

Agenda – Public Accounts Committee

Meeting Venue:	For further information contact:
External Location	Fay Bowen
Meeting date: Monday, 3 July 2017	Committee Clerk
Meeting time: 12.30	0300 200 6565
	SeneddPAC@assembly.wales

Cardiff and Vale College

(Private pre-meeting 14.00 – 14.15)

- 1 Introductions, apologies, substitutions and declarations of interest**
(14.15)
- 2 Paper(s) to note**
(14.15 – 14.20) (Pages 1 – 4)
- 3 Welsh Government oversight of further education colleges 'finances and delivery': Evidence Session 1**
(14.20 – 15.20) (Pages 5 – 98)

Research Briefing

PAC(5)–19–17 P1 – Auditor General for Wales Report: Welsh Government oversight of further education colleges 'finances and delivery'

Iestyn Davies – Chief Executive Officer, ColegauCymru

Mark Jones – Principal, Gower College

Sharron Lusher – Chair, ColegauCymru

(Break 15.20 – 15.30)



Cynulliad
Cenedlaethol
Cymru

National
Assembly for
Wales

4 Welsh Government oversight of further education colleges 'finances and delivery': Evidence Session 2

(15.30 – 16.30)

(Pages 99 – 104)

PAC(5)–19–17 P2 – Welsh Government's response to the Auditor General for Wales' Report (20 March 2017)

PAC(5)–19–17 P3 – Welsh Government's response to the Auditor General for Wales' Report (8 June 2017)

Huw Morris – Director for Skills, Higher Education and Lifelong Learning, Welsh Government

Geoff Hicks – Head of Post 16 Funding, Welsh Government

5 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

(16.30)

Item 6

6 Welsh Government oversight of further education colleges 'finances and delivery': Consideration of evidence received

(16.30 – 17.00)

Concise Minutes – Public Accounts Committee

Meeting Venue:

Committee Room 3 – Senedd

Meeting date: Monday, 26 June 2017

Meeting time: 14.00 – 16.49

This meeting can be viewed

on [Senedd TV](#) at:

<http://senedd.tv/en/4113>

Attendance

Category	Names
Assembly Members:	Nick Ramsay AM (Chair) Neil Hamilton AM Neil McEvoy AM Rhianon Passmore AM Lee Waters AM Mike Hedges AM (In place of Vikki Howells AM)
Witnesses:	James Price, Welsh Government Tracey Mayes, Welsh Government
Wales Audit Office:	Alistair McQuaid Mike Usher
Committee Staff:	Meriel Singleton (Second Clerk) Claire Griffiths (Deputy Clerk) Katie Wyatt (Legal Adviser)

Transcript



1 Introductions, apologies, substitutions and declarations of interest

1.1 The Chair welcomed the Members to the Committee.

1.2 Following a change in Committee membership on 21 June, the Chair welcome Vikki Howells to the Committee and thanked Mike Hedges for his work. However, Mike Hedges substituted for Vikki Howells today.

2 Paper(s) to note

2.1 The papers were noted.

2.2 The Committee agreed that the Chair should write to the Children, Young People and Education Committee advising them of the work the Committee has undertaken as they may wish to seek updates from the Welsh Government during their scheduled ministerial scrutiny sessions.

2.3 Mike Hedges AM asked that the Chair write to the Welsh Government seeking further clarification on Advanced Manufacturing in relation to Kancoat.

2.1 Regional Education Consortia: Additional information from the Welsh Government (16 June 2017)

2.2 The Welsh Government's Funding of Kancoat Ltd: Letter from the Welsh Government (21 June 2017)

3 The Welsh Government's initial funding of the Circuit of Wales Project: Evidence Session

3.1 The Chair made an opening statement regarding the recent correspondence between the Welsh Government and himself.

3.2 The Committee scrutinised James Price, Deputy Permanent Secretary, Economy, Skills and Natural Resources Group, and Tracey Mayes, Head of Governance and

Compliance, Economy, Skills and Natural Resources Group, Welsh Government on the Welsh Government's initial funding of the Circuit of Wales Project.

3.3 James Price agreed to:

- Write to the Committee with clarification on the total expenditure incurred and the funding the Welsh Government has put in to date;
- Send the internal guidance officials adhere to when assessing grant applications;
- Provide further details, following the Cabinets' decision on funding the Circuit of Wales project, on the due diligence process carried out; and
- Investigate who from the Welsh Government made the comment on a press statement about 'grandstanding' and advise the Chair.

4 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

4.1 The motion was agreed.

5 The Welsh Government's initial funding of the Circuit of Wales project: Consideration of evidence received

5.1 Members considered the evidence received and agreed that a report be prepared for their consideration.

6 Natural Resources Wales

6.1 Members noted the additional information from Natural Resources Wales and agreed the draft letter to the Climate Change, Environment and Rural Affairs Committee.

7 Inquiry into Regulatory oversight of Housing Associations: Consideration of draft report

7.1 Due to time constraints, this item was not reached but Members were asked to send any comments on their initial consideration of the Committee's report to the Clerks who will reschedule the item for a future meeting.

Document is Restricted

Archwilydd Cyffredinol Cymru
Auditor General for Wales

Welsh Government oversight of further-education colleges' finances and delivery



WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU



I have prepared and published this report in accordance
with the Government of Wales Act 2006.

The Wales Audit Office study team comprised Steve Ashcroft,
Sophie Knott, Stephen Martin, and Ben Robertson under the
direction of Matthew Mortlock. The study team were supported
by staff from Grant Thornton.

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Mae'r ddogfen hon hefyd ar gael yn Gymraeg.

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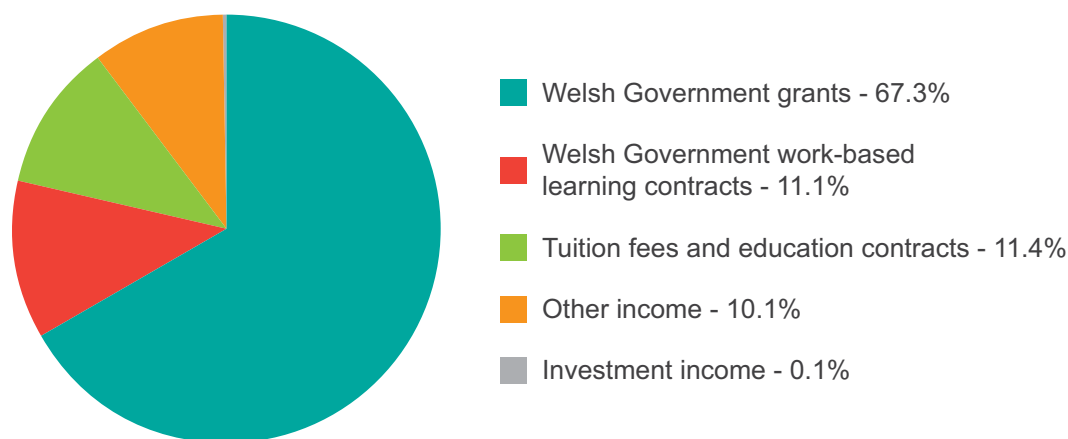
Summary report

Summary

- 1 Further education is formal education and training provision mainly for people aged 16 and over but excluding delivery in universities. The further-education sector has a significant role to play in enabling young people and adults to fulfil their potential and in delivering a skilled workforce. In some areas in Wales, further-education colleges provide all education provision for 16 to 18 year olds. However, in most areas, sixth forms in schools also provide A-level education, as well as some vocational qualifications.
- 2 Most vocational qualifications offered by colleges are at levels 1 to 3 of the National Qualifications Framework, but many colleges do offer higher-level qualifications up to degree level. The Framework classifies qualifications from entry level (basic skills) to level 8 (a doctoral or equivalent post-graduate degree). For example, a GCSE grade A* to C is at level 2, an A level or AS level is at level 3, a Higher National Certificate is at level 4, a Higher National Diploma is at level 5, and an undergraduate honours degree is at level 6.
- 3 Further-education colleges are autonomous bodies that are outside the public sector. They are not-for-profit organisations regulated under the Further and Higher Education (Governance and Information) (Wales) Act 2014, which established their current status and increased their autonomy from the Welsh Government¹. [Appendix 2](#) details the status and governance of colleges. ColegauCymru, a member-led body, represents all colleges in Wales.
- 4 The Welsh Government sets the overall policy framework for further education, and provides the majority of the funding to colleges ([Figure 1](#)). The Welsh Government has reduced funding levels to the sector over the last five years. The total income of the sector in 2015/16 was around £449 million.

¹ There are currently 14 further-education institutions in Wales: ten further-education corporations, which are tax-exempt charities established under the Further and Higher Education Act 1992; three companies limited by guarantee, which are part of higher-education institutions; and one institution designated under the Further and Higher Education Act 1992 (WEA YMCA Community College Cymru, recently renamed Adult Learning Wales, which operates across Wales). In practice, these institutions have the same functions and level of autonomy and we refer to them as colleges throughout this report.

Figure 1 – Further-education sector income sources 2015/16



Note: 'Welsh Government grants' includes some capital funding paid in previous years that has been treated as income, to match depreciation of the assets that it funded.

Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

Use of data in this report

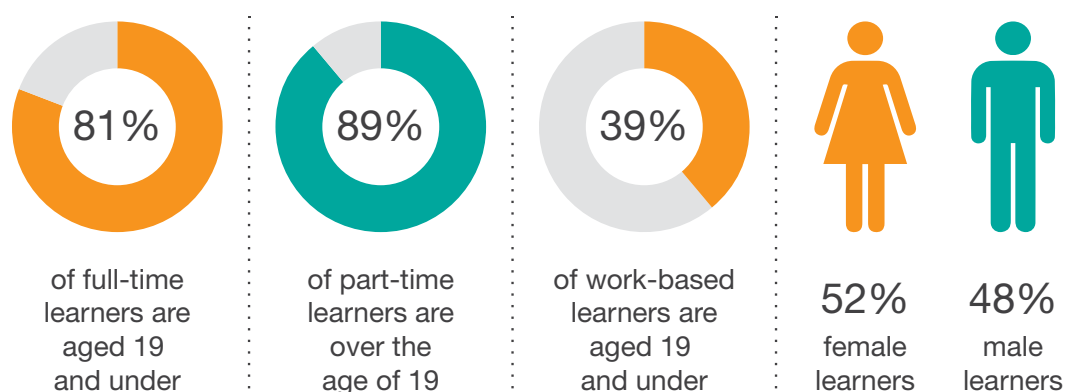
Academic and financial years explained

Throughout this report we refer to financial and other information based on colleges' academic years, which end on 31 July and are also their accounting periods (shown in the format '2016/17'). The Welsh Government sets priorities and funding for colleges on the academic year, but budgets for its own expenditure on an annual basis to 31 March (shown in the format '2016-17').

Timescales explained

Throughout this report we have used the most up-to-date information available. For Welsh Government funding allocations the most up-to-date information is for 2016/17. Our financial analysis of the sector's income is based on audited figures for 2015/16. Learner numbers are based on provisional figures for 2015/16 (published November 2016) and outcome measures are actual figures for 2015/16 (published February 2017).

- 5 The Welsh Government monitors the financial health and performance of colleges. Around half of colleges also fall within the oversight responsibilities of the Higher Education Funding Council for Wales (HEFCW)², either because they are part of higher-education institutions, or because they deliver higher-education provision which is regulated directly by HEFCW under the Higher Education (Wales) Act. We reported on higher-education finances in late 2013³.
- 6 Based on provisional data, there were approximately 131,000 learners at colleges during 2015/16. Of these around 48,000 (37%) were in full-time study, 67,000 (51%) were undertaking part-time study and 16,000 (12%) were engaged through work-based learning. Based on 2015/16 data:



- 7 Mergers have been a key feature of the further-education sector in Wales and between September 2008 and August 2015 the number of colleges in Wales reduced from 25 to 14 (Appendix 3). Figure 2 shows the location of the main campus at each college, although colleges may have several campuses. Colleges serve catchment areas that generally follow local-authority boundaries except for WEA YMCA Community College Cymru (Adult Learning Wales), which operates across the whole of Wales. Learners living in Wales are free to apply for courses at any college and significant numbers of learners do study at colleges other than the one that usually provides for their local catchment area. Colleges vary in size and structure. The number of 2015/16 learners⁴ at individual colleges ranged from 21,500 at Grŵp Llandrillo Menai to just over 1,000 at Coleg Ceredigion.

² The Higher Education Funding Council for Wales regulates fee levels at universities, ensures a framework is in place for assessing the quality of higher education and scrutinises the performance of universities and other designated providers.

³ Auditor General for Wales, **Higher education finances**, November 2013.

⁴ Excludes higher-education and adult community-learning courses.

Figure 2 – Further-education colleges in Wales (main campus locations)



Note: WEA YMCA Community College was renamed Adult Learning Wales on 5 November 2016.

Source: ColegauCymru

- 8 On behalf of the Auditor General, Wales Audit Office staff have examined whether the Welsh Government is fulfilling effectively its oversight role to ensure that, despite financial constraints, further-education colleges are financially well placed to deliver the Welsh Government's expectations. Specifically, we examined:
- Whether the Welsh Government has a clear and effective approach to setting the direction and funding of the sector, and to overseeing its financial position and performance; and
 - How colleges have responded to financial challenges, the financial resilience of the sector, and the impact of funding reductions on colleges and on learner outcomes.
- 9 Our review covered the 14 colleges in Wales that exist specifically to provide further education. We did not cover schools that provide sixth-form teaching, work-based learning providers other than colleges, or private education providers. We did not undertake a detailed review of the financial-management arrangements of individual colleges. We engaged the audit firm Grant Thornton to assist us with the review. [Appendix 1](#) provides further detail about the scope of our work and the methods we used to gather evidence.
- 10 We concluded that, **while generally sound, the Welsh Government's funding and oversight arrangements would benefit from a longer-term and more integrated approach. In response to reduced funding, colleges have cut part-time provision and costs substantially and are aiming to develop their commercial operations to increase revenue. The sector as a whole reported small operating deficits in each of the three years to July 2016 after several years of surpluses. Financial health varies across the sector but significant cost pressures remain for all colleges. The impact of reduced funding on quality and outcomes is not yet clear, but the available evidence indicates that the sector has maintained its performance to date.**

The Welsh Government has cut grant funding for the sector, and while funding allocation and oversight arrangements are generally sound, they would benefit from a more integrated and long-term approach

- 11 The Welsh Government has cut revenue grant funding for the sector by £22 million between 2011/12 and 2016/17, a reduction of 7% in cash terms and 13% in real terms. However, funding for full-time provision has risen by 3% in real terms while funding for part-time courses has dropped by 71%, reflecting the Welsh Government's decision to prioritise its statutory duty to make reasonably sufficient provision for 16-19 year olds⁵. Funding for work-based learning (apprenticeships and traineeships) has also been maintained. The UK and Scottish Governments have taken similar approaches to further-education funding in recent years.

