/02 increasing planned public funding to £416 million for the year and announced funding of £424 million and £436 million for 2002/03 and 2003/04 respectively. And in October 2001 Ministers announced a further one-off sum of £7 million for the specific purpose of accelerating the move towards financial health and viability for those colleges in most financial difficulty who have put in place too narrowed strategies.

- in October 2001 the Department provided additional resources to SFEFC to enable it to establish a new FE Development Directorate with responsibility for preparing SFEFC's development strategy for the further education sector and for working more closely with colleges facing financial and management difficulties.

24. The range of initiatives undertaken by SFEFC clearly indicates its determination to maximise the cost-effectiveness of expenditure in the FE sector and deserves full support. Such initiatives are, however, costly in terms of resources and time and SFEFC faces a challenge in managing such a heavy workload within the limited resources available. It may therefore be prudent for SFEFC to further prioritise its efforts to encourage the improvements necessary within the sector in line with a clear view of what is likely to provide the greatest benefit over time. The new FE Development Directorate will have a key role in this process.

Overall conclusions

25. The financial health of the further education sector is important. Deficits may be sustainable in the short term but if allowed to continue could lead to erosion in colleges' infrastructure leading to inefficiency, declining teaching facilities and consequently declining quality. It is therefore essential to reverse the trend of poor financial performance in colleges as soon as possible.

26. Scottish Ministers have announced that an additional £272 million capital and revenue funding is being made available to the sector over the three years 1999/2000 to 2001/02 to help support a number of improvement initiatives. These extra resources will clearly be a major benefit to the sector. However colleges have a responsibility to improve the management of their own resources in order to maximise the benefit available and SFEFC has a continuing responsibility to ensure that the resources available to colleges are managed to best effect in improving the sector's financial performance and quality of provision.

Part 1: Introduction

Further education colleges and their funding

1.1 Under the Further and Higher Education (Scotland) Act 1992 (the 1992 Act), most Scottish further education colleges were transferred from local education authority control on 1 April 1993. Forty-three colleges were incorporated as independent corporate bodies, each governed by a board of management, and assumed ownership and control of all their assets and liabilities at the date of transfer. Two smaller colleges remained within the control of local authorities whilst another two remained as independent bodies although not incorporated in terms of the 1992 Act. On incorporation colleges were no longer subject to local education authority controls and boundaries, and became free to attract students from different and wider catchment areas, in competition with schools, other colleges, and private training providers.

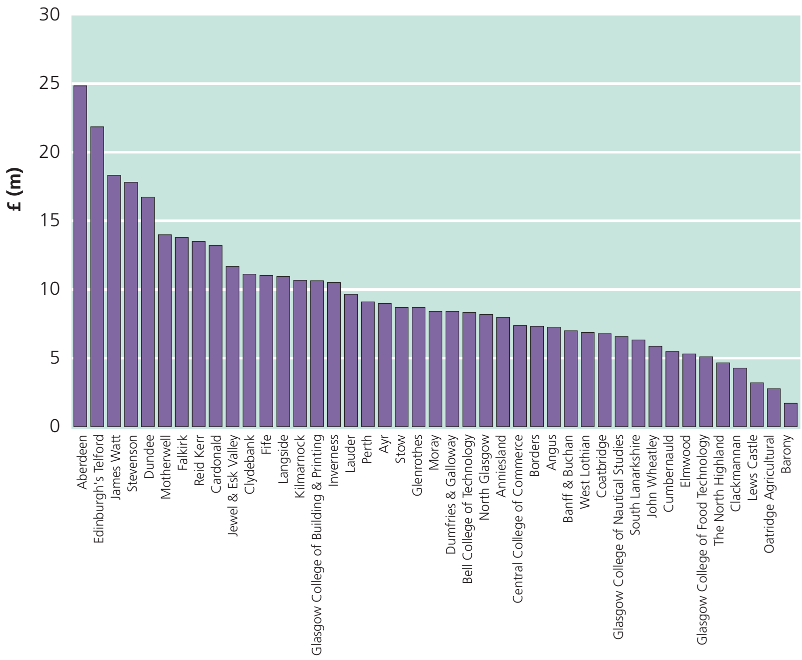
1.2 The main source of funding for the 43[1] colleges to which this report relates is grant in aid payments from the Scottish Executive. In the period from 1 April 1993 until 30 June 1999 grant-in-aid was paid directly to the colleges by the Scottish Office Education and Industry Department (SOEID). On 1 July 1999 a new body, the Scottish Further Education Funding Council (SFEFC), took over responsibility for securing the adequate and efficient provision of further education, primarily through the distribution of grant-in-aid funds to the colleges in accordance with Ministerial policy guidance and by promoting and monitoring the value for money provided by the sector.

1.3 The 43 incorporated further education colleges provide education and training opportunities for a wide range of people from school-leaving age upwards. They have a total income of around £550 million per annum, about three quarters of which is derived from grant-in-aid provided by the Scottish Executive Enterprise and Lifelong Learning Department (the Department) via SFEFC. The remainder of college income is derived from a range of sources including European grants, tuition fees and income from the provision of consultancy and research services.

1.4 From July 1999 the funding of colleges was aligned with their natural planning cycle by changing the funding year from a financial year basis (April to March) to a period based on the colleges' academic year (August to July). The change was implemented during 1999/2000 and, as a result, annual accounts produced by colleges covered the 16-month period from April 1999 to July 2000. During this period the SOEID and SFEFC distributed a total of £347 million grant-in-aid to the 43 incorporated further education colleges in Scotland plus a further £64 million in bursary grants to allow colleges to make bursary payments to low income students (Exhibit 3).

[1] On 1 August 2001 Bell College of Technology became a Higher Education Institute reducing the number of further education colleges to 42.

Exhibit 3: Grant-in-aid and bursary funding of the 43 incorporated colleges, April 1999 to July 2000



Source: Audit Scotland

External audit arrangements

1.5 Under the terms of the Public Finance and Accountability (Scotland) Act 2000 (the 2000 Act) responsibility for securing the audit of the 43 incorporated further education colleges in Scotland transferred from the college boards to the Auditor General for Scotland with effect from 1 April 2000. Transitional arrangements applied to the audit of 1999/2000 accounts. The audits of further education colleges, which had been commissioned in advance by the colleges themselves, and carried out in accordance with guidance first issued in 1996 by SOEID, were reported to the Auditor General after their completion. The colleges appointed commercial accountancy firms to conduct the 1999/2000 audits. Auditors also reported to and agreed findings with individual colleges and provided copies of their management letters to SFEFC. This report, which I present under section 23 of the 2000 Act, is my first overview report on the further education sector. The report has been prepared from information contained in reports prepared by the colleges' appointed auditors at the conclusion of their audits. Where appropriate, I have supplemented this with other relevant, contextual information including SFEFC's own work in monitoring the financial health of the sector. My report covers all the significant issues arising out of the 1999/2000 audits of incorporated further education colleges.

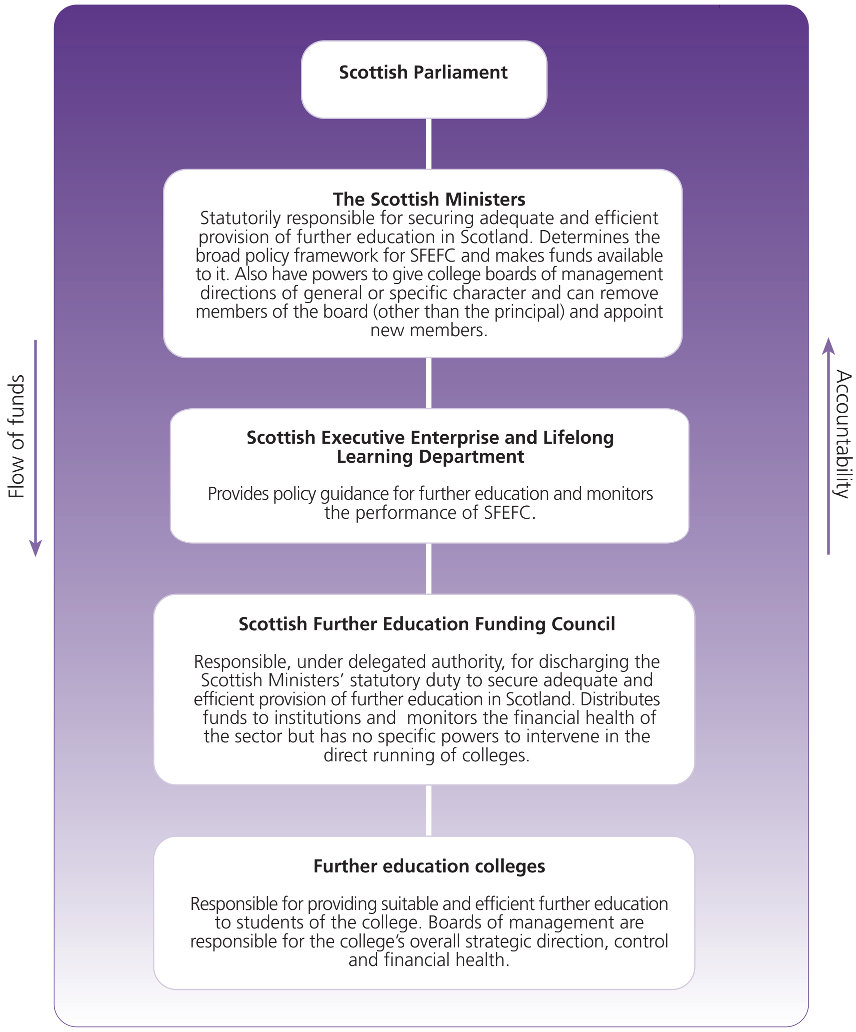
1.6 Overall, colleges are experiencing severe financial pressures. Audited accounts for the period to 31 July 2000 showed that a total of 34 colleges reported an operating deficit for the accounting period and auditors' opinions on the financial statements of five colleges noted that the colleges only remained going concerns on the understanding that financial support from SFEFC or the college's bankers would continue. Furthermore SFEFC have required 15 colleges to prepare financial recovery plans to address deficits accumulated over a number of years.