⁵ The decision to reduce funding for further-education colleges between 2013/14 and 2015/16 was driven by a reduction in the block grant from the UK Government and increases in the funds made available to the NHS in Wales.

- 12 In response to the pressure on public finances, the Welsh Government intends that employers will have greater influence over skills provision and take a greater share of costs. However, the UK Government's new Apprenticeship Levy has important implications for this 'co-investment' policy.
- 13 The Welsh Government does not operate a specific capital budget for the sector, but colleges are able to bid for funding through the 21st Century Schools and Education Programme. The programme has been targeted on schools, but five colleges have secured £38 million of funding for infrastructure projects. The Welsh Government also provided £22 million for small-scale capital projects earlier in 2016-17 after funds became available at short notice. Colleges welcomed this extra funding, but the short notice and March 2017 spending deadline have constrained the type of projects that could be delivered.
- 14 The Welsh Government made substantial reforms to the funding framework for post-16 education in 2014/15. Core funding is no longer allocated on the basis of small units of activity, which allowed colleges to enrol students on supplementary courses to generate additional income. The new framework awards a particular value to a complete learning programme for each learner, which is intended to provide a comprehensive package of support. Colleges receive a fixed annual allocation which they draw down according to the value of the learning programmes that they deliver⁶. The general consensus was that these reforms had simplified and improved funding, created a stronger focus on learner needs and avoided unnecessary provision while providing a degree of certainty for colleges. However, the current approach does not enable local changes in need – for example, as a result of demographic change – to be reflected in funding allocations, and the sector would prefer longer-term funding horizons.
- 15 There is no single, unified strategy for further education or for post-16 education generally, with policy direction coming from three main strategies⁷. The 'Hazelkorn' review of oversight arrangements for post-16 education and training in Wales concluded that the Welsh Government lacked an overall vision for the system, and there was a lack of strategic thinking and joint working between public bodies⁸. The report recommended that a single, autonomous public body be established to oversee the whole system, supported by an overarching vision set by government that emphasised closer links between policy, providers and social and economic goals. The Welsh Government announced in January 2017 that it would consult on establishing a new, arm's length strategic authority to oversee post-compulsory education and training.

⁶ There are uplifts for deprived areas and rural areas where the cost of provision is higher (although two rural colleges told us this was insufficient to cover the extra cost).

⁷ Welsh Government, **Youth Engagement and Progression Framework** (2013), **Policy Statement on Skills** (2014) and **Qualified for Life** (2014)

⁸ Professor Ellen Hazelkorn (for the Welsh Government), **Towards 2030: a framework for building a world-class post-compulsory education system for Wales**, March 2016

- 16 Colleges have a good relationship with officials in the Welsh Government responsible for overseeing the sector, aided by the small size of the sector in Wales and staff continuity in the Welsh Government. Most colleges also provide some higher education, and relations with universities are also generally favourable although there were some concerns about competition for higher-level vocational courses.
- 17 Relationships with schools were more variable. There are examples of good joint working at local level, but colleges reported difficult relationships with some schools. The sector believes that larger sixth forms or provision in further-education colleges (a 'tertiary' model) offers greater efficiency, more subject choice for learners, better teaching quality and ultimately better outcomes. Colleges also told us that such consolidation reduces the risk of small sixth forms being cross-subsidised by a school's pre-16 teaching. However, an independent review commissioned by the Welsh Government found a lack of robust evidence that small sixth forms were unviable, and that the most practical option was not to adopt a tertiary model across Wales but to develop locally tailored solutions. Subsequent research published in 2016 found no relationship between school sixth-form size and A-level results, except for a clear link between larger sixth forms and better achievement of the highest grades (three A* to A grades).
- 18 The Welsh Government sets clear annual guidance in the form of a remit letter to all colleges from the relevant Minister. However, the guidance is not grounded in a long-term sector strategy and priorities have varied to some extent from year to year, with the 2016/17 letter introducing a lot of new requirements, which colleges felt were difficult to incorporate into their delivery plans and made the 'real priorities' insufficiently clear. The Welsh Government has responded to these concerns by issuing a more focussed remit letter for 2017/18. Colleges also had some concerns about particular aspects of the guidance, notably the emphasis on universal adoption of the Welsh Baccalaureate, the cost of applying the Welsh Government's policy of mandatory GCSE resits in Maths and English for certain learners, and the greater emphasis on higher-level skills.
- 19 The Welsh Government has effective procedures to monitor the financial health of the sector. Colleges complete detailed financial returns three times a year, with colleges' financial health then rated from A to D ([Appendix 5](#)). Colleges in categories C and D are required to prepare a recovery plan that is monitored by the Welsh Government. In recent years the Welsh Government has required annual forecasts for only one year ahead, but has recently extended this to three years, which should support a longer-term assessment of financial resilience. Some colleges had already been preparing longer term forecasts, usually to contribute toward the longer term forecasts required from universities (which own some further-education colleges in Wales) by HEFCW.

- 20 Officials monitor progress against each college's agreed annual delivery plan on an ongoing basis, and publish statistics on the learners' completion, attainment and success rates annually. There were sector-wide learner opinion surveys each year between 2013 and 2015, and Estyn's inspection work and colleges' own self-assessment reports provide additional information on quality of provision. However, the Welsh Government does not consolidate the available data into a complete set of performance indicators. Colleges in England and Scotland, and universities in Wales, are required to report against a wider range of targets and performance indicators to their respective funding and oversight bodies.
- 21 Officials are taking various steps to strengthen outcome monitoring. New measures of learner retention and attainment (including grades where appropriate) will enable comparisons with school sixth forms for the first time. A new educational valued-added measure is being developed, and officials are working with HM Revenue and Customs to match Welsh Government with employment and earnings data, so that learners' destinations can be tracked and the information used to inform the planning of provision.
- 22 The Welsh Government has issued clear guidance on accountability through the Financial Memorandum for colleges and has supported ColegauCymru in developing its own code of governance for the sector. Officials rely on a review of colleges' annual accounts and other official reports to identify any major governance issues. HEFCW undertakes a more in-depth risk review for higher-education institutions, and the Welsh Government now plans to develop its own institutional review that will bring together available information on financial health, outcomes, quality, estates and any other important issues. The Welsh Government has also funded leadership development and consultancy programmes to support the sector.
- 23 The Welsh Government is at an early stage in considering how the Wellbeing of Future Generations Act will affect its direction, funding and oversight of further education. Colleges are not bound by the Act, but ColegauCymru has commissioned a research project on the sector's current sustainable development practice and the implications of the Act.

In response to reduced funding, colleges have cut part-time provision and costs, financial health varies across the sector and the impact on quality and outcomes is not yet clear

- 24 While colleges are financially stable in the short term, their financial health varies and the reductions in Welsh Government funding since 2011/12 have resulted in some deterioration of the sector's financial position. Income has fallen by around 11% in real terms and operating deficits were recorded in each of the three years to July 2016, while rising pension contributions and deficits are likely to reduce reported bottom-line surpluses from 2016/17. A large increase in pension deficits in 2015/16 following an actuarial valuation means that three colleges now have negative total reserves, and all colleges face rising pension contributions from April 2017. Nevertheless, the sector has shown resilience, maintaining cash reserves and liquidity and generating underlying surpluses (before adjusting for non-recurrent restructuring costs and pension revaluations) each year. Two colleges have recovery plans to address specific concerns but have not been considered by the Welsh Government to be in financial danger.
- 25 The quality of the further-education estate varies considerably and colleges see capital investment as a key business risk. The most recent data shows around 29% of the estate as being in poor or bad condition, and colleges estimated that it would cost about £192 million to restore the whole estate to a good condition. Colleges were concerned that current funding levels were insufficient both to replace ageing infrastructure and to maintain the estate in a good condition. Overall, Welsh Government funding to support the sector's capital expenditure has dropped from an average of £34 million a year in the two years to July 2011 to £17 million a year in the subsequent five-year period, and colleges have relied increasingly on their reserves and on external borrowing to finance capital investment. Some colleges are able to sell surplus property or borrow to fund investment, but many lack adequate security and income to borrow on a significant scale, especially with the recent increase in pension deficits.
- 26 Financial management in colleges is generally sound with regular reporting and a reasonable quality of financial information. However, medium-term financial planning is not well developed, with colleges citing uncertainty about future income streams as a reason for not doing more to model scenarios and plan finances over the longer term.
- 27 Colleges have responded effectively to smaller funding settlements by cutting costs and changing course delivery, but believe they have limited scope to make further savings without cutting provision for the 16 to 19 age group. Upward pressure on costs has partly offset some of the savings gains. Most notably increases in National Insurance and employer's pension contributions, and contractual entitlements under the Common Employment Contract. Expenditure cuts have resulted in large reductions in the workforce and with many remaining staff having wider or different responsibilities. Total whole-time equivalent staff numbers fell by 16.9% between 2012/13 and 2015/16, including an 11.5% reduction in teaching posts.

- 28 The sector as a whole has not been able to replace lower Welsh Government grant income with income from other sources. Net income from work-based learning contracts has increased modestly, but income from tuition fees, other grants and training contracts with other public-sector bodies has declined significantly with the decline in part-time learner numbers and reductions in public-sector budgets. However, several colleges have established business development teams to develop new commercial income, and income from these sources has increased significantly from a low base. Colleges in cities and areas with large employers with specialist training needs are best placed to exploit commercial opportunities.
- 29 The European Social Fund (ESF) has been a significant source of income for the sector and is projected to rise over the next three years, but would come to an end once the UK leaves the European Union. The UK Government has guaranteed funding for all projects approved before the withdrawal date, but the scope and amount of any replacement funding are inevitably uncertain at this stage.
- 30 Mergers were intended to ensure financial resilience and quality of provision, and while there has been limited formal evaluation there is some evidence that these benefits have been realised. However, the evidence points to an improvement in financial resilience, especially for smaller colleges merging with larger ones. Colleges have been able to achieve some efficiencies through consolidating courses and campuses, and sharing central services. Colleges merging with universities also cited improvement to students' progression to higher education as an advantage, but reported more limited financial benefits.
- 31 There has been a sharp fall in the number of students since 2010/11 as result of the Welsh Government's funding reductions. The number of full-time learners has increased slightly, but the number of part-time learners has fallen by 47%. Colleges have withdrawn many part-time courses and in some cases full-time courses have also been withdrawn or restricted to a small number of campuses to save money. This has been particularly challenging in rural areas where travel times between campuses are considerable.
- 32 An equality impact assessment by the Welsh Government highlighted the likely negative impact of funding reductions on over-18s (who mainly study part time) and women. Colleges also highlighted the effect on lower-income adults, especially women, who are more likely to study part time in community settings. The Welsh Government provides several EU-funded projects to help disadvantaged groups access the labour market, but the extent to which these projects replace lost funding for part-time provision is unclear.

- 33 The sector has maintained its performance on quality and outcome indicators over the three years to 2014/15. Learner voice surveys in 2013, 2014 and 2015 indicated that most learners continued to rate key aspects of their education and their overall learning experience as 'good' or 'very good', with rates remaining broadly unchanged over the period. Learner outcomes (in the form of completion, attainment and successful completion rates) have improved slightly over the period, continuing an upward trend evident since 2006/07. Estyn reports a strong record on quality at the three colleges that they have inspected in 2015 and 2016. These results are encouraging, but it is probably too early to fully evaluate the impact of funding reduction on standards and outcomes. The sector has started to identify options, through the Creative Solutions programme, for delivering services more efficiently while maintaining quality and promoting the Welsh Government's objectives of up-skilling the workforce. The financial outlook remains uncertain and colleges will need to sustain this proactive approach to face the main challenges ahead ([see below](#)).

Some key challenges facing the further-education sector in Wales

Changing demand	• Falling number of 16 to 18 year olds: the demand for full-time further education in this core group – the mainstay of colleges' services and funding – is likely to fall, and will fall in some colleges more than others. • The changing labour market: the local demand for education and skills changes continually in response to demographic trends, economic conditions and technological change, among other factors. • Evolving policy: the sector needs to adjust to Welsh Government requirements for the introduction of the Welsh Baccalaureate, the emphasis on literacy and numeracy and the emphasis on higher-level qualifications.
Continuing financial constraint	• Cost efficiency: the outlook for Welsh Government and European funding is uncertain and colleges need to plan for this uncertainty and for ongoing financial constraint. There are upward pressures on costs, much of the estate is in poor condition and future cost savings will become increasingly difficult without cutting provision. Many of the options for reducing costs, such as the greater use of e-learning or reducing formal accreditation requirements, will need policy changes or up-front investment. • Maintaining quality: colleges had maintained or improved the quality of their provision to 2015 but need to sustain this record in the face of lower budgets and changing demands on their services. • Developing alternative sources of income: all colleges are seeking to increase their commercial revenues to offset the decline in public-sector funding. Opportunities vary considerably across Wales and there has been mixed progress to date.
Setting a clear strategic direction	• Vision and oversight: the Welsh Government is considering its response to the Hazelkorn Review, which recommends a more integrated approach to post-16 education with a single vision and oversight body. • Well-being of Future Generations (Wales) Act 2015: while colleges are not bound by the Act, the response to the Hazelkorn Review provides an opportunity to re-set policy and guidance in the context of a longer-term strategy for the sector, and with appropriate links to policy objectives in line with sustainable development principles. • Collaboration: the sector needs to work with employers, schools and local authorities among others to plan its provision and deliver services in the most effective way. Relationships with schools in particular will need to be improved in some areas.

Recommendations

Recommendations	
Financial planning	
R1	The Welsh Government's revised revenue funding system was intended to provide three-year financial settlements for colleges (with the last two years being indicative allocations only) to aid financial planning. However, the need to cut the budget at short notice in 2013 has led to revenue funding allocations being made for only one year ahead. Such short funding horizons, coupled with unpredictable changes in revenue funding, have made it more difficult for colleges to plan effectively. While recognising the uncertainties facing the Welsh Government's own revenues, we recommend that the Welsh Government re-introduce three-year funding settlements at the earliest opportunity to assist colleges in their financial planning.
R2	Colleges welcomed additional funding provided by the Welsh Government for minor capital expenditure in 2016/17, but noted that it was offered with an unduly tight timescale for bids to be prepared and approved projects to be delivered; and as a result, only straightforward projects could be put forward. We recommend that the Welsh Government consider, as part of its institutional review process, how well placed colleges are to respond in the event of capital funds becoming available with tight timescales.
R3	At the time of our fieldwork, the majority of colleges forecast for only one year ahead and medium-term financial planning was not well developed, in part because the Welsh Government had been setting funding allocations annually and colleges were uncertain about future revenues. Medium-term financial planning would inform the Welsh Government's longer term planning for the sector, and enable it to better understand the likely impact of budgetary changes. We recommend that the Welsh Government requires colleges to prepare medium-term financial plans, including longer-term financial forecasts, and provide appropriate guidance and support, working with the sector to discuss any key underpinning assumptions.
Demand-responsive funding	
R4	The Welsh Government allocates core funding to colleges based principally on historic funding settlements, applying a uniform uplift on previous years' allocations. However, changes in the number of 16 to 18 year-olds are projected to vary considerably across Wales over the next 10 years, and learner numbers are likely to vary between colleges accordingly. We recommend that the Welsh Government develop a mechanism that links funding more closely to likely demand for further education in each area, while recognising the need to phase in significant changes in order to manage the financial impact on individual colleges.