1.7 My report is in four parts. In Part 2 of the report I provide background to the roles and responsibility involved in accountability for expenditure in further education colleges. Part 3 of the report details the results of the audit of college accounts for 1999/2000 and the main findings of auditors at individual colleges including value for money issues. Part 4 reviews the financial history of the sector and the action SFEFC has taken and proposes to take in managing the financial health of the sector. Part 5 of the report reviews recent developments which are likely to affect the adequacy and efficiency of the provision of further education in Scotland in the future.

Part 2: Roles and responsibilities in the further education sector in Scotland

2.1 The roles and responsibilities in the Scottish further education sector are set out in Exhibit 4.

Exhibit 4: Roles and responsibilities in the Scottish further education sector



Source: Audit Scotland

Duties of the Scottish Ministers

2.2 Under Section 1 of the 1992 Act the Scottish Ministers have a duty to secure adequate and efficient provision of further education in Scotland. In exercise of this duty Ministers have the power to do all that is expedient for the purposes including establishing new colleges, merging two or more colleges or closing colleges of further education.

2.3 Ministers may, under section 21 of the 1992 Act, give boards of management directions of a general or specific character with regard to the discharge of their functions; and it is the duty of a board of management to whom any such directions are given to comply with the directions. Under section 24 of the 1992 Act, if it appears that the affairs of the board of management of any college of further education have been or are being mismanaged, Ministers may by order:

- remove all of the members of the board or any of them (other than the principal of the college)
- subject to certain restrictions, appoint new members to the board in place of those so removed.

Role of the Scottish Executive Enterprise and Lifelong Learning Department

2.4 The Minister for Enterprise and Lifelong Learning and the Department sets the policy guidance according to which SFEFC and colleges are expected to secure adequate and efficient provision of further education in Scotland. The Department also sponsors SFEFC and monitors its performance against the terms of a management statement first issued in July 2000 which sets a broad policy, management and financial framework for SFEFC's operations, in particular:

- the rules and guidelines relevant to the exercise of SFEFC's powers, functions and responsibilities
- the conditions under which public funds are paid to SFEFC
- how SFEFC will account for its performance.

Role of SFEFC

2.5 SFEFC was established by The Scottish Further Education Funding Council (Establishment) (Scotland) Order 1998 (the 1998 Order) as a non-departmental public body of the Department in January 1999, taking up its functions in July 1999. The 1998 Order delegates to SFEFC the duties of Ministers for securing adequate and efficient provision of further education in Scotland. In doing so SFEFC may use the following powers:

- to do all that is necessary or expedient to exercise the duty to secure adequate and efficient provision of further education in Scotland
- those relating to the funding of further education defined in the 1992 Act
- to give consent to the board of management of a further education college to borrow money from any source, give any guarantee or indemnity or create any trust or security over or in respect of any of their property

- under section 18 of the 1992 Act to give consent to the disposal of certain types of property.

2.6 Under the 1992 Act SFEFC consists of not less than 12 and not more than 15 members (known as the Council) who are responsible for the strategic direction and overall management of SFEFC consistent with the overall provisions of the 1992 Act and other ministerial policies, together with a staff of around 100. The chief executive of SFEFC is also its designated accountable officer and a Council member. The accountable officer is responsible to the Scottish Ministers and for ensuring that the funds received by SFEFC are put to uses consistent with the purposes for which they were given and used in compliance with any conditions attached to their use.

2.7 Under the terms of the management statement agreed between the Department and SFEFC, SFEFC is also required to comply with any directions of a general or specific character with regard to the discharge of its functions given by Ministers. The management statement provides that SFEFC should have maximum autonomy to conduct its business in accordance with the various requirements and guidance of Ministers and that it should seek to ensure value for money is obtained in respect of all funds administered by it within a range of strategic and other responsibilities (Exhibit 5).

2.8 SFEFC undertakes an ongoing review of the financial health of the further education sector. A Financial Appraisal and Monitoring Services (FAMS) Directorate has been established with responsibility for: analysing financial forecasts, mid-year financial information, annual financial statements and, where required, financial recovery plans produced by colleges; assessing colleges' financial control and audit, governance and management arrangements; and initiating and undertaking studies and other such projects and disseminating good practice aimed at developing and improving financial management and governance in the sector. FAMS is also responsible within SFEFC for promoting, developing and disseminating good practice on value for money within the further education sector.

2.9 FAMS staff visit institutions on a regular basis to assess audit and financial control arrangements. Although FAMS has no executive role within colleges, nor does it have any responsibility for the development, implementation or operation of colleges' systems, it may from time to time work closely with college financial managers to provide advice and guidance and to help them follow good practice guidelines.

Colleges and the role of the boards of management

2.10 The 43 incorporated colleges in the sector provide education and training towards a wide range of qualifications with some colleges offering specialist provision in agriculture, building and printing, commerce, food technology, and nautical studies. Courses offered include programmes leading to vocational qualifications, general education including those leading to standard and higher grade qualifications, and higher education including those leading to professional qualifications. In addition, many colleges offer courses for students with learning difficulties and/or disabilities and courses designed to improve basic skills in, for example, literacy and numeracy.

Exhibit 5: SFEFC responsibilities

Strategic

- To work with the further education colleges in ensuring the sector plays a full part in taking forward the Scottish Ministers' policy objectives for further education.
- To improve access to further education for a wider range of students, particularly from groups who are presently under-represented among further educations students, encouraging and supporting colleges in addressing this policy priority.
- To facilitate strategic developments that improve the sector's capacity to meet Scotland's education and training needs.
- To promote sound governance and the highest standards of management.

Funding and investment

- To adopt and apply arrangements for the distribution of funds made available by the Scottish Parliament for further education, and keep arrangements under review to ensure they continue to meet SFEFC's statutory responsibilities and policy objectives.
- To identify and assess capital investment needs across the sector.
- To support learning innovations that improve the learning experience for students.

Quality and performance assessment

- To secure a system for assessing quality of learning and teaching within the further education colleges, and to promote a process of continuous quality improvement in learning and teaching in the sector.
- To maintain and publish in an accessible form appropriate statistical, performance and financial information on the further education colleges, covering the range of the sector's activities.

Financial appraisal and monitoring

- To operate internal administrative and monitoring systems in relation to the application of programme and running cost resources, in line with the financial memorandum between the Department and SFEFC.
- To monitor the administration by colleges of funds provided by SFEFC and the colleges' general financial performance and health, in line with the financial memorandum between the Department and SFEFC.

Advice

- To provide Scottish Ministers with such information and advice as they may require as regards the provision of further education, and as SFEFC think fit to provide.

Working relations

- To establish and maintain close working relations with the further education colleges in Scotland, the Scottish Higher Education Funding Council and the Scottish Further Education Unit, the other national funding councils, the Scottish Qualification Authority, Scottish Enterprise and Highlands and Islands Enterprise, government departments and other external bodies with an interest in further education.

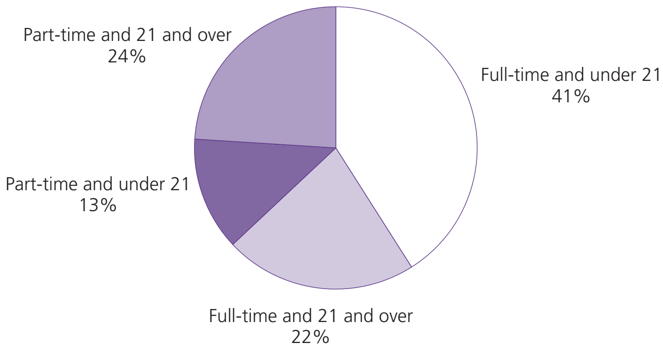
Source: Management Statement between the Scottish Executive Enterprise and Lifelong Learning Department and SFEFC, July 2000

2.11 Some 60% of further education students are adults aged 21 and over attending college on a part-time basis. But analysis of the number of hours students spend in directed learning activity shows that college resources are concentrated on full-time students and on delivering recognised further and higher education (Exhibit 6). Colleges enrol students onto courses throughout the year, some 430,000 students enrolling in academic year 1999/2000. Colleges range in size from around 1,000 to 38,000 students with the median college having around 8,500 students.

Exhibit 6: Students and the types of courses attended (academic year 1999/2000)

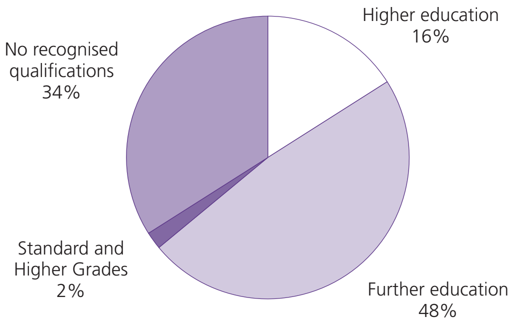
a. The age and mode of attendance of students

Around 63% of student learning activity is directed towards full-time students.



b. The types of courses attended by students

Almost two-thirds of students at further education colleges are pursuing qualification in higher and further education.



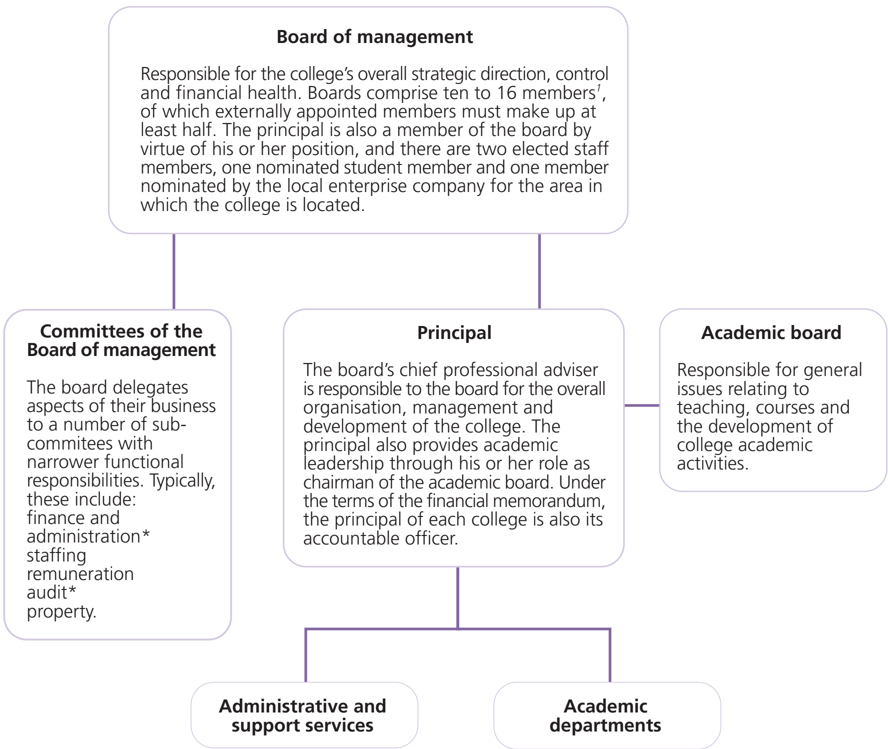
Notes:
1. 'Further education' encompasses non-advanced qualification including Scottish Vacational and Scottish General Vocational Qualifications. Data included students studying for modules or individual units of learning rather than whole qualifications.
2. 'No recognised qualification' includes students on courses where there is no independent warding body, including recreation and leisure courses primarily designed for adult learners.

Source: Audit Scotland analysis 'in.fact' database

2.12 Under the 1992 Act boards of management of colleges consist of between ten and 16 members of which externally appointed members must make up at least half. The principal of the college is a member of the board by virtue of his or her position and the board should also include two elected staff members, one nominated student member and a person nominated by the local enterprise company for the area in which the college is located.

2.13 Boards of management are primarily responsible for setting the policies and overall strategic direction of the college and for its control and financial health so as to ensure the college provides suitable and efficient further education to its students. Each college has a standard financial memorandum agreed with SFEFC governing the use of SFEFC funds and specifying the general conditions under which funding is provided. Subject to this, each college's board of management has discretion over the use of funds received and is ultimately responsible for proper stewardship of those funds, for ensuring that they are used for the purposes intended and for delivering value for money in the use of all the college's resources. The arrangements for governance and management at colleges are summarised at Exhibit 7.

Exhibit 7: Governance and management arrangements at Scottish further educatiion colleges



Notes:

* Formal requirements of SFEFC.

1 Externally appointed members: defined as persons appearing to the board of management to have experience of, and to have shown capacity in, industry, commerical or employment matters or the practice of any profession, and who are not members, staff or students of the institution or an elected member of a local authority.

Source: Audit Scotland

Part 3: Audit results

3.1 This part of the report covers:

- completion of accounts and audits of the 43 incorporated further education colleges
- governance and internal financial control
- other matters arising
- general value for money issues.

Completion of accounts and audits

3.2 Section 22 (5) of the Public Finance and Accountability (Scotland) Act 2000 (the PFA Act) requires Scottish Ministers to lay before Parliament a copy of every account and report sent to them via the Auditor General not later than nine months after the end of the financial period to which the account relates. In order to meet this requirement in the further education sector, the Auditor General set the colleges' appointed auditors audit certification and reporting deadlines of 31 December 2000 for the accounts covering the 16-month period ending 31 July 2000. The deadline is also set out in SFEFC's financial memoranda with individual colleges and SFEFC wrote to all colleges in December 2000 reminding them of this date.

3.3 The auditors of 13 of the 43 incorporated colleges completed their audits, certified the accounts and sent them to the Auditor General by the end of December 2000. The completion of audits and transmission of accounts and auditors' reports to the Auditor General for a number of colleges were delayed over the Christmas period and by the end of January 2001 the Auditor General had received 39 accounts.

3.4 Completion of the audits of four colleges was delayed beyond the nine month target set out in the PFA Act. There are a variety of reasons as to why these delays occurred (Exhibit 8) including, in the case of Moray College, the knock-on effect of delays in completing the audit of 1998/99 accounts.

3.5 The deadlines for the completion of audits to allow accounts to be laid in the Scottish Parliament set out in the PFA Act apply to all sectors of Scottish Executive expenditure. In some areas, such as the NHS in Scotland, departments have set tighter target dates for audit completion and bodies concerned have achieved those revised targets. It is therefore disappointing to note the performance of the four further education colleges whose accounts were not transmitted to the Auditor General for Scotland until at least April 2001. Exhibit 9 sets out action required to ensure that performance can be improved in future years.

Exhibit 8: Reasons for delays in the completion of college's audits

Aberdeen College
Although the auditor signed off the accounts in December 2000, the financial statements and the auditor's report were not transmitted to the Auditor General until April 2001. This was as a result of a dispute between the college and the auditor over the cost of additional work which the auditor claims was necessary to complete the audit. The college has now instigated the auditor's complaints procedures in an effort to resolve the dispute over the level of audit fees.

Inverness College
The auditor signed off the accounts in March 2001 but the financial statements and the auditor's report were not transmitted to the Auditor General until May 2001. The main reason for the delay was the need for the college to make more progress in the completion of its financial recovery plan to address its underlying financial deficit in order that the auditor could certify that the accounts had been prepared on the basis that the college remained a going concern.

Lews Castle College
The auditor signed off the accounts in March 2001 but the financial statements and the auditor's report were not transmitted to the Auditor General until May 2001. The main reason for the delay was the need for the college to make more progress in the completion of its financial recovery plan to address its underlying financial deficit in order that the auditor could certify that the accounts had been prepared on the basis that the college remained a going concern.

Moray College
The certified financial statements and the auditor's report were completed and transmitted to the Auditor General in April 2001. The main reason for the delay in completing the audit of the 1999/2000 accounts was sickness absence in the college's finance department during 1998 and 2000 which delayed completion of the 1998/99 accounts. The college's board approved a temporary appointment to clear the backlog on the 1998/99 accounts but this had the knock-on effect of delaying the 1999/2000 audit.

Source: Audit Scotland

Exhibit 9: Action required to achieve audit deadlines

- A timetable for the conduct and completion of the audit should be agreed in advance and the accounts and supporting working papers should be made available to the auditors in accordance with that timetable.
- Guidance and directions on the form and content of the annual accounts should be notified by SFEFC well in advance of the point at which college accounts are being prepared for the Auditor General.
- In the event that completion of the audit will be delayed, early dialogue should be entered into with Audit Scotland so that revised deadlines can be agreed.

Source: Audit Scotland

Auditors’ opinions on the accounts

3.6 Auditors provided unqualified opinions on the 1999/2000 accounts of 42 colleges. In the remaining college, Glenrothes College, the auditor provided a technical qualification on the basis of limitation of scope in that the college had not complied fully with the provisions of Financial Reporting Standard 15 (FRS 15), Accounting for Tangible Fixed Assets. The college decided to continue with an accounting policy to record fixed assets in the balance sheet at their current value but had not undertaken an interim valuation of its land and buildings and therefore had not fully applied the standard.

3.7 Auditors of five colleges, Bell College of Technology, Inverness College, Lews Castle College, Moray College and North Glasgow College, drew attention to the financial circumstances of the college. While the auditors’ did not qualify their opinions on the financial statements of any of the colleges, each of the auditors drew attention to the fact that the accounts had been prepared on a going concern basis on the assumption that SFEFC’s financial support to the colleges and access to bankers’ overdraft facilities would continue. In view of the comments made by the auditors, I presented a report to the Scottish Parliament under section 22(3) of the 2000 Act on the circumstances of each of these colleges with the colleges’ accounts. I also presented a separate report to the Scottish Parliament on specific governance and financial management issues which had arisen at Moray College.

3.8 Part 4 of my report considers the financial health of the further education sector as a whole in more detail.

Action plans

3.9 Each of the auditors of the 43 colleges has produced reports on their findings. Where the auditors have concluded that action needs to be taken to make the improvements necessary in response to their findings, they have agreed action plans with respective boards of management. As part of my responsibilities for the audit of further education colleges I shall require that implementation of the action plans is monitored and followed-up by the appointed auditors.