Recommendations

Institutional reviews

- R5 The Welsh Government monitors a range of indicators relating to learner outcomes and financial health. However, these have not been consolidated into a formal performance framework for the sector, and colleges are not subject to specific targets other than delivery of the budgeted level of learning provision. **We recommend that the Welsh Government develop its institutional review framework to provide a comprehensive assessment of each college's performance and risks, and to report publicly on the main findings of these reviews each year.**

Strategic guidance

- R6 The Hazelkorn Review on the future of post-16 education in Wales recommended the development of a single, overarching strategy for post-16 education. Annual guidance varies from year to year, and in 2016/17 introduced extensive new requirements that colleges felt were difficult to incorporate into their delivery plans, although the 2017/18 guidance is more focussed. **We recommend that the Welsh Government provide focussed annual guidance for colleges, set in the context of longer-term, sector-wide strategic guidance.**

Impact assessment

- R7 The largest cuts in funding for colleges were made in 2015/16, but learner-outcome data is not yet available for that year. Equality impact assessments for previous funding allocations identified risks from cutting part-time provision that would be monitored and mitigated if necessary, but no further evaluation work was undertaken. **We recommend that the Welsh Government evaluate the impact of funding reductions on learners (including the impact on equality) once this data is finalised and use the results to inform future decisions on policy and funding.**

Part 1

The Welsh Government has cut grant funding for the sector, and while funding allocation and oversight arrangements are generally sound they would benefit from a more integrated and long-term approach



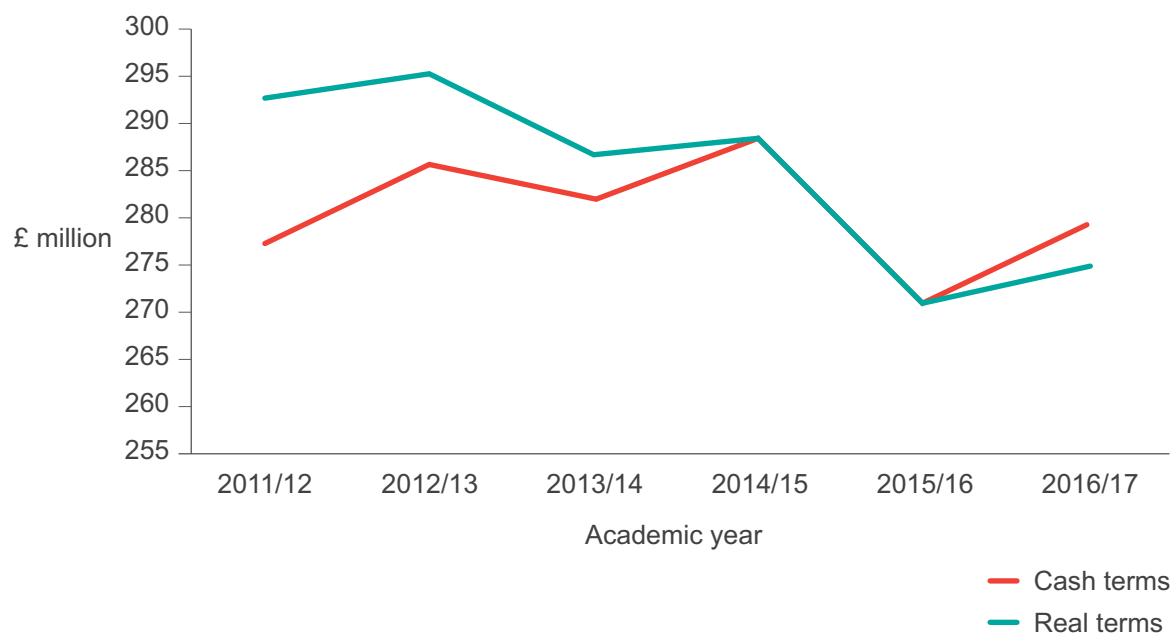
- 1.1 This part of the report examines the approach taken by the Welsh Government to further education. In particular we consider the Welsh Government's direction and funding of the sector and how it oversees the financial position, performance and governance of colleges.

The Welsh Government has reduced its grant funding but has protected full-time provision and work-based learning

The Welsh Government reduced overall grant funding for the sector by 13% in real terms between 2011/12 and 2016/17, with core funding for full-time provision increasing by 2.9% but with funding for part-time provision and for specific programmes and initiatives decreasing significantly

- 1.2 Welsh Government grants are the main source of funding for colleges, accounting for over two-thirds of the sector's income. Welsh Government revenue grant funding has reduced from £303 million in 2011/12 to £281 million in 2016/17, a decline of £22 million, or 7% in cash terms and 13% in real terms.
- 1.3 The Welsh Government provides grant funding mainly through a general revenue grant (referred to as 'core funding'). Between 2011/12 and 2016/17, Welsh Government core funding has increased by 0.5% in cash terms but has declined in real terms by 6.1% (Figure 3).

Figure 3 – Core revenue funding allocations to the further-education sector in cash and real-terms, 2011/12 to 2016/17



Note: Real-terms figures calculated from GDP deflator published on the HM Treasury website, taking June 2016 as the base.

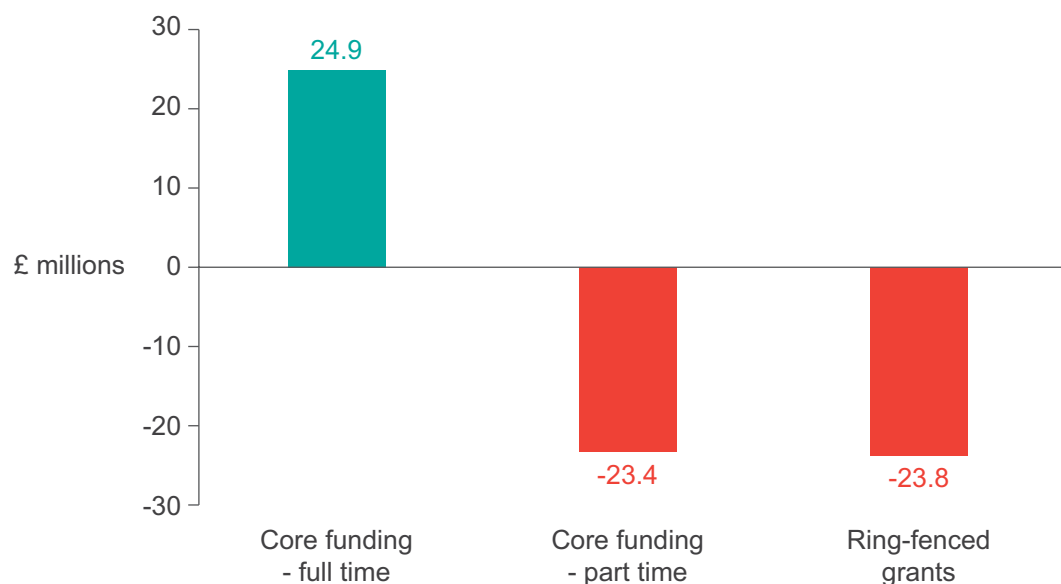
Source: Welsh Government funding allocation letters

1.4 The Welsh Government has sought to protect full-time provision for young people in the 16 to 19 age group, and has targeted core-funding reductions on part-time provision. Most (89%) part-time learners are over 19 years of age. As a result between 2011/12 and 2016/17:

- Core funding for full-time provision has risen by 2.9% in real terms; and
- Funding for part-time provision has dropped by 70.8% in real terms, with the main cuts falling in 2014/15 and 2015/16 (37.5% and 50% in cash terms respectively). Part-time provision has accounted for a relatively small proportion of core funding, falling from 12% in 2011/12 to 4% in 2016/17.

The protection of full-time provision for young people in the 16 to 19 age group is reflected in the pattern of change to grant funding (Figure 4).

Figure 4 – Changes in grant funding between 2011/12 and 2016/17 (cash)



Source: Welsh Government funding allocation letters

1.5 In addition, the Welsh Government can also provide grants which are ring-fenced for specific purposes (Box 1). Over time, the Welsh Government has phased out most ring-fenced grants or incorporated them into core funding. The total value of these grants in 2011/12 was £25.6 million, and increased slightly to £26.2 million in 2012/13 before falling in the following two years. For 2016/17, the Welsh Government is not providing any ring-fenced grant funding other than £2.0 million for the Enhanced Engineering Programme (now included as part of core funding) and £1.8 million of new funding for pilot projects intended to test new ways of delivering services put forward by the sector under the 'Creative Solutions' programme.⁹

⁹ The Creative Solutions working group, suggested by Welsh Ministers, was established by Colegau Cymru in July 2015 to develop proposals that were intended to create efficiencies while maintaining or improving the experience of learners. The Welsh Government has accepted most of the group's recommendations and implementation began in 2016.

Box 1: Welsh Government ring-fenced grants since 2011/12

Pathways to apprenticeships

The programme was launched in 2009 to provide a flexible route for young people to acquire the underpinning knowledge needed to complete a full apprenticeship successfully. The programme provided learners with an intensive one-year course, including a work placement, to prepare them for an apprenticeship at level 3. The Welsh Government provided funding of £25.8 million between 2011/12 and 2013/14 for this programme. An evaluation in 2014 found that the programme, overall, had not met its goals. The programme was discontinued from 2014/15, except for the engineering pathway which continued as a separate ring-fenced programme (see below).

Enhanced engineering programme

The programme emerged from the pathways to apprenticeships programme, where the engineering pathway had superior results for progression rates and feedback from learners, institutions and employers. The Welsh Government provided a total of £3.9 million for this programme over two years (2014/15 and 2015/16). In its second year a larger programme of learning was offered to a small number of engineering students. The Welsh Government continues to allocate funding for the enhanced engineering programme but it is now paid as part of the core funding allocation.

Skills priority funding

This funding was for colleges to deliver programmes of innovative training capable of raising and widening the occupational skills of employees, in line with local/regional labour market demand and opportunities. It provided part-time training for accredited qualifications to help develop an employer's overall workforce and to assist progression of individuals within the workforce. A total of £12.5 million was allocated for 2015/16 only.

Adult skills

Between 2011/12 and 2013/14 the Welsh Government provided £51.8 million for general adult skills provided through part-time courses.

GCSE resits

The Welsh Government allocated one off funding of £1.4 million in 2015/16 as a contribution towards the cost of applying its policy on GCSE resits. The policy outlines that all school-leavers enrolling on a one-year further-education course, and who obtained a grade D in GCSE English or Mathematics, should study for and re-sit the relevant examination with the aim of securing a grade C or above. For two-year courses the policy applies also to learners who obtained a grade E in English or Mathematics.

- 1.6 The decision to reduce funding for further-education colleges between 2013/14 and 2015/16 was driven by a reduction in the block grant from the UK Government and increases in the funds made available to the NHS in Wales. Within the Education and Skills expenditure group, Ministers have prioritised pre-16 education (especially early years) over post-16 education. Further-education funding has been targeted on full-time education for 16 to 19 year olds in light of the Welsh Government's statutory obligation to secure the proper facilities for the provision of education for that group, which means that part-time provision for older learners has borne the brunt of budget cuts.
- 1.7 Recent reports on further education by Audit Scotland and the National Audit Office highlighted broadly similar funding reductions in England and Scotland.¹⁰ There has also been a similar emphasis on prioritising full-time provision (mainly for younger learners), leading to a significant decline in the number of part-time older learners.

The Welsh Government has maintained the level of real-terms funding for work-based learning since 2011/12 with colleges securing a significant amount of the available funds

- 1.8 The Welsh Government also provides funding for work-based learning. There are a range of work-based programmes, including apprenticeships and traineeships, that support around 54,000 individuals in Wales to develop the skills needed to enter the labour market or to learn job-related skills while employed. Work-based learning contracts are issued by the Welsh Government following a competitive procurement process which is open to colleges, private and third-sector providers. For 2016/17, Welsh Government work-based learning funding amounts to £135.5 million, of which around 40% (£54.1 million) is for contracts led by colleges.¹¹
- 1.9 The Welsh Government has maintained funding for work-based learning contracts, with total funding rising by 7.5% in cash terms and 0.4% in real terms between 2011/12 and 2016/17. The sector reported net income of £35 million from work-based learning contracts in 2015/16 after sub-contracting £15 million to providers outside the sector. The Welsh Government's current 'Programme for Government'¹² commits to creating at least 100,000 high-quality all-age apprenticeships over the current Assembly term, and as a result expenditure on work-based learning may provide a financial opportunity for the sector.

¹⁰ The National Audit Office report (**Overseeing financial sustainability in the further education sector**, July 2015) highlighted an 11% reduction in Government funding in cash terms between 2010/11 and 2013/14. The Audit Scotland report (**Scotland's Colleges 2016**, August 2016) highlighted a 12.3% reduction in real-terms funding between 2011/12 and 2016/17.

¹¹ On an annual basis: the funding for the contracts was allocated for 16 months, so the annual figure is three-quarters of the amount allocated.

¹² Welsh Government, **Taking Wales Forward, 2016-21**, September 2016.

The Welsh Government intends that employers will have greater influence over skills provision and take a greater share of costs, although the UK Government's new Apprenticeship Levy has important implications for this co-investment policy

- 1.10 In response to the pressure on public finances, the Welsh Government intends to shift the emphasis from a government-led approach to skills investment to a system influenced and led by employers. The aim is to involve businesses more closely in identifying need and planning skills provision. Employers would then bear a greater share of the cost. This policy is known as co-investment (Box 2).

Box 2: Co-investment explained

The co-investment policy prioritises resources as follows:

- Government-led investment will focus on areas of economic and social return where government can take a lead role and support the focus on jobs, growth and tackling poverty. These areas include apprenticeships (especially higher level apprenticeships), essential skills and Welsh for adults.
- Any additional resources that become available will be used to fund joint action with employers. This will occur when the priorities of employers and Welsh Government align and when useful time-limited projects can be funded. These projects are intended to develop the supply of, and expand the demand for, skills provision, and improve the quality of skills investment.
- Employers will be expected to support their own workforce needs and to fund apprenticeships up to level 3. They would also fund other employer-specific training for those aged 19 and over. It is not yet clear how the Welsh Government commitment to create 100,000 high quality apprenticeships links to the co-investment agenda.

- 1.11 Greater co-investment provides an opportunity for the sector to develop and offer provision tailored to the needs of employers, which would generate additional revenue and contribute to the costs of running colleges. Colleges told us that co-investment had considerable potential but that it would take many years for them to fully develop commercial business operations sufficient to make a significant contribution to their finances, while requiring initial investment for marketing, working capital or acquisition of existing companies. Colleges also emphasised the need for a change in attitude among small and medium-sized enterprises, which they felt had become used to subsidised provision (especially from the European Social Fund in West Wales and the Valleys), and were therefore very unwilling to make any financial contribution towards the cost of training staff.

- 1.12 The introduction of the Apprenticeship Levy by the UK Government from 2017 has important implications for the co-investment policy. The levy will be payable by all large employers at a rate of 0.5% of their wage bill over £3 million a year and is intended to incentivise employers to invest in educating and training their workforce. The levy will be collected from Welsh employers as elsewhere in the UK and passed to the Welsh Government by adjusting the block grant, but the Welsh Government is expecting that this income will be offset by the effect of various other changes, with no increase in funding for the Welsh Government overall.
- 1.13 The Welsh Government has decided to maintain the budget for work-based learning, but does not wish to alter its current policy of targeting provision on certain sectors, so levy-payers cannot be sure of receiving publicly funded work-based training to the value of the levy that they have paid. The Welsh Government acknowledges that this situation will dampen large employers' willingness to co-invest in workforce development. Companies with a pay bill of less than £3 million a year are not affected but smaller employers tend to be less willing to spend on education and training. The 2017/18 annual Ministerial remit letter for colleges urges the sector to continue efforts to encourage co-investment. The majority of apprenticeship delivery takes place in smaller businesses that will not be subject to the Levy.

The Welsh Government has no core capital funding programme specifically for the sector, and, although some colleges have had projects supported through the 21st Century Schools and Education programme

- 1.14 The Welsh Government does not operate a regular capital budget solely for the further-education sector, but has a capital budget for all educational infrastructure administered through the 21st Century Schools and Education Programme. The programme provides grants to cover 50% of the cost of new buildings or major upgrades¹³ and is run over a number of waves, or bands of investment.
- 1.15 The first round of 21st Century Schools and Education Programme funding covered projects that were to be completed between 2014 and 2019. This round of funding was focussed mainly on schools due to the poor condition of many buildings, and the need to rationalise the schools estate to deal with surplus capacity. Schools have accounted for 94% of the £1.4 billion set aside for the first round of the programme. Nevertheless, the further-education sector has also benefited, with £37.9 million of grant approved for five projects with a total project investment of £79.7 million. One of these projects – for the Cardiff and Vale College's city centre campus in Cardiff – is the second largest in the whole programme, with a grant of £20 million towards an overall cost of £44 million.

¹³ On behalf of the Auditor General, Wales Audit Office staff are currently undertaking a separate examination of the 21st Century Schools and Education Programme.

- 1.16 Colleges will shortly be able to bid in the second round of the 21st Century Schools and Education Programme covering the period 2019 to 2024. As yet, the total amount of Welsh Government funding available, the proportionate contribution from the sector and the funding mechanism are still to be confirmed. Colleges have recently provided updated condition survey data for their estates to support their and the Welsh Government's future decision-making.
- 1.17 Since the start of the 21st Century Schools and Education Programme, the Welsh Government has made dedicated capital funding available to colleges on one occasion. In March 2016, the Welsh Government confirmed that it would be making available around £22 million in grant funding for small-scale capital projects after funds became available at short notice (Box 3). The funding was for IT equipment, training equipment and small-scale construction projects. Colleges submitted bids for £38.2 million and the Welsh Government approved bids for £23.3 million of grant. Individual colleges received between 50% of the funding requested for capital build projects and 100% of the funding requested for IT and skills equipment.

Box 3: Welsh Government funding of small scale capital projects in 2016-17

In March 2016, officials responsible for Welsh Government capital funding were notified that £22 million could be made available from the 2016-17 budget for capital projects in the further-education sector. However, the projects would have to be completed and grants paid before 31 March 2017. Colleges were invited to bid in April 2016 for grants from three funds (£5 million for IT equipment, £5 million for training equipment, and £12 million for small-scale construction projects that could be completed before the end of March 2017). The Welsh Government subsequently approved grants for £12.7 million worth of small-scale construction projects, £5.5 million for training equipment, and £5.1 million for IT equipment.

Given the tight timescale, officials amended the usual appraisal process for capital projects to evaluate bids more quickly and most grants were awarded in July 2016, with some construction projects being approved shortly afterwards. Nonetheless, the colleges we visited noted that timescales were very tight and that it would not be possible to undertake construction work in the summer (the most suitable time of year). They also commented that the short notice – two weeks – for completion of bids meant that only straightforward projects could be put forward.

Welsh Government officials acknowledged these concerns but responded that they had to work within the disciplines of the Welsh Government's annual budgeting process, and that they had run the process as efficiently and quickly as possible in order to maximise the time available for colleges to deliver their projects. We have not reviewed the detail of the Welsh Government's administration of this grant funding.

The sector has mostly welcomed recent reforms to the way core funding is allocated to each college but would prefer longer-term funding horizons, and allocations do not account for local changes in need

Reforms to the way funds are allocated to colleges are generally welcomed by the sector

- 1.18 Since 2014/15, and in response to colleges requesting more certainty over annual funding levels, the Welsh Government has used the same base allocations to calculate indicative allocations for each college. The base allocation for each college typically increases or decreases by the same proportion, unless a specific transfer of provision needs to be funded (for example, between schools and colleges for sixth-form provision).
- 1.19 Each college develops an annual delivery plan for the type and amount of learning provision that a college expects to deliver in the following academic year. The plan is based on the college's own assessment of learning needs in its area in the context of available labour-market information and the Welsh Government's policy and guidance on skills and further education. The annual plan is finalised in the spring once the college receives confirmation of its final funding allocation for the following academic year, usually in January.
- 1.20 The Welsh Government, in consultation with the sector, has developed a new planning and funding framework that changes the way that colleges plan their provision and draw down their funding allocations. The new framework came into effect from the 2014/15. The previous system awarded a specific amount for each credit equivalent unit, with each element of provision worth a certain number of credits. As a result, colleges were able to increase their credits and the income then drawn down by enrolling learners on supplementary courses or other activities. The new framework awards a particular value to a complete learning programme for each learner. Each programme is intended to provide a comprehensive package of support for the learner (Box 4).

Box 4: The complete learning programme explained

A complete learning programme comprises:

- **The core:** essential skills development and support and enrichment activities to help learners achieve their main qualification, and progress into employment or higher education. It is based on the core of the current Welsh Baccalaureate Qualification.
- **Main qualification:** teaching for an approved vocational or general educational qualification.
- **Community, learner, industry focus:** additional provision to tailor the programme to the specific needs of the community, learner or a specific industry. This might include a GCSE resit or a mandatory health and safety certificate, for example.
- **Work-related experience:** any additional work experience that is required to complete the learning programme, over and above the 30 hours set out in the Welsh Baccalaureate core.

In almost all cases, a learner has a single learning programme at any one time.

- 1.21 The number and value of learning programmes actually delivered determines the amount of income that a college can draw down from the financial allocation made available by the Welsh Government. There is some flexibility as colleges are able to draw down their full allocation, providing the value of the learning programmes actually delivered is within 2.5% of the financial allocation.
- 1.22 The new planning and funding framework is intended to ensure that colleges have no financial incentive to provide unnecessary activities. The new framework includes a number of other changes intended to improve value for money:
- Restricting approved learning programmes to those that are likely to add value in terms of a learner's life chances. Programmes must lead to an approved qualification and provide a coherent and substantial programme of learning, with, for example, a programme based on a single A level not being eligible for funding.
 - Funding rates are based on the assumption that colleges achieve an average successful completion rate of 81%.
 - Programmes relating to early drop-outs (learners leaving the course less than eight weeks after it begins) are not funded, nor are they counted in performance statistics. This approach incentivises colleges to avoid early drop-outs while not penalising them by counting early drop-outs when calculating success and completion rates.

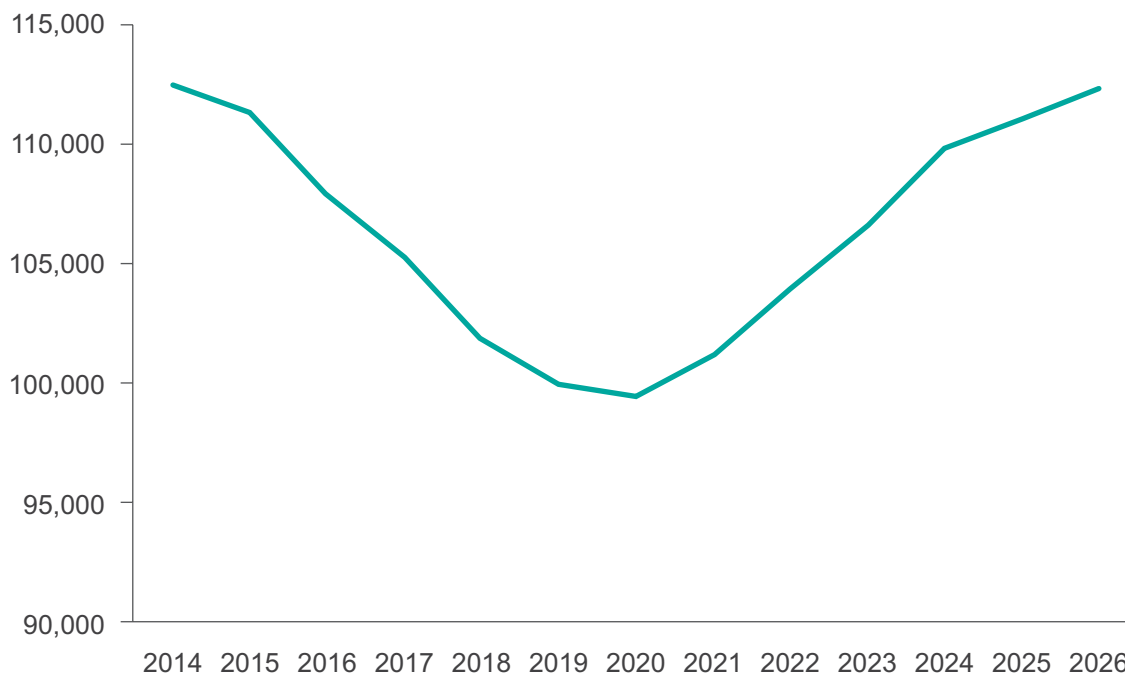
- 1.23 To reflect the higher costs of providing services, the Welsh Government includes uplifts for the most deprived areas and for sparsely populated areas. The total allocation for deprivation is £13.6 million for 2016/17. Sparsity uplifts are based on the size of the college and number of learners drawn from rural areas, and around £3.6 million was allocated in 2016/17. The Welsh Government reviewed the uplift rates when developing the new planning and funding framework but decided to leave them unchanged, and has since adjusted the uplifts in line with the general allocation.
- 1.24 Most of the colleges that we visited supported the new planning and funding framework. They believed that it had simplified and improved funding, created a stronger focus on learner needs and avoided unnecessary provision. Their views accorded with those of Welsh Government officials. However, Coleg Ceredigion and Grŵp Llandrillo Menai commented that the sparsity uplift did not fully cover the additional cost of delivering accessible services in rural areas.
- 1.25 The new planning and funding framework also applies to A-level and vocational provision in sixth forms in local-authority funded schools. However, as local-authority secondary schools also receive separate funding for GCSE provision (ages 11 to 16) they have the potential to cross-subsidise sixth-form provision. A review of sixth-form provision in 2016 acknowledged this risk and concluded that it warranted further assessment ([paragraph 1.46](#)) but the question of whether cross subsidy actually takes place was outside the scope of this report.

The current approach does not enable local changes in need to be reflected in funding allocations and the sector would prefer longer-term funding horizons

- 1.26 The new way the Welsh Government calculates funding allocations that was introduced in 2014/15 is based on a uniform percentage uplift to previous settlements ([paragraph 1.18](#)). While this approach may provide a degree of certainty for colleges, it means that funding allocations cannot reflect changes in the level of need across Wales, for example in the population of young learners. A key determinant of the need for full-time courses is the number of 16-18 years olds, as further-education provision is targeted at this group. Other factors will influence the need for full-time courses, most notably the choices made by young people. But the level of need for provision across colleges is likely to be sensitive to sharp changes in the population size of this age group.

1.27 The number of 16 to 18 year olds is projected to continue to decline in Wales until 2020, with a projected fall of 11.6% between 2014 and 2020, before recovering to the 2014 level in 2026 (Figure 5). The same general pattern is seen in population projections for Scotland and England, although the decline in the number of 16 to 18 year olds bottoms out a year earlier in these parts of the UK. The number of full-time further-education learners in Wales increased slightly between 2011 and 2015, despite a 4.9% reduction in the number of 16 to 18 year olds, in part reflecting the transfer of some sixth-form provision into the sector from schools. However, the predicted continued reductions in the size of this age group may reduce the need for full-time courses.