Governance and internal financial control

Governance

3.10 The board of management of each college is required to include in its financial statements a description of how the college has applied the principles of corporate governance set out in Section 1 of the Combined Code on Corporate Governance issued by the London Stock Exchange in June 1998.

3.11 All 43 colleges complied with the requirement to provide a statement on corporate governance in their 1999/2000 report and accounts and 42 of the colleges were able to confirm that they had complied with the principles of the Combined Code on Corporate Governance. The board of management of Borders College stated that the ongoing process for identifying, evaluating and managing significant risks had not been in place for the entire period.

Internal financial control

3.12 The reports of the boards of management of all colleges contained statements confirming that they had taken reasonable steps to ensure appropriate financial and management controls were in place to safeguard public funds and the assets of the college and to prevent and detect fraud.

Audit Committees

3.13 An effective audit committee with sufficient authority, expertise and independence can provide the executive management of an organisation with partial and authoritative advice on matters relating to audit and internal control. To be successful, an audit committee must be objective and independent of the executive management and any finance committee which exists. SFEFC's financial memorandum requires each college to establish an audit committee to monitor the operation of the overall system of financial control. The role of the audit committee is described in more detail in SFEFC's code of audit practice for colleges.

3.14 SFEFC regard 1999/2000 as a transitional year for the further education sector inasmuch that it was the first year in which it assumed responsibility for the monitoring of colleges. Whilst all colleges had audit committees in 1999/2000, the requirement to have such committees and the precise nature of their role was only formalised when SFEFC issued its financial memorandum and code of audit practice in August 2000.

3.15 The boards of management of each college reported that audit committees had met regularly during 1999/2000. As part of their monitoring of the sector, SFEFC reviewed audit committees' reports for 1999/2000. SFEFC found the standard and content of reports varied widely and not all provided the audit committee's own opinion to the college's board of management of the operation of internal financial controls. SFEFC, while recognising that 1999/2000 was a transitional year, has written to all colleges reminding them of the need for audit committees to provide an opinion to the board of management and providing guidance on the format of audit committee reports.

Internal audit

3.16 SFEFC's financial memorandum requires each college to establish an internal audit function whose primary responsibility is to provide assurance on the adequacy and effectiveness of colleges' internal control systems and to produce an annual report on their work for consideration by the audit committee. SFEFC undertook a review of internal auditors' reports covering internal controls operated by the colleges during 1999/2000. The review found that, by December 2000, reports were not available for 11 of the 43 colleges and that the reports that were available did not always provide assurance on the complete system of internal control.

3.17 SFEFC's review highlighted that where internal auditors had identified weaknesses in financial control college management had unequivocally accepted internal auditors' recommendations to address these weaknesses. SFEFC intends to follow up with colleges to ensure the necessary corrective action is being taken.

Reports of the boards of management

3.18 College auditors do not formally express an opinion on the statements produced by the boards of management but they are expected to report if the board of management's report is not consistent with the financial statements. No auditor made any such report.

Moray College

3.19 In February 2001 the accountable officer for SFEFC reported to the Council on a number of issues of serious concern relating to governance and financial management at Moray College. In the light of these concerns I produced a separate report on the issues arising at the college to record the weaknesses involved and the action taken to overcome them and to raise issues for the college, for SFEFC and the Department and for governance and accountability in the further education sector as a whole.

Other matters arising from audits

Compliance with the Statement of Recommended Practice

3.20 In August 2000 the Committee of Vice Chancellors and Principals established a steering committee drawn from representatives of the further and higher education sector and, working under the auspices of the Accounting Standards Board, issued a Statement Of Recommended Practice (SORP) Accounting for Further and Higher Education. The SORP was produced after collaborative work between key stakeholders in further and higher education including college and university representative bodies, funding councils in Scotland, England and Wales and accounting practitioners and is applicable to all further and higher education institutions in the United Kingdom for accounting periods commencing on or after 1 August 1999. The SORP was issued so that, as far as possible, the financial statements of institutions should be prepared on a comparable and consistent basis. Key requirements set out in the SORP are listed in Appendix 1.

3.21 Although the SORP was published later than expected and is not strictly applicable to the accounts of 1999/2000, SFEFC reviewed individual college's financial statements to gauge the level of compliance with disclosure requirements of the SORP. SFEFC found that the non-compliance rate against its checklist varied from 6% to 32% between colleges with the average for the sector as a whole of 14%. SFEFC concluded that colleges mostly complied with the requirements of the SORP but, equally, every college could improve its compliance.

European funding issues

3.22 The European Social Fund (ESF) supports measures aimed at equipping unemployed people with the skills to secure a job, re-skilling the existing workforce and improving the skills base of particular geographic areas in order to promote a high level of employment, as well as addressing equality, sustainable development and economic and social cohesion. The European Regional Development Fund (ERDF) provides support for the promotion of economic and social cohesion, particularly relating to creation and safeguarding of sustainable jobs, investment in infrastructure and support to local development and employment initiatives.

3.23 Further education colleges receive support from the ESF for the provision of a wide range of training courses from basic training in literacy and numeracy to more complex courses aimed at encouraging people to increase their use and understanding of information technology. Support to colleges from the ERDF is less common but some colleges have obtained support for the development of infrastructure projects such as the construction and fitting-out of business centres and IT suites.

3.24 In 1999/2000 40 colleges recorded income from EU grants, amounting, in total, to £31 million (representing 5.6% of total income recorded by colleges). Nine colleges recorded EU grant income in excess of £1 million and in five colleges European grants contributed over 10% of total college income.

3.25 In April 2000 the European Commission approved new programmes covering the period 2000 to 2006 based on revised eligibility criteria for ESF and ERDF grants. Under the new programmes colleges may still be eligible for ESF grants although some development priorities have changed and, as a result of changes in the designation of the economic development status of some areas, the total funding available to Scotland is lower. These changes to European funding led the auditors of a number of colleges to comment in their reports on the potential impact on future income streams. The auditors recommended to colleges the need to monitor developments in ESF so that colleges can maximise funding from this source in the future without putting the colleges' financial health at risk by building up fixed cost structures on the basis of an income stream that may be uncertain.

3.26 The Scottish Executive has issued revised guidance to colleges and higher education institutions likely to be applying for EU funds under the new programmes. The guidance covers: the need for applicants to identify clearly the added value that would result from training courses in receipt of ESF monies; and the need to clearly demonstrate that when a course contains both ESF supported students and other students, the ESF beneficiary receives additional support to mainstream trainees. The Scottish Executive's guidance also sets additional information requirements which the European Commission will apply from July 2003. To comply with the additional requirements many colleges will need to develop their existing costing systems.

Provisions for pensions and early retirements

3.27 Since incorporation many colleges have undergone a process of restructuring with consequent job losses and staff early retirements. Boards of management have often used, or intend to use, restructuring of college management structures, departments and facilities as integral parts of financial recovery plans. Such restructuring is designed to align future costs more closely with college income projections but the initial costs incurred arising from early retirements often place a heavy burden on college budgets.

3.28 Where employees retire early, SSAP 24: Accounting for Pensions requires colleges to establish provisions in the balance sheet to meet the cost of enhanced pensions. The annual cost of the enhancement is funded from the provision and the provision level is maintained by an annual charge in the income and expenditure account. At 31 July 2000 all but one college had established a provision for enhanced pension liability and the total of the provision amounted to £36 million. Charges to the provision in 1999/2000 amounted to £3.7 million whilst payments from the provision totalled £2.8 million.

3.29 In 1999/2000 accumulated deficits were incurred in seven colleges as a result of pensions provisions being made to meet the requirements of SSAP 24. SFEFC regards this as more of an ongoing technical accounting treatment than being indicative of any underlying financial problem. Accordingly, SFEFC has not required these colleges to prepare financial recovery plans but colleges have been made aware of the need to understand the profile of the pension liability and the need to plan to match this over time as the liability emerges.

Value for money issues

3.30 Prior to 1 April 2000, value for money studies of the further education sector in Scotland were undertaken by the National Audit Office on behalf of the Comptroller and Auditor General. Under transitional arrangements reports arising from such work was reported to the Scottish Parliament. Since 1 April 2000 the Auditor General for Scotland may also undertake and where appropriate, report on value for money examinations of the further education sector in Scotland.

3.31 In June 1999 the Comptroller and Auditor General published his report on Scottish Further Education Colleges, '*Managing Costs*'. The report examined colleges' costs in general and the approaches used to manage costs at a sample of 12 colleges and drew on best practice in the sector and elsewhere to suggest a framework for improving colleges' management of costs.

3.32 On the basis of the Comptroller and Auditor General's report, the Scottish Parliament's Audit Committee examined the financial health of the sector and ways of improving colleges' performance, building on best practice in September 1999 and January 2000. The Committee took evidence from the accountable officers of the Department and of SFEFC.

3.33 The Audit Committee published its findings, and conclusions in March 2000 and recommended that SFEFC should complete various reviews which were referred to in evidence and report back to the Committee by 31 December 2000 on:

- a root and branch review of the sector and on the action planned to tackle college deficits, improve college management, and to rationalise further education provision in Scotland
- a review of the recovery plans at ten colleges in poor financial health, and on the progress made in implementing action plans and improving financial health of the colleges concerned
- a review of the estates strategy and the scale of any backlog maintenance and plans to invest further in this key aspect of infrastructure
- the development of benchmarking, of performance indicators including a 'balanced scorecard', and plans to improve college costing systems
- a target for efficiencies that can be achieved without harming the quality of education.