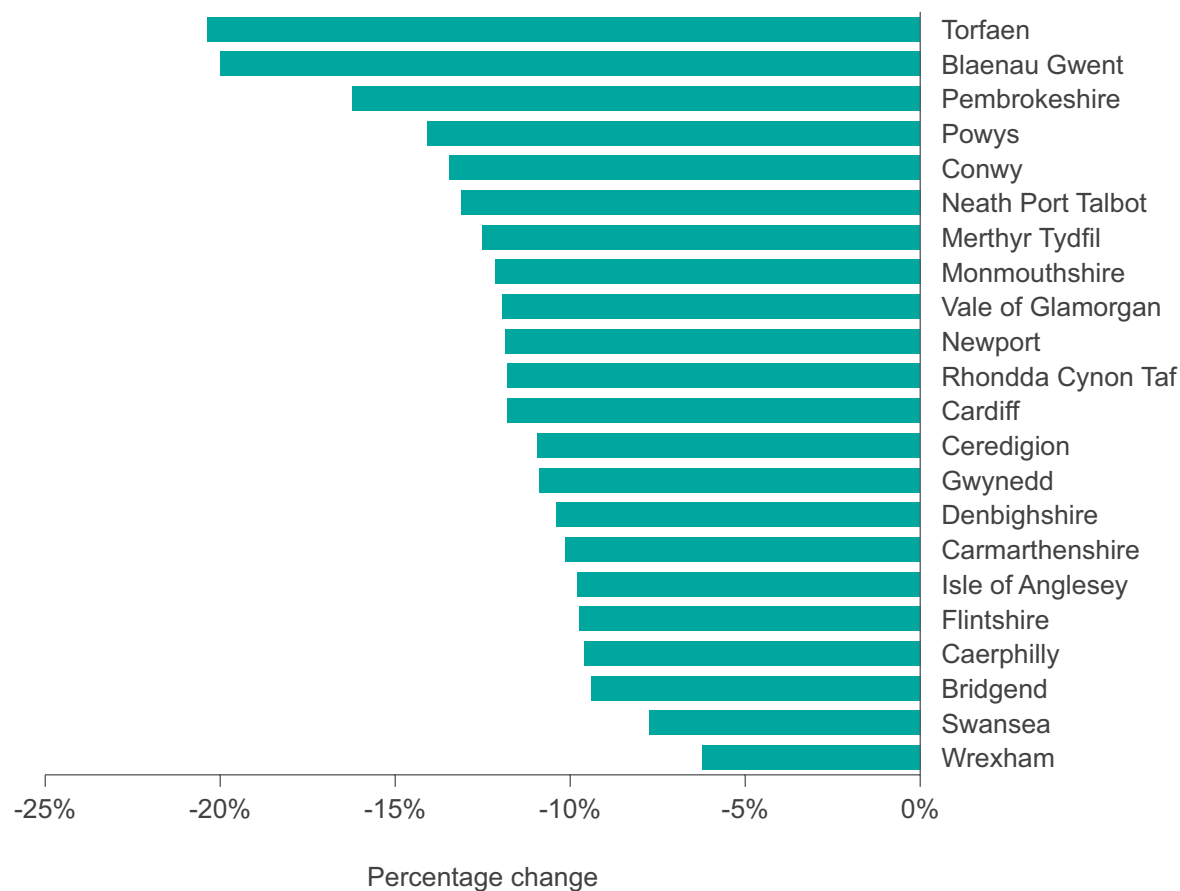
Figure 5 – Projected numbers of 16 to 18 year olds in Wales, 2014 to 2026



Source: Wales Audit Office analysis of Welsh Government (StatsWales), **2014 based local-authority population projections for Wales, 2014-2039**, September 2016

1.28 Between 2014 and 2020, the numbers of 16 to 18 year olds is projected to fall in all local-authority areas. However, the extent of the projected falls ranges from 6.2% in Wrexham to 20.4% in Torfaen (Figure 6). Therefore, the potential financial impact of any reduced need for full-time provision is likely to vary across colleges. Under the current approach, these projected changes and their likely impact on need cannot be reflected in the individual allocations to colleges.

Figure 6 – Projected change in the number of 16 to 18 year olds by local authority, 2014-2020



Source: Wales Audit Office analysis of Welsh Government (StatsWales), **2014 based local-authority population projections for Wales, 2014-2039**, September 2016

- 1.29 Colleges would like the Welsh Government to set longer-term funding horizons. This would offer colleges more certainty about their income levels and aid their business planning. The Welsh Government had introduced three-year financial allocations from the 2011/12 academic year, with the first year being a firm allocation and the following two years indicative only. Colleges welcomed this approach and the Welsh Government intended to maintain it under the new planning and funding framework. However, having confirmed the 2013/14 allocation in January 2013, there were unexpected changes to the Welsh Government's block grant from the UK Government. As a result, the Welsh Government cut the 2013/14 allocations only a month before the start of the year.
- 1.30 The Welsh Government believes that such issues cast doubt on the reliability of indicative funding estimates, and as a result reverted to annual budgeting from 2015/16. The result of the referendum on the UK's membership of the European Union has created additional uncertainties, and for 2017-18 the Welsh Government has focused on a single-year budget with no future-years' commitments. Officials informed us, however, that they would prefer to offer three-year allocations if this became practical in the future.
- 1.31 The colleges we visited also criticised the Welsh Government approach to capital funding. They see capital funding being made available at short notice and on an ad hoc basis, rather than as part of a planned, long-term approach to capital requirements (paragraphs 1.14 to 1.17 and Box 3).

There is no unified strategy for the further-education sector or for post-16 education, and although collaboration and joint working are generally sound, relationships between colleges and schools are a concern in some areas

There is no unified strategy for the sector or for post-16 education generally

1.32 The Welsh Government does not have a single, unified strategy for the further-education sector or for post-16 education generally. The three main strategies that affect the further-education sector are:

- The **Youth Engagement and Progression Framework** published in September 2013 – which aims to reduce the number of young people aged 11 to 25 who are not engaged in education, employment or training¹⁴;
- The **Policy Statement on Skills** made in January 2014, supported by the **Skills Implementation Plan** published in July 2014 – which covers post-19 skills and employment policy; and
- The Welsh Government's overall strategy for education for 3-19 year olds, **Qualified for Life** published in October 2014 – which sets out a long-term vision for education provision across all providers.

1.33 These policy documents cover the whole post-16 education sector, and in the case of Qualified for Life the entire education system for 3-19 year olds. With some exceptions, the actions contained in them are not specific to colleges. Nevertheless, the contribution of the further-education sector is fairly clear in most cases.

1.34 The Welsh Government commissioned the 'Hazelkorn Review'¹⁵ to examine the oversight arrangements for the post-16 education and training system in Wales. The Hazelkorn Review reported in March 2016 and concluded that:

- the Welsh Government lacked an overall vision for the post-compulsory education system that is aligned to the social, cultural and economic needs of Wales; and
- there was a lack of strategic thinking and joint working between public institutions, leading to insufficient collaboration, lack of critical mass, and too much competition for limited resources with little benefit to Wales.

¹⁴ The Auditor General's July 2014 report, **Young People not in Education, Employment or Training**, found that the Welsh Government was well placed to help 16-18 year olds but the Framework is not sufficiently clear about support for 19-24 year olds.

¹⁵ Professor Ellen Hazelkorn (for the Welsh Government), **Towards 2030: a framework for building a world-class post-compulsory education system for Wales**, March 2016.

- 1.35 The Hazelkorn Review recommended developing a single over-arching vision for post-16 education, based on certain guiding principles and closer links between policy, providers and social and economic goals. Professor Hazelkorn also recommended that a single, autonomous agency be established to co-ordinate and oversee the sector and to deliver the vision. In January 2017, the Welsh Government announced that it would consult on establishing a new, arm's-length strategic authority to oversee post-compulsory education and training. The new body would be given responsibility for planning, funding, contracting, ensuring quality, financial monitoring, and performance and risk review.
- 1.36 Any strategy specifically for the further-education sector would need to be integrated with the over-arching vision recommended by Professor Hazelkorn for post-16 education and training. A sector-specific strategy could set longer-term priorities for the sector and explain more fully how the sector is expected to contribute to relevant policy objectives. College leaders and senior officials in the Welsh Government indicated to us that they would support the development of such a strategy, although they did not think its absence had hindered individual colleges in developing appropriate provision in their areas.

The Welsh Government has a good relationship with the sector, collaboration and joint working are generally sound, but relationships between colleges and schools are a concern for colleges in some areas

- 1.37 Until 2015, responsibility for further education and schools lay in a single Welsh Government department, and until 2016 further-education funding and skills policy was the responsibility of a single Deputy Minister served by that Department. However, recent changes have created different lines of responsibility and accountability:
- The Minister for Lifelong Learning and the Welsh Language has responsibility for further-education funding and vocational skills, and issues the Ministerial remit letter – but the Cabinet Secretary for Education approves the further-education budget, and the Minister for Skills and Science (reporting to the Cabinet Secretary for Economy and Infrastructure) is responsible for work-based learning, sector skills, youth and adult employability. The Cabinet Secretary for Finance and Local Government remains responsible for the European Structural and Investment Funds, including the European Social Fund.
 - Officials responsible for further-education work mainly in the Skills, Higher Education and Lifelong Learning part of the Economy, Skills and Natural Resources Group – but the Education and Public Services Group is responsible for schools policy.

- 1.38 At this early stage, the new arrangements do not appear to have caused any practical difficulties, but colleges that we spoke to highlighted the risk that policy and delivery could become less integrated and coherent over time.
- 1.39 Colleges have a good relationship with officials in the Welsh Government responsible for further education. The colleges we visited consider officials to be supportive, experienced and having an excellent understanding of the sector. These colleges also consider that the nature and timing of communications are effective. Both the colleges and Welsh Government officials cited the small size of the sector in Wales and staff continuity in the Welsh Government as key benefits in sustaining close working relationships.
- 1.40 Colleges have established several networks that meet regularly to discuss particular topics, for example, for finance directors and heads of curriculum. These networks and ColegauCymru provide an efficient way for the Welsh Government to consult and liaise with the sector, and college leaders see these arrangements as effective.
- 1.41 Most colleges provide some higher education and reported good relationships with higher-education institutions, despite some concerns about competition between the sectors in the provision of higher-level vocational courses. ColegauCymru has asked the Welsh Government to ensure that Welsh universities are not planning to increase traditional three-year degree programmes to four years (with the first year being a level 3 qualification, typically offered by further-education colleges). The Welsh Government has consulted on ending publicly funded student support for such courses. The Welsh Government also published a review of higher education in further-education colleges in 2015¹⁶, which recommended greater collaborative working between the sectors, supported by regional planning (Box 5).

Box 5: Summary of the 2015 review of higher education in further-education colleges

The review found that colleges were well placed to deliver higher-level skills training, such as foundation degrees and Higher National Diplomas, because of their good connections with local employers. The report concluded that colleges could deliver intermediate courses flexibly and locally. The review found that colleges could also contribute to widening access to higher education, especially for learners who needed part-time provision or wished to study close to home. The report recommended expanding such provision in critical economic sectors and that HEFCW and ColegauCymru work together to determine how this could be best achieved.

¹⁶ Welsh Government, **Review of Higher Education in Further Education Institutions**, Welsh Government Research Document 063/2015, June 2015.

- 1.42 Good working relationships between colleges and schools are vital to ensure that learners receive appropriate guidance on their options at age 16. They are also needed to help learners move smoothly to the next stage of education, training or employment, and can be beneficial in a range of other areas. For example, colleges reported good co-operation on school and college transport (Coleg Gwent), an agreement to take on a school's sixth-form provision (Bridgend College), and joint working with Cardiff Council to build a new school and sixth-form centre on a site in the east of the city (Cardiff and Vale College).
- 1.43 However, working relationships with schools are variable even within college catchment areas, and some colleges reported that relationships with individual schools can be difficult. This is especially the case where colleges or local authorities are seeking to consolidate sixth-form provision in new sixth-form centres or further-education colleges. Some colleges expressed concern that schools were deliberately routing pupils towards their own sixth-form classes even if a vocational route at a college was clearly more appropriate. The sector's view is that most schools continue to reinforce a strongly academic culture that causes learners and parents to see vocational education as a second-class option. The sector is keen for this to change and to develop a more integrated and balanced educational system.
- 1.44 Colleges told us that there was often strong local resistance from schools and parents towards any proposal that involved closing schools' sixth forms and transferring provision into a sixth-form centre (the tertiary model). The tertiary model has made limited progress in Wales, although Blaenau Gwent and Merthyr Tydfil have now introduced a fully tertiary model (Box 6). An element of consolidation is taking place or is proposed in several other areas. We asked the Association of Directors of Education in Wales (ADEW) for their perspective on the issue of sixth-form reconfiguration. The Association emphasised that the likelihood of a successful outcome for any local review can be enhanced through effective relationship building and partnership working between all interested parties based on a common purpose and clear evidence.

Box 6: Tertiary sixth-form model in Blaenau Gwent

In 2010, Blaenau Gwent County Borough Council committed itself to closing sixth-form provision in its secondary schools and transferring all post-16 education to a new purpose-built 'Learning Zone' in Ebbw Vale to be run by Coleg Gwent and part-funded through the transitional Programme, which was the precursor to the 21st Century Schools and Education Programme. The Council believed that centralising post-16 provision at a new site would deliver the following benefits:

- Specialist teaching for a wider choice of A-level courses, made possible by the larger number of learners;
- An expanded range of vocational provision, which had previously been limited in Blaenau Gwent, meaning that learners had to travel further afield for many courses;
- An improvement in the learning environment; and
- Due to these factors, an improvement in academic attainment.

The Council pressed ahead with the changes despite some opposition from schools and sections of the local community. School sixth forms were closed to new entrants in September 2012 when the new Learning Zone was opened. Since then, both A-level and GCSE results across the county borough have improved, as have certain other indicators such as student attendance. The Council believes that the improvement in A-level academic performance is attributable mainly to the centralisation of post-16 provision at the Learning Zone.

The ongoing financial impact is neutral as schools and colleges are funded in the same way and at the same rates for A-level provision. The Council funded the cost of transition, which was around £1 million for schools to continue teaching learners in the second year of their A-level course in 2012/13. The Council considers that the withdrawal of post-16 teaching did not have a detrimental financial impact on the schools affected, and reports that all three of those schools recorded a financial surplus in 2014/15.

- 1.45 The further-education sector generally believes that rationalising sixth-form provision is both more efficient and in the best interests of learners. They believe larger sixth-form centres provide better choice, teaching quality, and ultimately better outcomes. The view from the sector is that small school sixth forms provide a limited range of subjects and often very small class sizes. The sector also believes that small class sizes indicate that schools are cross-subsidising, funding their sixth forms with income intended for pre-16 education.
- 1.46 In light of these concerns and differing views on the tertiary model, the Welsh Government commissioned a review of options for sixth-form provision from Professor Sue Maguire, which reported in March 2016¹⁷. The report concluded that there was a lack of robust evidence to support the notion that small sixth forms were unviable. The report also concluded that there was a risk of schools subsidising their sixth forms with funding for pre-GCSE education that warranted further assessment.
- 1.47 Professor Maguire identified four options for delivery of sixth-form provision, one of which was a fully tertiary model across Wales. While a tertiary model had been implemented successfully in parts of Wales, this had tended to be in urban areas where transport to the new sixth-form centres is cheaper and easier, and had been accompanied by the construction of new facilities that would be prohibitively expensive to replicate across the whole of Wales. A variety of local factors, such as a desire to maintain Welsh medium provision and the availability of faith based options, influenced resistance to change. Professor Maguire suggested that a more flexible and feasible approach would be for local area partnerships to review provision and develop locally tailored solutions, underpinned by targets for removing surplus places in schools. She also highlighted the need to develop comparable post-16 performance data for further education and schools (now underway – [paragraph 1.63a](#)) and conduct further research to fill evidence gaps and spread good practice in collaborative working.
- 1.48 The Welsh Government commissioned separate research¹⁸ on possible links between the size of school sixth forms and A-level results. The study concluded that sixth-form size was not related to A-level performance except for the highest grades, with a pupil's chance of securing three A* to A grades increasing steadily from 5% in sixth forms with around 100 pupils to 11% in sixth forms with around 500 pupils. This effect was boosted if a sixth form had a large Year 13 and a smaller Year 12. Conversely, pupils attending sixth forms with a larger Year 12 were likely to have poorer A-level point scores. The reasons for this effect remain to be investigated.