3.34 In December 2000 SFEFC provided a progress report against each of the areas covered by the Committee's recommendations. SFEFC noted, however, that in recognition of the scale of its root and branch review of the sector, the timetable for colleges to produce action plans to implement improvements had been extended and that SFEFC would provide a further report to the Committee. SFEFC intends to produce a further report on progress in October 2001.

Part 4: Financial health of the further education sector

4.1 This part of the report follows up conclusions on the financial health of the sector in the Audit Committee's report, examines financial performance in 1999/2000 and comments on the action being taken by SFEFC to support improvements in management of the future financial performance of colleges.

The Audit Committee's conclusions on financial health

4.2 The Audit Committee's report included four conclusions on the financial health of the further education sector (Exhibit 10) covering: the level of forecast deficit to 1998-99; initiatives being taken to encourage growth and improve college infrastructure; recovery plans for colleges with serious financial health problems; and restructuring costs.

Exhibit 10: Audit Committee conclusions on financial health

- The further education sector in Scotland is in poor financial health, with a forecast deficit of over £22 million for 1998-99. Partly this arose from a legacy of problems on incorporation. Partly it was caused by the twin pressures of increasing student numbers and a squeeze on funding since 1993. But it also reflects variations in management practice and capability across the sector.
- Extra funds are being provided over the three years starting in 1999-2000 to encourage growth and improve college infrastructure. The Department, and the new Funding Council for Further Education have acted swiftly to set in train a root and branch review of the strategy for the sector, of the funding formula, of management in colleges, of the financial monitoring framework, of standards and quality improvement and of key assets such as estates and information and communications technology.
- Thirteen colleges have serious financial health problems, and six to eight of these are particularly bad. Work is underway to implement or develop recovery plans. Where plans are needed, these will be in place or in preparation by 31 December 1999.
- A key factor in college financial problems has been the cost of restructuring. Although this should yield savings downstream, the up front costs are a heavy burden on college budgets despite some additional funding from the Department. In the 13 colleges most at risk, restructuring has cost £22.9 million.

Source: Audit Committee 1st Report 2000

4.3 Paragraphs 3.27 to 3.29 of my report comment on the impact of restructuring costs evident in the 1999/2000 accounts and paragraphs 3.32 to 3.33 set out SFEFC's plans for updating the Committee on the various initiatives it had planned to improve financial management of the colleges. The following paragraphs provide details of how the level of deficit has changed since the Committee's report and of SFEFC's approach to identifying colleges with serious financial problems and the action to address those problems.

Financial performance

Trends since 1993

4.4 As autonomous institutions, colleges are expected to match their costs with the income they receive. Deficits therefore represent a shortfall between the level of expenditure and the availability of income, and current year deficits have to be repaid from subsequent years' income. By continuing to record annual deficits colleges are deferring the reductions or changes in services that are required to repay earlier years' overspends and restore financial balance. Whilst a deficit of income over expenditure may be endured in the short term, and indeed even be planned in one or more years, it cannot be sustained in the long term as eventually the college will become insolvent.

4.5 SFEFC's financial memorandum requires each further education college, inter alia:

- to ensure that it has a sound system of internal financial management and control so that a college's income is sufficient to meet its total expenditure and the financial viability of the college is maintained

- to inform SFEFC of the likelihood of an unplanned (or greater than planned) annual deficit as soon as is practicable

- to clear any accumulated deficit on the income and expenditure account within a reasonable and defined period of time, normally the end of the third accounting period after the period in which the deficit began to accumulate.

4.6 Although colleges as a whole have improved efficiency and reduced unit costs since incorporation in 1993/94, the historic financial results of the sector have been poor. Despite achieving efficiency savings, the sector moved into overall deficit in 1994/95. The overall operating deficit increased sharply in 1995/96 and a further sharp increase in the deficit to £23 million was experienced in 1998/99 (Exhibit 11). The number of colleges with operating deficits also increased sharply in 1994/95 and has been increasing since.

Financial performance in 1999/2000

4.7 In July 1998 Ministers announced that a total of £214 million of extra resources would be made available for further education over the three year period from 1999/2000 to 2001/2002. The additional resources were to be targeted as follows:

- £102 million to support the objective of increasing student numbers by 40,000 by 2001/02
- £56 million to support the financial position of the sector
- £29 million for information and communications technology
- £27 million towards investment in infrastructure.

During 1999/2000 SFEFC paid £2.6 million for the specific purpose of providing assistance to colleges in financial difficulty.

Exhibit 11: Consolidated college income and expenditure statements

	1993/94 £ m	1994/95 £ m	1995/96 £ m	1996/97 £ m	1997/98 £ m	1998/99 £ m	1999/2000[1] £ m
Total income	326	346	358	416	424	381	553
Total expenditure	322	354	372	430	435	404	570
Operating surplus/(deficit)[2]	4	(8)	(14)	(14)	(11)	(23)	(16)
Number of colleges with operating deficit	12	27	27	35	35	36	31
Operating surplus/(deficit) as % of income	1.3%	(2.3%)	(3.8%)	(3.4%)	(2.6%)	(3.3%)	(3.0%)

Notes:

1 Following changes to the funding of colleges from a financial year basis to an academic year basis, college accounts for 1999/2000 were prepared for the 16 month period April 1999 to July 2001.

2 The operating surplus/(deficit) represents the financial result for the year after taking into account all costs including depreciation on the current value of assets. This indicates the ability of colleges to recover their direct operating costs and generate a surplus.

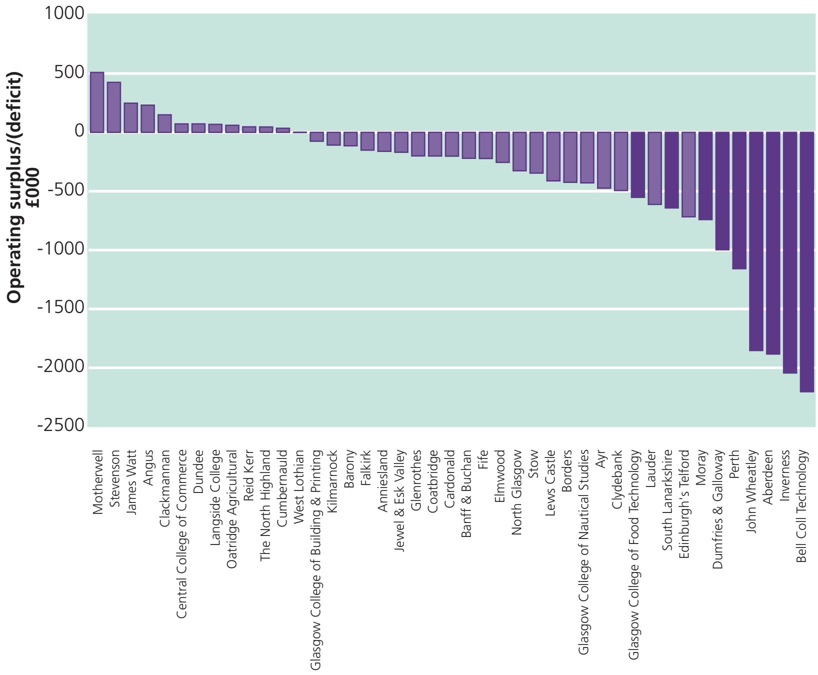
Source: Audit Scotland

4.8 The financial results of the sector improved slightly in 1999/2000 following record levels of deficit experienced in 1998/99. The total operating deficit was reduced to £15.8 million some £7.9 million lower than in 1998/99. And the ratio of surplus/(deficit) as a percentage of income also improved although the use of a 16-month accounting period in 1999/2000 may have partly contributed to this (Exhibit 9).

4.9 The improved financial results of the sector as a whole does, however, mask the large number of colleges experiencing a deficit in 1999/2000. Whilst there was some improvement compared to 1998/99, a total of 31 colleges returned an operating deficit in 1999/2000 (36 in 1998/99) (Exhibit 12). For those colleges recording deficits the total operating deficit amounted to £18.0 million. Altogether, nine colleges returned operating deficits which were both in excess of £0.5 million and which were more than 5% of total income in 1999/2000.

Exhibit 12: College operating surpluses/(deficits) 1999/2000

The darker columns indicate those nine colleges where the operating deficit for 1999/2000 was both greater than £500,000 and greater than 5% of income.



Source: Audit Scotland

4.10 Although an operating deficit for the sector as a whole was experienced in 1999/2000, the accumulated deficit fell £2.4 million to £15 million as a consequence of the accounting treatment for the depreciation of fixed assets. By 31 July 2000 some 21 colleges had accumulated deficits with nine colleges having accumulated deficits in excess of £1 million (Exhibit 13).

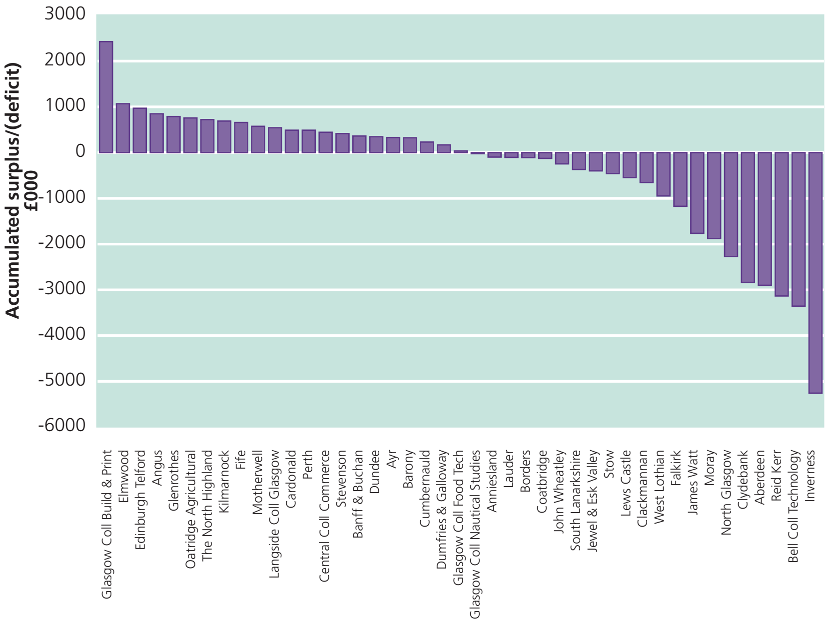
Availability of working capital and level of external borrowings

4.11 The calculation of a college's operating surplus or deficit gives an indication of financial performance over the course of an accounting period. Of equal importance is the need for colleges to have sufficient working capital to meet running expenses and to service fixed assets on a daily basis, and to contain external borrowings to a level which permits capital and interest repayments. In theory, cash flow problems can require organisations to enter into short term borrowing arrangements at high interest rates which may place an additional strain on scarce financial resources.

4.12 SFEFC's financial memorandum requires colleges to obtain written consent from the Council before entering into capital financing agreements where the level of capital and interest repayments each year exceeds either 5% of total annual income or half of the average surplus achieved in the last three years (or half of the surplus forecast for the current year if that is lower). In such cases, written consent will only be given if:

[2] Colleges' Income and Expenditure Accounts report an operating surplus/(deficit) for the year. Both the operating surplus/(deficit) and the difference between historic cost depreciation and the actual charge for the period calculated on the revalued amount are transferred to the Income and Expenditure Account Reserve to indicate historic accumulated surplus/(deficits).

Exhibit 13: College accumulated historic cost surpluses/(deficits)



Source: Audit Scotland

- the college can demonstrate its ability to repay the capital and interest charges whilst maintaining financial and academic viability without recourse to requesting additional grant from SFEFC

- the college can demonstrate the value to be generated by the transaction whether it involves refinancing, or purchase of any new investment or assets

- the college can demonstrate that any such new investment or asset acquisition is in accordance with the college's strategic plan and, where appropriate, its estate strategy.

4.13 SFEFC monitors college's performance in this area through the use of two key performance indicators:

- the ratio of cash and other current investments to total expenditure (this provides an indicator of the number of days where average daily expenditure can be met from existing cash balances at a particular point in time)

- borrowing as a percentage of income.

4.14 The consolidated cash balances of all colleges amounted to £30.3 million as at 31 July 2000 compared to £23.3 million as at 31 March 1999. However, increased expenditure in 1999/2000 meant that the number of days in which cash balances could meet average daily expenditure fell from 26 days as at 31 March 1999 to 20 days as at 31 July 2000. Total outstanding borrowings by colleges increased from £37.1 million as at 31 March 1999 (10% of total income) to £46.2 million as at 31 July 2000 (8% of total income) partly as a consequence of investment in new and replacement estate and equipment.

4.15 The average performance for the sector as whole again hides wide variation between individual colleges. A total of ten colleges had borrowings as at 31 July 2000 which were in excess of 10% of income during 1999/2000 and 13 colleges had sufficient cash balances to finance fewer than ten days average daily operating expenditure (Exhibit 14).

Exhibit 14: College borrowings and cash balances

This Exhibit shows that whilst some colleges have relatively healthy cash balances with low levels of borrowing, there are several (to the bottom of the Exhibit) where borrowings are high and cash balances are low. For some of these colleges, the need to make interest and capital repayments together with cash shortages results in a constraint on new investment and maintenance of capital assets.

The dark columns show the availability of cash balances to meet average daily expenditure. The light coloured columns show borrowings and ovedrafts as a percentage of income.

Source: Audit Scotland

Indicative results for 2000/01

4.16 The audit of college accounts for the year ended 31 July 2001 are expected to be completed and passed to the Auditor General for Scotland by 31 December 2001. The full financial position of the colleges will not be available until the audit process is complete but SFEFC require colleges to provide regular financial forecasts which provide an interim assessment of changes in each college's financial position. The financial forecasts provided by the colleges to June 2001 indicated that the overall operating deficit for the sector was likely to be around £14.2 million for 2000/01 and that 37 colleges were likely to incur an operating deficit during the year (6 more than in 1999/2000). Consequently, 22 colleges are likely to have an accumulated deficit at 31 July 2001 (1 more than in 1999/2000). The overall accumulated deficit across the sector is expected to have increased from £15 million in 1999/2000 to £15.6 million in 2000/01. SFEFC expects that the number of colleges recording operating deficits will fall to 24 in 2003/04.

SFEFC's approach to monitoring financial health

4.17 SFEFC assumed responsibility for monitoring the financial health of further education colleges in July 1999. Since then, SFEFC has worked hard to develop an approach to monitoring the financial health of the sector which provides assistance and support to colleges to help them recover their deficits but, at the same time, recognises that responsibility for achieving financial stability rests in the first instance with the boards of management of individual colleges. Key features of SFEFC's approach include: new guidance on managing financial affairs, including additional financial reporting requirements; the introduction of new arrangements for monitoring financial management at colleges; and new procedures for reviewing the financial position of each college.

Guidance on financial management

4.18 SFEFC has introduced a series of guidance to assist colleges in managing their financial health including:

- **a new Financial Memorandum between SFEFC and individual colleges.** This describes the accountability arrangements for colleges and the conditions under which SFEFC offers grant-in-aid to colleges.

- **a new Code of Audit Practice.** This sets out SFEFC's mandatory requirements in relation to colleges' audit arrangements including the requirement to establish an Audit Committee and to appoint an internal audit service, and provides guidance on good practice on the activities of both together with the role and responsibilities of the board of management.

- **the submission of annual development plans and budgets.** Colleges are required to submit to SFEFC forecasts for three years ahead of their income and expenditure, balance sheet position and expected cash flows together with associated sensitivity analysis and contingency plans. These forecasts are expected to be the financial expression of colleges' strategic and operational plans.

Monitoring financial arrangements

4.19 SFEFC has introduced a programme of visits to review the effectiveness of colleges' financial management, audit and governance arrangements by:

- assessing the financial health of colleges

- assessing the effectiveness of the financial and management framework in place at colleges

- confirming that colleges are complying with the financial memorandum and SFEFC's Code of Audit Practice

- assessing the effectiveness of colleges' processes for implementing or taking account of good practice, guidance on financial management and value for money and governance arrangements, including that published by the Department, SFEFC, Audit Scotland and the National Audit Office

- assessing the adequacy and effectiveness of colleges' audit arrangements.

4.20 Initially SFEFC visited those colleges whose financial health appeared to be of most concern and the programme has been gradually rolled out so that visits have now been undertaken to 42 of the 43 colleges. A visit to the final college will be made during 2001. A report is produced after each visit in which the recommendations are graded and set out in an action plan with a management response, a responsible officer and a date for implementation. The action plan forms the basis for follow-up work by FAMS.

4.21 The programme of visits is driven by SFEFC's assessment of the financial health of each college. SFEFC categorises the financial health of individual colleges using a system which assesses financial performance against standard criteria and SFEFC's knowledge of the college's financial background. The standard criteria include the level of financial surpluses or deficits in-year and over time, short-term solvency and borrowing levels. Colleges are categorised into four financial health categories ranging from those exhibiting serious financial health concerns to those considered to be low risk. In 1999/2000 19 colleges were judged to exhibit serious concerns (a reduction from 24 in 1998/99). No colleges were categorised as low risk. SFEFC is proposing to refine its financial categorisation system so as to provide a better indication of those colleges most at risk which will be the key determinant of monitoring.

Reviewing financial health

4.22 SFEFC monitors the financial health of colleges' through financial analysis of: three-year financial forecast projections, financial forecast updates recording the mid-year position and colleges' annual financial statements. The most important of these three elements is the financial forecasts, which provide a forward look and identify the 'direction of travel' of a college in financial terms. That enables potential problems to be identified at an early stage and action initiated as appropriate.

4.23 The mid-year financial forecast update and annual accounts are used to compare actual performance against that forecast. A wider exercise in which annual reports by college audit committees, college internal auditors, as well as management letters prepared by colleges' external auditors is also undertaken.

4.24 While the financial analysis is largely a desk-based exercise, there is also a strong interactive element in which matters arising are followed up with college management and, where necessary, with boards of management.

Financial recovery plans

4.25 SFEFC's financial memorandum permits colleges to incur an annual financial deficit where the deficit can be recognised as an approved board of management policy. SFEFC's financial memorandum states that it expects that any accumulated deficit on an income and expenditure account should be cleared by the end of the third accounting period after the year in which the deficit began to accumulate, unless an alternative timescale has been agreed with SFEFC. In practice, SFEFC looks to see that colleges have robust plans to recover a deficit within a reasonable and specified timescale.

4.26 Financial recovery plans are either in place or are at as advanced stage of preparation at 11 of the 19 colleges whose financial health SFEFC assessed as being of most concern. For each of these colleges SFEFC is monitoring the achievement of recovery plans through regular reports and meetings with colleges' boards and management.