¹⁷ Professor Sue Maguire, **A Think Piece on the Possible Options for Improving the Performance and Efficiency of sixth forms in Wales**, Welsh Government social research paper no 12/2016, March 2016.

¹⁸ Professor James Foreman-Peck, **The Impact of Schools Sixth Form Size on Educational Attainment of Pupils at Key Stage 5**, Welsh Government social research paper no 78/2016, November 2016.

The Welsh Government sets clear annual guidance for the sector but colleges have had concerns about some aspects of the guidance

- 1.49 The relevant Minister issues an annual remit letter to all colleges that sets out the priorities that colleges are asked to take into account when planning provision for the following academic year. The annual remit letter was introduced from 2011/12 in response to a request from the sector for clearer, more specific guidance on policy priorities. This guidance is not binding on the colleges, but Welsh Government officials expect the priorities and associated actions to be reflected in each college's operational plan.
- 1.50 The Welsh Government does not intend that the annual remit letter creates a new policy framework each year. Rather the priorities are simply intended to emphasise certain aspects of existing policy and identify specific actions that colleges are expected to take. For example, in 2015/16 the letter identified a series of actions to help support the tackling poverty agenda such as identifying and supporting learners at risk of dropping out of courses.
- 1.51 The annual remit letter reflects the Minister's own views on policy priorities as well as suggestions from relevant heads of division within the Welsh Government. The colleges we visited consider that the letters are clear and that they address them appropriately through their annual operational plans. The colleges were mostly comfortable with the content of the annual guidance within the remit letter but had concerns about certain specific aspects (Figure 7).
- 1.52 There was also a consistent view from the colleges that we visited that the 2016/17 priority letter was more extensive than in previous years, and that it introduced a considerable number of new requirements. Colleges had some concerns about the range and extent of the work required, whether the 'real priorities' were sufficiently clear, and a loss of local autonomy. As a result, colleges reported that it was more difficult for them to incorporate the requirements of the letter into their delivery plans. Welsh Government officials acknowledged these concerns and accepted that more focussed guidance would be desirable, ideally set in the context of a longer-term strategy for post-16 education, and the 2017/18 letter includes fewer specific requirements. Some colleges also expressed a preference for longer-term guidance on priorities to make planning easier and more effective.

Figure 7 – Concerns from colleges on current Welsh Government guidance

Requirement	Concerns from colleges
Welsh Baccalaureate The new Welsh Baccalaureate was introduced from 2015/16 with the intention that it would be universally adopted by September 2020.	Many colleges thought that this policy was unduly prescriptive and was driving some learners in border areas to study for A levels in England instead of Wales.
GCSE re-sits From 2015/16 many post-16 learners are required to re-sit their Mathematics and English GCSE exams if they have not obtained grades A* to C in these subjects.	- The Welsh Government believes that an A* to C grade in Mathematics and English is a major benefit for further learning and for the employment market. It now requires further-education learners to re-take the relevant exam if they obtained a grade D and are following a one-year course, or obtained a grade D or E and are following a two-year course. - Several colleges felt that the policy was impractical because they could not realistically provide the amount of tuition time required for learners to reach the necessary standard. They also expressed concern that the cost was not fully covered by the Welsh Government, despite an additional £1.37 million of funding announced in March 2016 for the 2015/16 academic year.
Emphasis on higher-level skills The Welsh Government priority letters make clear the emphasis on developing higher-level skills (level 3 and higher), as research indicates a big improvement in career/earnings potential for people with qualifications at this level and above (lower level qualifications having little or no impact). Welsh Government officials are keen for colleges to shift their focus towards higher-level qualifications, pushing all learners to progress as far as possible.	- Several of the colleges perceived a reluctance by the Welsh Government to fund level 1 and, to a lesser extent, level 2 courses. Welsh Government officials told us that they remained open to funding level 1 and level 2 qualifications, and that it was up to colleges to make a case for the volume of provision that they felt was necessary. - Colleges reported a continuing demand for lower-level courses from learners and employers across the country; and believed these qualifications were important foundations for further learning as well as being appropriate stand-alone qualifications for many learners who are not academically inclined. - Colleges were also concerned that the emphasis on higher-level skills was inconsistent with the Welsh Government's drive to tackle poverty, which often required a focus on basic skills and lower-level qualifications to provide a pathway out of economic inactivity and poverty.

Source: Grant Thornton and Wales Audit Office fieldwork visits

The Welsh Government's financial monitoring is effective but there is no consolidated set of indicators to assess performance

The Welsh Government's financial monitoring is effective and has recently been improved by the re-introduction of medium-term financial forecasts

- 1.53 In January 2007, the Welsh Government issued a circular setting out its financial health-monitoring procedures and the associated requirements for colleges. The circular requires each college to provide detailed financial information¹⁹ in a consistent format three times a year. The Welsh Government then analyses the data provided by colleges and calculates key financial ratios and other indicators of financial health. Based on this information, officials allocate each college to one of four financial health categories (Box 7).

Box 7: The Welsh Government's financial health categories explained

Category A reflects that the institution's financial position and its financial strategy fully support the institutional plan.

Category B reflects that the institution's financial position and its financial strategy currently support the institutional plan but could be strengthened.

Category C reflects that the institution's financial position or its financial strategy require improvement to support the institutional plan.

Category D reflects that the institution's financial position is weak and does not support its financial strategy or the institutional plan

Appendix 5 summaries the criteria for allocating a college to a category.

- 1.54 The category is notified to the college but is otherwise confidential to the Welsh Government on the grounds of commercial sensitivity. A summary of the financial information provided by each college and a sector summary is presented to the further-education finance directors network. An annual report summarising the results of financial-health monitoring is also submitted to the relevant Minister. The current financial health of the sector is covered in paragraphs 2.2 to 2.18.
- 1.55 The circular includes appropriate guidance for action if colleges are in financial difficulty. The guidance requires any college categorised as D, or as C with a deteriorating position, to prepare a recovery plan. The Welsh Government is flexible on the precise content and format of the recovery plan, but requires a college's governing body to monitor progress with the plan. Two colleges have prepared recovery plans since 2012.

¹⁹ Information includes a detailed breakdown of income and expenditure, cash flows, and a balance sheet with details of assets, liabilities and reserves.

- 1.56 The Welsh Government has the authority to request specific information and undertake additional monitoring for colleges in financial difficulty. However, the extent of monitoring activity undertaken depends on the Welsh Government's assessment of the college's recovery plan and the calibre of its management team. Senior officials visit financially weak colleges regularly to discuss progress with their recovery plans. The Welsh Government believes that these arrangements are adequate and proportionate.
- 1.57 We consider the Welsh Government's monitoring procedures for assessing each college's current financial health to be effective. The process is well established and works smoothly, and the colleges we visited were content with the process and the parameters used.
- 1.58 In recent years, most colleges only prepared forecasts for one year ahead, in line with Welsh Government requirements, while colleges in England and Scotland were required to prepare forecasts for two years ahead. However, the Welsh Government asked colleges to prepare their July 2016 forecasts for the following three years instead of one year ahead. HEFCW requires higher-education institutions to produce forecasts each year for four years ahead. Several colleges are now having to complete such forecasts, either because they receive funding directly from HEFCW and need to prepare them to gain approval for their fee and access plan, or because they are part of higher-education institutions that are covered by the same requirement. In the absence of medium-term financial planning, Welsh Government officials make their own assessment of each college's financial resilience and likely future prospects.

The Welsh Government does not yet have a single consolidated set of performance indicators to monitor the sector against

- 1.59 A college's operational plan forms the basis for the Welsh Government's non-financial monitoring procedures. Welsh Government officials meet college leaders twice a year to discuss progress against the agreed plan, using data on learners and qualifications submitted by colleges. Officials compare enrolments by course and qualification type with those forecast in the operational plan and question any significant variances. Following the end of the academic year, officials discuss actual achievements against targets in the plan and against wider benchmarks. The three main performance measures are completion, attainment, and success rates (Box 8).

Box 8: Learner-outcome measures explained

Completion rate is the number of learners who go on to complete their full course, as a proportion of all learners enrolled on their course eight weeks after it starts ie excluding any early leavers.

Attainment rate is the number of learners that achieve the targeted qualification for their course, as a proportion of all learners completing their course.

Success rate is the number of learners that achieve the targeted qualification for their course, as a proportion of all learners enrolled on their course eight weeks after it starts (again excluding early leavers).

- 1.60 Officials also monitor learning activity drop-out rates for each course to ensure that they remain reasonably low. Early drop-outs, defined as students leaving within eight weeks of the start of their course, are excluded from this calculation and not counted when calculating funding entitlements or success rates (paragraph 1.22). The Welsh Government also collects data on early drop-out rates, which are relatively low, although these are not formally monitored and the Welsh Government is uncertain about actual figures due to concerns about data accuracy. A proposed new methodology for calculating performance aims to measure early drop-out at programme level, although improvements in data quality will be required to implement this.
- 1.61 The Welsh Government has monitored student satisfaction through the 'Learner Voice Wales' survey, which took place annually between 2013 and 2015 (paragraph 2.60). The full survey results, together with summaries for each college, are published on the Welsh Government's website. The Welsh Government also publishes annual learner-outcome reports for each college. The reports include:
- The overall completion, attainment and success rates at the college compared with the Wales average;
 - Success rates by subject area and course type (classified into four performance categories), compared with the Wales average; and
 - Contextual information on age and gender, ethnicity and deprivation level of the learner's domicile (the electoral ward in which they live) – to assess the profile of the college's learners.

- 1.62 The Welsh Government has made limited progress in developing reliable and comprehensive data on learner destinations – what happens to learners after they leave their courses in terms of progression to further education or employment and the impact on earnings. This outcome data is not currently collected, except to a limited extent for work-based learning programmes. Instead the Welsh Government relies on periodic surveys of former learners as part of project evaluations. It is difficult to collect destination data through surveys, as colleges do not have regular contact with learners once they have left the college.
- 1.63 The Welsh Government is reviewing its outcome measures²⁰ for further education to address the shortcomings of the current system. There are three main strands to the work:
- a **Learner achievement:** The success rate for further-education colleges counts only outcomes achieved within a single academic year and does not consider progression to the second year for two-year courses. Nor does it capture differences in grades or qualification points. In contrast, outcome measures for A-level qualifications delivered by school sixth forms do consider qualification points (linked to grades) but not learner retention. The Welsh Government is modelling new measures that will take account of learner retention and attainment, including grades where appropriate, for both sectors so that they can be assessed consistently. Officials plan to have the new measures in place for 2016/17.
 - b **Added value:** There is currently a measure of added value for pre-16 education but not post-16. Added value is a measure of the additional progress that learners have made beyond the level expected given their prior attainment and other factors such as gender, ethnicity and deprivation. The Welsh Government has contracted with consultants to develop a model to assess added value for post-16 qualifications, and aims to have the new measures in place for 2017/18.
 - c **Destinations:** the Welsh Government is working with the Department for Education and Department of Work and Pensions, which have agreed in principle that Wales should participate in the Longitudinal Education Outcomes Study. The study will match learner-outcome data from providers with PAYE records at HM Revenue and Customs, which show an individual's earnings and employment status, in order to track the impact of courses on learners. The Welsh Government expects to begin collecting destination data during 2017. In parallel, it is also establishing its own data linking programme to enable the calculation of learners' educational destinations.

²⁰ Welsh Government, **Consistent Measures for post-16 Learning in Wales**, Welsh Government Consultation Document, January 2017

- 1.64 Colleges assess the quality of their own courses. They are required to send a quality development plan to the Welsh Government each year as part of a comprehensive self-assessment report. This report is not assessed in detail by Welsh Government officials, who rely on Estyn to provide external oversight of course quality, academic performance, and leadership (Box 9).

Box 9: Estyn's inspection of the further-education sector explained

Estyn suspended full inspections in 2013 for two years while it reviewed the inspection system for the sector following changes in the Welsh Government's planning and funding framework and several college mergers. During the interim period, Estyn reviewed each college's self-assessment report and an inspector (known as a 'link inspector') maintained contact with the college and discussed progress regularly. The link inspector issued an annual letter to the college's governing body in 2014, in effect a concise report of their views on the college's progress based on these meetings and on a review of published data. Estyn continues to maintain contact with colleges through regular link inspector visits.

Estyn has recently begun a new period of inspections for all colleges from 2015 onwards. Inspections include an assessment of colleges' overall performance and quality of provision, a review of college leadership and management, and more detailed assessment of a sample of learning areas to assess their outcomes, quality of teaching and learning, and leadership.

- 1.65 The Welsh Government does not consolidate the available data and sources of information into a single set of performance indicators against which it measures and reports the sector's and individual colleges' performance. As autonomous bodies, each college determines its own key performance indicators (which always include the completion, attainment and success rates described in Box 8) and its governing body is responsible for setting performance objectives and monitoring achievement. The Welsh Government does not intervene in this process or set specific targets for the sector, confining itself to approval and monitoring of the operational plan and specific requirements for matters such as data collection. This position contrasts with that for higher education, where HEFCW sets a range of targets that apply to the sector as a whole and cover objectives such as widening access, quality of provision, employment of graduates, research, and increasing the number of part-time learners.
- 1.66 The Welsh Government recognises that it lacks an overall picture of each institution's performance and capability. Other parts of the UK have developed different approaches to assessing performance (Box 10). Officials trialled a process in 2015 that scored each college on its financial health, infrastructure, funding, curriculum planning and delivery, quality and data management, and general policy but decided that further work was needed before it could be launched as a robust performance framework.

Box 10: Performance monitoring of further education in Scotland and England

In **Scotland**, incorporated colleges are arm's-length central government bodies within the public sector ([Appendix 2](#)). The Scottish Funding Council evaluates the performance of college regions through outcome agreements which set out the contribution that each college region will make to the Scottish Government's strategic aims and national priorities for post-16 education. Outcome agreements cover a three-year period, and are refreshed annually and contain a range of performance indicators. The performance indicators cover such issues as financial health, volume of provision overall, and for priority groups, quality of learning (including qualifications and progression to higher levels) and employer engagement. The Scottish Funding Council reports on performance for the sector overall but not for individual colleges; and has in the past imposed financial penalties when agreed outcomes are not met.