4.27 In the remaining eight colleges no financial recovery plan has been prepared largely because action is already in hand or the financial position is forecast to improve in future years. In each of these colleges, SFEFC has informed the board of management of its concerns and is monitoring closely the position. Appendix 2 details action being taken in those colleges where financial recovery plans have been required and Appendix 3 provides information on the causes and nature of SFEFC's concerns in those colleges where action plans have not been prepared.

Part 5: Recent developments

5.1 In addition to the measures outlined in Part 4 to improve monitoring of the financial management of colleges, SFEFC has also commenced a number of initiatives to address the adequacy and efficiency of the provision of further education in Scotland. This part of the report sets out progress to date of some of these important initiatives.

Management review of further education colleges

5.2 In March 1999 Ministers asked SFEFC to undertake a major review of the management of Scotland's further education colleges and to report to them. SFEFC appointed consultants to undertake fieldwork for the study and to report their findings and conclusions arising from reviews of sample of 12 colleges. Ministers subsequently endorsed SFEFC's report which was published in September 2000.

5.3 The report concluded that there was much good governance and management practice already in place in further education colleges although scope also existed for most colleges to learn from good practice and experiences in other colleges. Key messages included the need for greater involvement of board members in the formulation of the college vision, improved strategic and operational planning including the recognition of marketing as a strategic function, the need to develop significantly the financial management function particularly in relation to strategic financial planning and the need for colleges to develop comprehensive estate strategies.

5.4 As a result of the review SFEFC has asked colleges to prepare management action plans addressing how they intend to respond to the report's findings. Colleges were required to submit their action plans to SFEFC by the end of March 2001 and SFEFC engaged consultants to review the adequacy of action plans. SFEFC has provided sector-wide feedback and intends to provide feedback to individual colleges on the adequacy of action plans in October 2001.

Review of supply and demand

5.5 In summer 2000 SFEFC completed a review of links between the supply and demand for further education in Scotland. The review provided information on national trends in the provision of further education over the three year period 1996 to 1999 , together with the relative contributions made by each college. The review also included maps of student participation, profile of each college, breakdown of participation by age, gender, mode of study, and subject of study.

5.6 The review was structured around the identification of each college's provision and set against responses made by major stakeholders to structured questionnaires and interviews. The report concluded that on a national basis, provision of college based learning opportunities was broadly adequate. But the review recommended a further examination of the relative adequacy and efficiency of the provision in each area and for key industrial sectors. SFEFC has begun a comprehensive assessment of each geographical area and of key industrial sectors, due to complete by March 2002. SFEFC intends to follow up each review with dialogue with the relevant colleges and stakeholders, in order to agree action plans to deliver the necessary changes identified.

The provision of further education in Glasgow

5.7 In September 2000 SFEFC and the Glasgow Colleges' Group agreed to commission an external review to:

- generate and evaluate strategic options for consideration by the Glasgow Colleges Group and the Council for the provision of further education in Glasgow in order to be efficient and effective in meeting the needs of learners and cost effective in the use of estates.

5.8 It was expected that options generated from the review would address: the future curricular requirements of Glasgow; the location of further education provision across the city; geographical features of participation and need; and the most effective organisational structures and configuration to support such provision. Options generated were also expected to provide the basis for decisions on the development of provision in Glasgow and, in particular, investment in estate and infrastructure. In addition each option was to be appraised against their impact on:

- current and future needs of students
- current and future needs of employers and other sponsors
- the needs of the city and its communities
- quality of provision
- value for money.

5.9 The report was received by the Council in March 2001 and considered to offer an acceptable basis against which to judge proposals for the development of FE provision (including appropriate estates provision) within the city. The Glasgow Colleges' Group has established a committee with representation from SFEFC to oversee and co-ordinate consultation with college boards and with other stakeholders. This phase was completed in September 2001 and the Glasgow Colleges' Group expect to make the hidings public shortly in order that there can be joint consideration of the outcomes.

5.10 SFEFC is unaware of any proposals for merger being developed by other colleges outside Glasgow but a report outlining the Council's approach to collaboration and rationalisation between colleges has been circulated within the sector. This report was also sent to the Minister in January 2001 who welcomed the Council's approach. SFEFC has been made aware of the intention of Stow and North Glasgow Colleges, and, separately of the three Glasgow colleges in Cathedral Street (College of Building and Printing, Central College of Commerce and College of Food Technology) to explore the possibility of merger although no specific proposals have been received.

Condition survey of college estates

5.11 In May 2000 SFEFC considered the results of a sector wide survey into the overall condition of colleges' estate. The condition survey concluded that £116 million was required to bring colleges' estates up to an operationally acceptable standard excluding any provision for improvement or reconfiguration. £60 million was subsequently made available to colleges over the next years to 2003/04 to tackle the most pressing estates needs. The existence of college estates strategies is now a condition of grant funding. Estates strategies are now in place at 41 colleges and SFEFC have agreed a timetable for implementation with the other two colleges.

Future funding for the sector

5.12 In the Spending Review 2000, Ministers rolled forward their existing financial commitments to the further education sector for the three year period to 2003/04. Ministers provided an additional £22 million for 2001/02 thus increasing planned public funding for the sector from £394 million to £416 million in the year and announced funding of £424 million and £436 million for 2002/03 and 2003/04 respectively. And in October 2001 Ministers announced a further one-off sum of £7 million for the specific purpose of accelerating the pace of turnaround for those colleges in most financial difficulty.

SFEFC organisational changes

5.13 In October 2001 the Department provided additional resources to SFEFC to enable it to establish a new FE development directorate. The new director for further education development will be responsible for:

- leading the preparation of the Councils' strategy for the development of the further education sector
- ensuring, where appropriate, coherence and integration of the further education strategy with the Scottish Higher Education Funding Council's strategy for the higher education sector
- working with colleges and other stakeholders to ensure that the needs of geographical areas and different industries are met
- working with colleges to stimulate collaboration, rationalisation and merger where these will improve efficiency and/or the quality of service
- working with college boards of management and senior managers to develop management capability in the sector
- leading the Councils' work in supporting colleges that are facing financial and management difficulties.

Appendix 1: Statement of recommended practice

The Statement of Recommended Practice (SORP) Accounting for Further and Higher Education is founded on the principle that the financial statements of institutions should, as far as possible, be prepared on a comparable and consistent basis. The SORP takes account of best accounting practice, the requirements of Funding Councils, the accounting provisions of the Companies Act and any other relevant legislation, and Statements of Standard Accounting Practice and Financial Reporting Standards issued by The Accounting Standards Board.

A steering group consisting of representatives of the further and higher education sectors working under the direction of the Accounting Standards Board produced the SORP. The steering group included membership drawn from senior staff of colleges and universities in Scotland and England, representatives of the Association of Colleges and the Committee of Vice-Chancellors and Principals together with staff from SFEFC and its equivalent higher and further education funding councils in England.

The SORP requires higher and further education institutes to:

- prepare accounts on the basis of historic cost as modified for the revaluation of certain assets
- include fixed assets in the balance sheet at cost or valuation with revaluation being carried out in accordance with FRS 15 Accounting for Fixed Assets
- provide a report of its financial performance in the year and future developments
- provide a statement of its corporate governance arrangements
- provide a statement of the responsibilities of its governing body including confirmation that it had taken reasonable steps to ensure appropriate financial and management controls were in place to safeguard public funds and the assets of the college and to prevent and detect fraud
- prepare accounts together with supporting commentary and notes in accordance with the model format included in the SORP.

Appendix 2: Action set out in college financial recovery plans

Bell College of Technology

The college has been in financial difficulties for some time leading to the agreement of a financial recovery plan between the college and SFEFC in July 1999. In 1999/2000 the college recorded a deficit of £1.8 million (deficit of £1.7 million in 1998/99) and an accumulated deficit of £3.4 million. Much of the reason for this deficit can be attributed to exceptional restructuring costs (£800,000) arising from the implementation of the financial recovery plan plus a provision for the repayment of European Social Funding (£640,000). The latest financial forecasts indicate the college is making good progress towards its target of eliminating its accumulated deficit by 2004/05.

Bell College of Technology became a Higher Education Institute with effect from 1 August 2001.

Clackmannan College

The college was required to prepare a recovery plan following a reported operating deficit of £0.8 million on a turnover of £4 million during 1998/99. The board of management agreed its recovery plan in July 1999 which consisted of measures to cut costs and access new income streams while aiming for sustainable growth in student numbers at the same time. Phase 1 of the plan aims to reduce the deficit by £0.5 million by 2002/03 however the most recent forecasts show this target has slipped. The college is working closely with SFEFC to produce a revised recovery plan. In 1999/2000 the college reported a surplus of £150,000 on a turnover of £5.6 million and an accumulated deficit on the Income and Expenditure Reserve of £650,000.

Clydebank College

The college reported a deficit of £490,000 in 1999/2000 on a turnover of £13.8 million. The deficit is entirely due to the creation of a provision in the Income and Expenditure Account to repay an advance of £522,000 to SFEFC. The college also had a bank overdraft of £280,000 as at 31 July 2000. The colleges' financial position is further worsened by accumulated deficits of £2.8 million and having written down the value of its land and buildings to nil in 1999/2000 as the buildings are considered to be unsustainable in their present form. The college prepared a draft financial recovery plan in February 2001 but SFEFC expressed serious doubts over the robustness and deliverability of the plan. Working with SFEFC, the college is currently in the process of finalising revised financial viability proposals and has also taken steps to strengthen its board of management.