Colleges in **England** have the same status as those in Wales and are overseen by the Skills Funding Agency, which uses a range of performance indicators to assess risk at individual colleges. The approach, involves three key financial risk indicators, four key quality risk indicators, and more than 20 other risk indicators covering matters such as contracting and sub-contracting, data quality, and apprenticeships. The Skills Funding Agency reports back to colleges on its assessment of their financial health, and formally flags concern with colleges when its analysis indicates that college performance has deteriorated below certain defined trigger points to prompt an 'inadequate' rating. At this point, it is able to attach additional conditions to its funding

The Welsh Government has helped the sector to develop its own leadership and governance training and standards, although there are differences in the approach to monitoring governance between the further and higher-education sectors

- 1.67 The **Financial Memorandum**, issued by the Welsh Government in 2014, provides clear guidance on accountability for the use of public funding while reflecting the autonomous status of colleges. In addition, the Welsh Government has issued an audit guide with detailed guidance on the appointment, responsibilities and management of a college's internal and external audit functions and the operation of its audit committee. External auditors are required to confirm that public funds have been applied in accordance with the Financial Memorandum. The Welsh Government also issues an accounts direction that specifies the format and disclosures of colleges' annual accounts. The accounts direction is intended to ensure robust and consistent accounting by colleges, but we noted some inconsistencies in the way that remuneration of senior staff was recorded in colleges' 2014/15 accounts.²¹

²¹ The National Assembly's Public Accounts Committee reported on senior management pay in the Welsh public sector (including further-education colleges, given the amount of public money they received) in November 2014. The Committee recommended more consistency in the reporting of senior management pay and suggested specific disclosures that should be made in annual reports and accounts. The Welsh Government accepted these recommendations, but we noted some inconsistencies in the reporting of senior management pay in colleges' published accounts for 2014/15.

- 1.68 The Welsh Government has supported the sector to develop its own governance training and standards by funding projects undertaken by ColegauCymru. The sector has developed its own code of governance (Box 11). ColegauCymru also provides short governance training sessions for members of governing bodies on an annual basis.

Box 11: Further-education code of governance explained

ColegauCymru published the 'Code of Good Governance for Colleges in Wales' in January 2016 with financial support from the Welsh Government. The Code was developed collaboratively with college leaders and student representatives to replace the more prescriptive and detailed guidance produced in 1999 by the Further Education Funding Council for Wales (FEFCW), with something considered more suitable for colleges' greater autonomy following the introduction of the Further and Higher Education (Governance and Information) (Wales) Act in 2014.

The Code sets out the core values of college governance and seven elements to which college leaders are committed:

- Strategy and leadership
- Collective accountability
- Financial strategy and audit
- Teaching and learning
- Responsiveness
- Equality and diversity
- Effective governance

The Code contains guidance for each of these elements, much of it principles-based, but also with specific requirements. These include the need to have an independent governing body with a non-executive chair, supported by a clerk; and for the governing body to approve a strategic plan, a financial strategy and appropriate financial controls and delegations of authority.

- 1.69 The Welsh Government views its role as setting basic standards for the sector in line with legislation, and ensuring value for money and proper use of any public funding that it provides to colleges. In 2009, the Welsh Government discontinued in-depth governance assessments as part of an efficiency drive. The Welsh Government considered that the risk of poor governance had greatly diminished, as the colleges had matured as institutions and were developing greater management capacity through the programme of mergers. Welsh Government officials now believe that it is inappropriate for them to assess governance standards in each college. The strong relationship between colleges and the Welsh Government also provides a degree of assurance that risks are monitored and managed appropriately.
- 1.70 Estyn assesses the leadership and governance at each college as part of its full inspection process. Estyn concluded that leadership and management were generally sound and robust quality-assurance processes were in place at the three colleges it inspected in 2015 and 2016. Estyn rated two colleges as 'excellent' on leadership and management and the other college as 'good'.
- 1.71 Welsh Government officials conduct an annual review of each college's audited annual report and accounts, and the annual reports by internal audit and the governing body's audit committee. No major concerns have arisen from these reviews in recent years. Officials undertake separate, more detailed reviews of specific concerns that come to their attention. In the last three years, there have been two such reviews covering a financial problem at one college and governance arrangements for a newly merged institution.
- 1.72 In addition, the Welsh Government funds initiatives which are intended to improve leadership and management more generally in the sector (**Figure 8**).
- 1.73 The Further Education Trust for Leadership has also funded a review of eight colleges to assess how well the sector was equipped to meet current and future challenges. The report, **Changing the Face of FE Leadership in Wales**, was commissioned by Coleg Gwent and published in March 2016. In terms of governance, the report found that colleges needed to:
- Diversify their boards and be more proactive in recruiting new board members;
 - Resolve some residual uncertainty about the roles of governors and managers; and
 - Provide leadership training in change management and commercial awareness.

Figure 8 – Recent leadership and management initiatives funded by the Welsh Government

Initiative	What is involved
Leading Wales	A programme of leadership and management training, known as 'Leading Wales' for up to 15 senior college managers a year. The programme is designed to increase the personal effectiveness of individual leaders as well as building capacity in the further-education sector as a whole, given that many college leaders are nearing retirement age and there has been a reduction in the number of managers taking posts in the Welsh sector from outside Wales. It is delivered by AoC Create, working in partnership with ColegauCymru, on behalf of the Welsh Government. The total value of the programme is £500,000 over five years.
FE Resilience programme	The Welsh Government now plans to help the sector improve its resilience by commissioning independent consultancy for colleges. This support will be tailored to the needs of each college, with a focus on leadership, financial sustainability and employer responsiveness. The consultants will report to each college with recommendations and provide follow-up support as appropriate. The project will also include training and guidance for the sector as a whole, based on the results of the reviews. The total value of the programme is £200,000 over two years. The Welsh Government has tendered for the consultants but decided to put the procurement process on hold while it reviews the scope of the project.

1.74 There are differences in the way oversight bodies approach the monitoring of governance in the further-education and higher-education sectors in Wales. HEFCW undertakes more detailed monitoring of governance and leadership at universities than the Welsh Government does of colleges, although the two sectors enjoy similar levels of autonomy (Box 12). We have not sought to compare the effectiveness or proportionality of the different approaches to monitoring governance. We highlight the issue as this has implications for any further steps towards greater co-ordination or integration across the two sectors as, for example, envisaged by the Hazelkorn review (paragraph 1.35).

Box 12: Higher Education Funding Council for Wales – institutional risk review of higher-education institutions

HEFCW draws on a wide range of documentary evidence to inform its annual risk review of each institution, including universities' internal management information, published financial statements, published statistics and reports from the Quality Assurance Agency on the quality of provision. The institutional risk review process assesses institutions' finances, governance and management, estates, research and knowledge transfer, student and quality issues, and strategic direction. Based on the totality of this work, HEFCW classifies each aspect as high, medium or low risk, and issues a formal report to each institution with a single overall risk rating. The confidential report of the overall risk rating outlines HEFCW's view of any issues that require attention and whether each aspect of governance is assessed as improving, stable or deteriorating.

Additionally, Council members and senior officers from HEFCW meet universities' governing bodies on a regular (three yearly) cycle to discuss key issues facing each institution. HEFCW believes that these meetings provide it with a valuable insight to the challenges faced by each institution and the sector as a whole, and the way in which each governing body exercises its scrutiny function. These meetings are supplemented by three-yearly Institutional Assurance Review visits, in which HEFCW officers review each institution's control environment, and other regular engagement with universities' senior management.

The Welsh Government is at an early stage in considering how the Well-being of Future Generations (Wales) Act 2015 will affect its direction, funding and oversight of further education

- 1.75 The Welsh Government has put in place the Well-being of Future Generations (Wales) Act 2015 as the latest step in embedding sustainable development in the public sector in Wales. The Act requires specified public bodies, including the Welsh Government, to set and publish objectives designed to maximise their contribution to the seven national wellbeing goals. They are also required to take all reasonable steps to meet those objectives. The Act identifies five ways of working which can support the wellbeing of future generations – integration, collaboration, long-term thinking, involvement and prevention (Figure 9).
- 1.76 The Welsh Government is bound by the Act but colleges are not. However, the Welsh Government provides the large majority of college funding, as well as policy guidance and direction, and therefore the Act should be a significant influence on the sector.

Figure 9 – The Well-being of Future Generations (Wales) Act 2015



Source: Welsh Government: Shared Purpose: Shared Future – Statutory guidance on the Well-being of Future Generations (Wales) Act 2015

- 1.77 Welsh Government officials responsible for further education acknowledge that their thinking about the Act is at an early stage, and they have not yet identified any changes they would wish to make to the direction, funding or oversight arrangements. Meeting the requirements of the Act will be a challenge for the Welsh Government. For example, the current focus on annual planning and budgeting and the absence of an overarching strategy could potentially be viewed as inconsistent with the Act's principles of long-term and integrated decision making.
- 1.78 In the meantime, all but one of the colleges are among 390 organisations across Wales that had signed up to the Welsh Government's Sustainable Development Charter (as at 31 March 2016). The Charter is a public, voluntary commitment by an organisation based in Wales to adopt sustainable development as its central organising principle and to embed sustainable development in its decision making and ways of working. Signing up to the Charter does not involve any specific commitments or require adherence to any formal procedures²².
- 1.79 ColegauCymru commissioned a research project in 2016 to assess the sector's current practice on sustainable development, consider the policy implications of the Well-being of Future Generations (Wales) Act and highlight how the further-education sector could contribute to the national well-being indicators.
- 1.80 The report²³ concluded that the sector was well positioned to build on existing strengths, and that some excellent practice existed where sustainability principles were integrated into specific management processes. However, the next step was to apply these principles to institutional planning. The report identified opportunities to use the Act as a framework for curriculum development, joint working with higher education, engagement with public-service boards, longer-term financial planning, workforce planning and leadership development.

²² Cynnal Cymru administered the network of signatories to the Charter on behalf of the Welsh Government. With the Well-being of Future Generations (Wales) Act 2015 now in force, the Welsh Government has indicated that the Charter is under review to make sure that it is aligned with that legislation.

²³ City and County of Swansea and Netherwood Sustainable Futures, **The Practical and Policy Implications of the Well-being of Future Generations Act on the FE sector in Wales**, ColegauCymru research report, January 2017.

Part 2

In response to reduced funding, colleges have cut part-time provision and costs, financial health varies across the sector and the impact on quality and outcomes is not yet clear



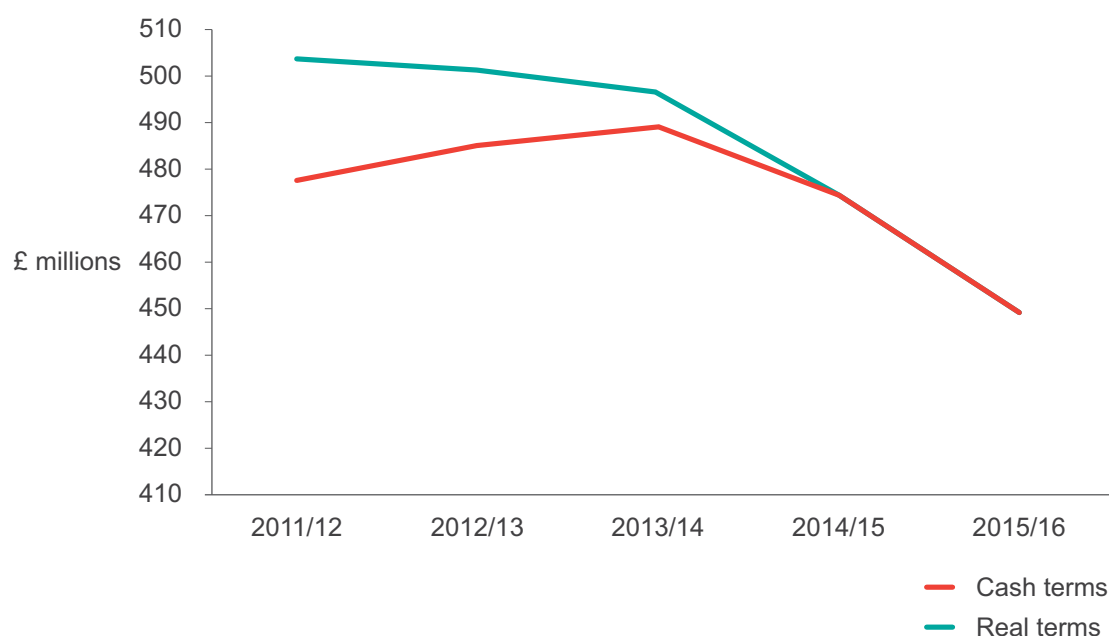
- 2.1 This part of the report examines the financial resilience of the further-education sector, the response to funding reductions and the impact of college mergers. In the context of funding reductions, it also considers evidence relating to the quality of provision and other outcomes.

While colleges are financially stable in the short term, their financial health varies, and colleges are concerned about rising costs and funding capital investment in the further-education estate

While colleges are financially stable in the short term, their financial health varies and rising pension deficits and contributions are a significant concern

- 2.2 The reductions in Welsh Government funding have driven a reduction in the further-education sector net income of 6.0% in cash terms, and 10.8% in real-terms, between 2011/12 and 2015/16 (Figure 10). Despite these financial pressures, the sector's finances are generally sound and in the short term colleges are in a stable financial position. Colleges have been able to cover reductions in income from savings in expenditure, although there has been some deterioration in financial performance as reflected in overall surpluses and deficits.