Inverness College

The college reported a deficit of £1.3 million in 1999/2000 the sixth consecutive annual deficit. The accumulated deficit at 31 July 2000 was £5.4 million which is equivalent to more than half the organisation's business turnover. At 31 July 2000 loans and bank overdrafts stood at £2.4 million, however this reduced by £400,000 in 2000/01 and is forecast to reduce significantly by 2004. SFEFC has monitored the implementation of the plan in its first year and is pleased with the progress made. In 2000/01 a small historic cost surplus is forecast, which is in line with the plan. SFEFC will continue to monitor progress of the plan over time. SFEFC consider the results to be encouraging and indicate that the college should recover its accumulated deficit in a period not exceeding nine years from the end of 2000/01. Key elements of the financial recovery plan included a programme of internal staff restructuring, a harmonisation of the curriculum to better match the needs of the region and improvements to the college's quality procedures including internal governance, management and administration processes.

Langside College

The 2000/01 funding announcement resulted in the college receiving £1.4 million of transitional funding due to the reducing profile of college activity in previous years. This necessitated the preparation of a recovery plan, designed to remove the college's dependence on transitional relief in the short-term. The college submitted its draft recovery plan to SFEFC in May 2001. A number of major issues required further analysis and explanation before SFEFC could be satisfied that the plan will effect recovery. More detailed proposals are at an advanced stage. In 1999/2000 the college recorded a surplus of £290,000 on a turnover of £12.8 million and an accumulated surplus of £540,000.

Lews Castle College

The college recorded a deficit of £410,000 during 1999/2000 bringing its accumulated deficit to £520,000. £440,000 of this deficit, however, is attributable to pensions provision. The 2000/01 funding announcement resulted in the college receiving £500,000 (£250,000 2001/02) of transitional funding due to the reducing profile of college activity in previous years. This necessitated the preparation of a recovery plan, designed to remove the college's dependence on transitional relief in the short-term. The college produced a draft financial recovery plan in January 2000. However this plan failed to address the requirements of SFEFCs Financial Memorandum, which requires colleges to produce a robust recovery plan. Consequently, SFEFC provided funding to the college to employ consultants to undertake a benchmarking exercise of the college and to help produce and deliver a robust recovery plan which addressed the question of long term financial viability. SFEFC received the revised plan in August 2001which is currently being reviewed in detail.

Moray College

In February 2000 the chief executive of SFEFC reported to the SFEFC Council the results of his investigation into alleged misconduct at Moray College (Auditor General for Scotland report '*Governance and financial management at Moray College*' AGS/2001/4, June 2001 refers).

In February 2000, SFEFC carried out a regular FAMS monitoring visit at the college. This review indicated that there were significant underlying financial weaknesses at the college as a result of weak financial controls. The college were required to develop an action plan to address these weaknesses and to prepare a recovery plan to arrest the weak financial position. The college's board of management and the acting principal prepared a draft recovery plan but this failed to meet the requirements of the SFEFC Financial Memorandum. Subsequently SFEFC provided funding for the college to employ a consultant to help produce a robust plan. The latest iteration of this plan was submitted to SFEFC in August 2001. The plan is undergoing detailed review, though SFEFCs initial findings indicate support "in principle" suggesting the college can achieve sustainable recovery.

At 31 July 2000 the college reported a deficit of £460,000 on income of £9.6 million and an accumulated deficit of £1.9 million. It also had loans and bank overdrafts of £2.4 million.

North Glasgow College

The college had an accumulated of deficit of £2.3 million and overdrafts and loans of £1.1 million at 31 July 2000. In view of the size of accumulated deficit the college prepared a financial recovery plan which has now been agreed with SFEFC. The recovery plan aims to eliminate the accumulated deficit by 2006/07 and the college has embarked on a programme of early retirals to address its cost base. The college has also announced its proposals to merge with Stow College.

Perth College

The college first experienced financial problems in 1998/99. These continued in 1999/2000 where a historic cost deficit of £675,000 was recorded on income of £13.8 million. At 31 July 2000 although there is an overall accumulated surplus, historic cost deficits are forecasts until 2001/02 which will erode this position. Historic cost surpluses are forecast from 2002/03 onwards. The college has adopted its 2001 financial forecast as its updated recovery plan. This takes account of UHI Millennium Institute funding. The board of management has given a commitment to SFEFC to ensure its recovery plan targets are met and that the college can comply with SFEFC's Financial Memorandum.

Reid Kerr College

Following a recorded deficit of £2.7 million in 1998/99, the college's financial recovery plan was agreed between the college and the then SOEID in April 1999. The college has now implemented a number of measures aimed at the elimination of the deficit including re-organisation of the college's departmental structure and a programme of voluntary redundancies. These measures contributed to a recorded surplus of £470,000 in 1999/2000 although the accumulated deficit remains high at £3.1 million and the college has overdrafts and loans totalling £1.9 million. The latest financial forecasts indicate that the college remains on target to eliminate the accumulated deficit during 2005/06.

South Lanarkshire College

The college recorded a deficit of £370,000 during 1999/2000 and an accumulated deficit of £270,000. The college's financial situation resulted in the board having to prepare a financial recovery plan at the end of 1999 and to agree this with SFEFC that was duly undertaken. As part of the recovery process, the college implemented a restructuring exercise in early 2000 resulting in the merger of 13 academic schools into 8 academic departments. The latest forecasts indicate that the college is capable of eliminating its accumulated deficit during 2005/06.

Stevenson College

The 2000/01 funding announcement resulted in the college receiving £2.3 million (£1.1 million 2001/02) of transitional funding due to the reducing profile of college activity in previous years. The college were required to produce a recovery plan as a result of this change. The college presented its draft financial recovery plan to SFEFC in August 2001. The plan is being reviewed in detail by SFEFC, though the initial review has determined that "in principle" the plan meets the terms of the Financial Memorandum and that sustainable recovery should be achieved.

Appendix 3

Colleges where financial health is of concern but SFEFC have not required action plans to be prepared

Dumfries & Galloway College

The college experienced a deficit of £580,000 in 1999/2000. Cash balances also fell over £400,000 during the year to £190,000 and the college has experienced some cash flow difficulties. The deterioration in performance is attributable to exceptional restructuring costs, high levels of spending on temporary teaching staff and a reduction in overall funding. The college's board of management is actively considering implementing a staff restructuring exercise. Deficit are forecast for 2000/01 and 2001/02 before recovery to a small surplus the following year. SFEFC is to liase closely with the college on the preparation of a strategy for recovery.

Glasgow College of Food Technology

Historic cost deficits of approximately £250,000 were recorded in both 1998/99 and 1999/2000 although the college still had a small accumulated surplus at 31 July 2000. Cash balances fell during 1999/2000 from £1.2 million but remain fairly healthy at £760,000. The college had no borrowings. College management is at an advanced stage of preparing a strategy for recovery. All activities are being reviewed as a means of achieving further efficiencies and generating additional commercial income.

Glenrothes College

The college returned small historic cost deficits in both 1998/99 and 1999/2000 but still has an accumulated surplus of £790,000. The main cause of concern in the college's financial health is the level of borrowing used to finance estates and information and communications technology developments. Borrowings amounted to £1.2 million at 31 July 2000 (down from £2.3 million at 31 March 1999) but cash balances increased to £230,000.

James Watt College

The college returned a surplus of £630,000 in 1999/2000 but still has an accumulated deficit of £1.8 million at 31 July 2000. In financial terms the college is amongst the most efficient in Scotland and has expanded rapidly in recent years. To do this it has taken on significant borrowing (£8.3 million at 31 July 2000 on annual income of £23 million). SFEFC has not required the college to prepare a recovery plan because future surpluses are forecast to finance borrowing charges and virtually eliminate the accumulated deficit by 2002/03.

John Wheatley College

The college recorded an operating deficit of £1.9 million and a historic cost deficit of £160,000 in 1999/2000 resulting in an accumulated deficit of £250,000. The significant operating deficit is largely due to accelerated depreciation charges on its main campus building at Easterhouse which is to be demolished once a new building is occupied at the start of the academic year 2001/02. The college had a bank overdraft of £700,000 at 31 July 2000. The latest financial forecasts indicate that the college will eliminate its accumulated deficit during 2002/03.

Lauder College

The college recorded a deficit of £300,000 in 1999/2000. At 31 July 2000 the accumulated deficit stood at £100,000 and the college had no cash balances and borrowings of £2.3 million. A major cause of the operating deficit was losses by the college's two subsidiary companies due to lower income being generated than forecast. SFEFC recently gave the college borrowing consent to increase its overdraft and take on additional capital finance to help the college trade its way out of financial difficulties.

Stow College

The college recorded a deficit of £100,000 in 1999/2000. At 31 July 2000 the accumulated deficit stood at £458,000, borrowings stood at £1.4million but cash balances were healthy. Much of the deficit and borrowings are associated with the refurbishment of the Stow West campus. The college expects to move in to a surplus position from 2000/01 and to eliminate the accumulated deficit by 2002/03.

West Lothian College

The college broke even in 1999/2000 but at 31 July 2000 had an accumulated deficit of £840,000 and borrowings of £300,000. Cash balances were healthy at £455,000. The accumulated deficit is largely the result of provisions for future pension liabilities. Operating and historic cost deficits are forecast for each of the next two years due to the transition caused by a recent move to a new PFI funded site. The college is forecasting operating and historic cost surpluses from 2002/03 onwards.

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