Figure 10 – Changes in total further-education sector net income between 2011/12 and 2015/16



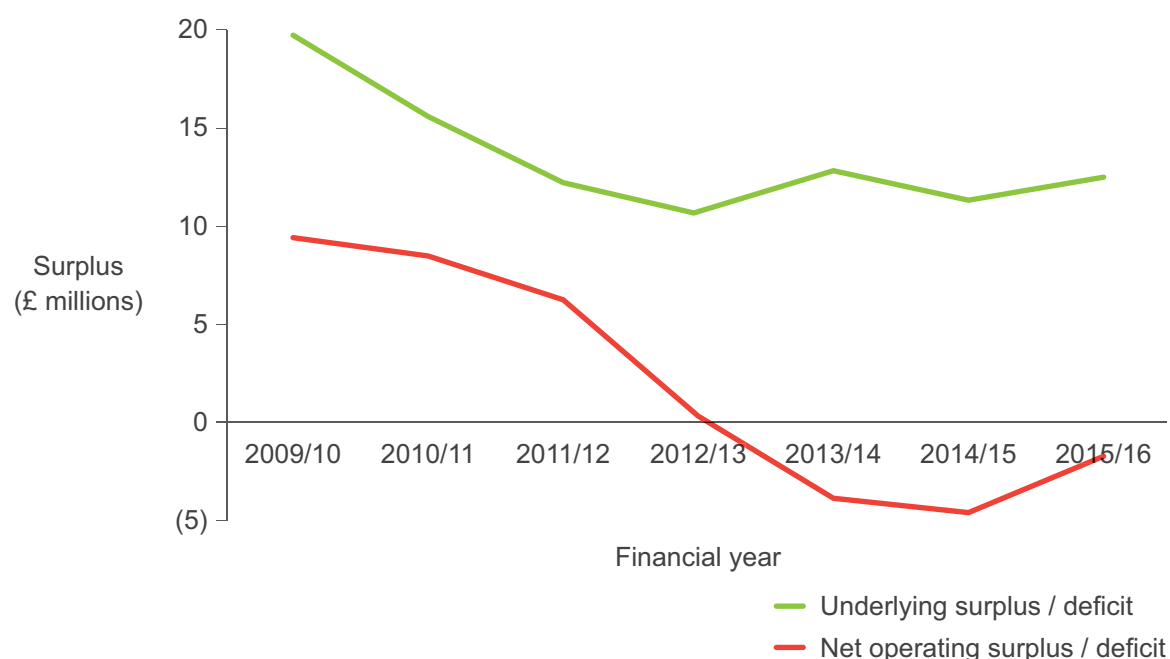
Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

- 2.3 The sector as a whole reported an operating deficit²⁴ of £3.7 million in 2013/14 and £4.5 million in 2014/15, compared with operating surpluses in the four preceding years (Figure 11). The sector reported a small improvement to a £1.7 million operating deficit for 2015/16, against a forecast of a £1.9 million surplus in their March 2016 financial returns. However, the figures for 2015/16 exclude the impact of an actuarial valuation of the Local Government Pension Scheme carried out in September 2016, which has resulted in a very large increase in pension deficits and an £89 million charge to the accounts, leading to an overall deficit for the year of £91 million (paragraph 2.10).
- 2.4 The operating surplus or deficit varies considerably from year to year, in part because restructuring costs (mainly for staff redundancies) and pension charges are unpredictable and liable to fluctuate. There is a more positive position on the sector's underlying surplus (excluding restructuring costs and changes in pension deficits), with a surplus of £12.9 million in 2013/14 and £11.5 million in 2014/15, broadly in line with the previous two years. The sector reported an underlying surplus of £12.5 million in 2015/16, indicating that colleges have mostly covered the reduction in Welsh Government funding through cutting costs or increasing revenues in other areas.
- 2.5 The Welsh Government does not set financial targets for colleges, which are the responsibility of governing bodies. An operating surplus of 3-5% each year would generate cash reserves to support future investment. However, taking the five years to July 2016 as a whole, the sector did not generate an operating surplus while underlying surpluses averaged 2.5% of income over the period.²⁵

²⁴ In this report, the term operating surplus or deficit refers to the surplus/deficit calculated as income less all expenditure except for corporation tax and gains or losses on the disposal of fixed assets (including investments).

²⁵ Capital expenditure is not included directly in the calculation of the operating surplus/deficit. Capital expenditure is spread across the lifetime of the assets funded and charged against the operating surplus as depreciation.

Figure 11 – Further-education sector surpluses and deficits, 2009/10 to 2015/16



Note: Due to change in accounting policies, operating surplus is calculated differently in 2015/16 than in previous years.

Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

2.6 Operating surpluses and deficits vary considerably between colleges (Figure 12). Nine colleges posted surpluses (after restructuring and pension deficit charges) in both 2013/14 and 2014/15, with three colleges moving from surplus to deficit and three from deficit to surplus. Half the colleges reported an improved position for 2015/16, with eight in surplus, three moving from surplus to deficit and two from deficit to surplus. As a percentage of turnover, Coleg Ceredigion and Cardiff and Vale College had the highest deficits in 2014/15, at 10% and 8% respectively. In the case of Cardiff and Vale, this was due to exceptional redundancy costs and an impairment charge on disposal of a property, and the operating deficit fell to 4% in 2015/16. For Coleg Ceredigion, a combination of funding reductions and cost increases that could not be contained in the short term caused a large increase in the deficit. This trend continued in 2015/16, with a 9% operating deficit, although an improvement to 3% had been forecast, and cash balances have fallen significantly.

Figure 12 – Operating and underlying surpluses and deficits of individual colleges as a percentage of total income, 2014/15 and 2015/16

College	2014/15 surplus / (deficit) as % of total income		2015/16 surplus/ (deficit) ¹ as % of total income	
	Operating	Underlying	Operating	Underlying
Bridgend College	0.2	6.4	1.4	4.0
Coleg Cambria	0.8	6.8	3.1	7.2
Cardiff and Vale College	(7.5)	(3.6)	(4.2)	(0.9)
Coleg Ceredigion	(9.7)	(7.4)	(8.7)	(6.1)
Coleg y Cymoedd	(3.2)	0.0	(3.8)	0.6
Gower College Swansea	0.4	2.7	0.3	3.4
Coleg Gwent	0.2	3.9	2.7	6.7
Grŵp Llandrillo Menai	2.0	2.9	(3.7)	(0.4)
Merthyr Tydfil	2.1	3.9	1.3	3.3
NPTC Group of Colleges	(1.1)	2.0	0.9	2.0
Pembrokeshire College	0.3	2.8	0.1	2.1
Coleg Sir Gâr	(5.0)	(0.6)	3.2	5.3
St David's Catholic College	1.3	3.3	(0.9)	0.9
WEA Cymru ²	2.4	2.3	(7.1)	(0.7)
YMCA ²	(3.7)	(3.7)		
Total³	(1.0)	2.4	(0.4)	2.8

Notes:

1 Due to change in accounting policies, operating surplus is calculated differently in 2015/16 than in previous years.

2 WEA Cymru and YMCA merged to become WEA YMCA Community College Cymru on 1 August 2015 (renamed Adult Learning Wales on 5 November 2016).

3 Totals are for the sector as a whole and include consolidation adjustments to remove the effect of transactions between colleges.

Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

- 2.7 Colleges have improved their liquidity (ability to pay debts as they fall due). The current ratio²⁶ for the sector as a whole was 2.28 at the end of 2014/15 and fell slightly to 2.03 at the end of 2015/16. Cash balances at most colleges are easily sufficient to meet current needs, but they do vary considerably between colleges. At the end of 2015/16, cash and short-term investments (which can easily be turned into cash) ranged from 25 days of total expenditure at Coleg Ceredigion to 124 days at Coleg y Cymoedd ([Appendix 4](#)). Ten colleges reported an improved position in 2015/16 compared with the previous year, and the sector average improved from 70 days to 75 days.
- 2.8 General reserves²⁷ (before deducting the pension deficit) remain relatively healthy with colleges holding reserves covering 46% of total expenditure in 2014/15, improving to 50% in 2015/16. Five colleges had notably lower reserve levels of between 22% and 31% of total expenditure.
- 2.9 Like many other employers, the sector faces a significant deficit on its funded defined benefit pension schemes. Most academic staff are enrolled in the Teachers' Pension Scheme and most administrative staff in the Local Government Pension Scheme ([Box 13](#)).

Box 13: Pension schemes explained

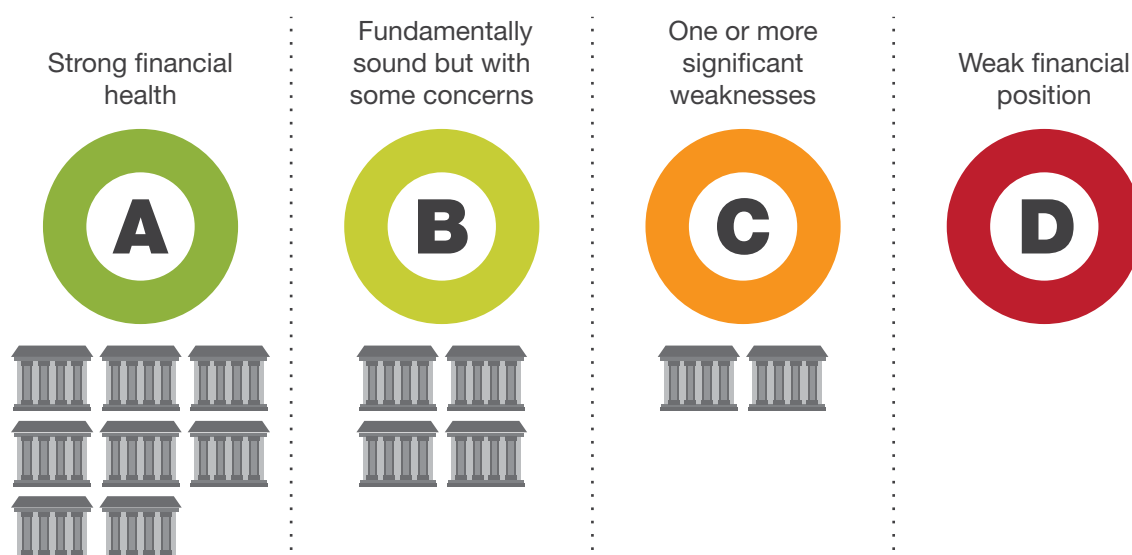
The Local Government Pension Scheme is a funded scheme whereby contributions are invested with a view to maintaining a fund of sufficient value to pay all pensions from investment returns as they fall due. The scheme is regularly valued by actuaries who calculate the difference between the actual value of the scheme (based on the market value of investments in the fund) and the value required to meet the scheme's obligations (based on assumptions about life expectancy, pay increases and investment returns). Any shortfall in the value of the fund (the deficit) must be disclosed in the accounts of the bodies subject to the scheme, but changes in the value of the deficit do not affect the income and expenditure account unless employers' cash contributions to the scheme are changed as part of a long-term plan to close the deficit. Further-education staff represent a small proportion of the total number of scheme members and the sector therefore has little influence over key aspects of the scheme, such as the level of contributions and benefits.

The Teachers' Pension Scheme is unfunded and all pensions are funded by contributions paid annually by employees and employers rather than investment returns. Consequently there is no fund to be valued and colleges do not need to account for any surplus or deficit.

²⁶ The current ratio is a liquidity measure that is calculated as current assets (cash, debtors and stocks – which can be turned into cash relatively quickly) divided by current liabilities (amounts payable within one year). A ratio greater than one means that current assets exceed current liabilities and the organisation is therefore able to meet its financial obligations as they fall due, provided that a sufficient proportion of current assets is in cash at any one time.

²⁷ Excluding revaluation reserves, which reflect increases in the value of property rather than surpluses accumulated from colleges' normal operations.

- 2.10 In 2015/16, the total pension deficit was £266 million, an increase of £103 million on the previous year, following an actuarial valuation of the Local Government Pension Scheme in 2016. The increase in the deficit reflects a mandatory change in accounting policy which requires future pension liabilities to be stated in colleges' accounts on the basis of the fund being invested in low-risk, low-return investments, whereas higher growth investments are typically used by the Local Government Pension Scheme. In addition, risk-free investment returns fell significantly in 2016, creating a further increase in liabilities.
- 2.11 Employers' pension contributions will increase from April 2017 to fund the increase in liabilities arising from the reduction in risk-free returns. The scale of the increase varies by college, but represents a significant cost pressure for all colleges. A pension deficit is sustainable in the short term because the liabilities will become payable over a long period, but the scale of the deficit has the effect of significantly diminishing colleges' total reserves – from 38% of total expenditure in July 2015 to 11% of total expenditure in July 2016, with three colleges having negative reserves. This situation potentially makes it difficult for colleges with low or negative reserves to raise private finance for capital investment as they may not be able to offer lenders adequate security for loans.
- 2.12 The Welsh Government's assessment of the overall financial health of each college, as at April 2016, showed most colleges to be in strong or sound financial health:



These categories are due to be updated in February 2017 to reflect the position apparent from 2015/16 audited accounts, which were submitted to the Welsh Government around the end of 2016.

- 2.13 Colleges tended to be classified as category B due to operating deficits and/or relatively low cash-backed reserves. Two colleges were classified as category C primarily because of concerns about their cash position or the size of their operating deficits. Welsh Government officials were confident that one of the category C colleges was likely to rise to a category B.

The condition of the further-education estate varies considerably and colleges see capital investment as a key business risk

- 2.14 A recent update to a survey undertaken in 2009 found that the majority of the estate was in a satisfactory or good condition with around 29% of floor space being in a poor or bad condition, and 14% classified as being between satisfactory or poor (**Figure 13**). Similar survey data for schools shows that around 53% of secondary schools are in a poor or bad condition. The total cost of restoring and maintaining the further-education estate was assessed by colleges at £192 million. This cost varied very widely from nil at Merthyr Tydfil (where all property is relatively new and in good condition) to £447,000 at Bridgend College and £67 million at Coleg Gwent.

Figure 13 – The condition of the further-education estate, as reported by colleges

Category	Area (square metres)	% of total area	Cost to maintain or restore (£000)	% of total cost
Good	119,082	17	1,312	1
Good or satisfactory	10,665	1	0	0
Satisfactory	250,981	35	12,504	7
Satisfactory or poor	96,283	14	17,797	9
Poor	148,987	21	103,501	54
Poor or bad	39,321	5	37,234	19
Bad	17,954	3	15,434	8
Unclassified	28,923	4	4,428	2
Total	712,196	100	192,209	100

Notes:

- 1 Condition was self-assessed by colleges in 2016 to update the results of an external survey undertaken by professional surveyors in 2009. The colleges' returns are being validated on a sample basis (10% of buildings) by surveyors commissioned by the Welsh Government. The estimated costs of maintenance and restoration will also be covered by the validation exercise, and there may be inconsistencies in the way that colleges have prepared cost estimates.
- 2 Condition is classified for each building as follows:
 - A Good: performing as intended and operating efficiently
 - B Satisfactory: performing as intended but exhibiting minor deterioration
 - C Poor: exhibiting major defects and/or not operating as intended
 - D Bad: life expired and/or serious risk of imminent failure
- 3 Many colleges have classified part of their property into more than one category, as shown above, to reflect varying conditions within a particular building. Note that 'Between satisfactory and poor' includes a small amount of space classified in both the 'satisfactory' and 'poor' categories.
- 4 Some space is not classified at all, mainly outdoor areas like car parks.
- 5 Area is the gross internal floor area.

Source: Estate condition returns submitted by colleges to the Welsh Government in 2016

- 2.15 Colleges usually require external funding for major capital projects, either from the Welsh Government in the form of grants or from commercial borrowing. The proportion of the sector's capital expenditure financed by Welsh Government grants has tended to decline in recent years, from an average of 64% in the two years to 31 July 2011 to 29% in the subsequent five-year period, making colleges more reliant on their reserves and on commercial borrowing to finance their plans. Nevertheless, the Welsh Government does support several major projects through the 21st Century Schools and Education Programme, including:
- Cardiff and Vale College: new campus at Dumballs Road, central Cardiff, completed in 2015 at a cost of £44 million with a Welsh Government grant of £20 million;
 - Coleg y Cymoedd: a new campus at Aberdare costing £22 million with a Welsh Government grant of £11 million; and
 - Coleg Cambria: a new campus costing £8.25 million with a Welsh Government grant of £4.12 million.
- 2.16 Colleges will also benefit from the next round of the 21st Century Schools and Education Programme, but the scale and nature of the funding are uncertain at present, and most of the colleges we visited highlighted capital investment as one of the most important risks facing their business. They were concerned that capital funding from the Welsh Government (paragraphs 1.14 to 1.17) was insufficient to restore the estate to a good condition, and revenue funding generally was insufficient to maintain the estate. Some colleges reported that they were reducing their reserves to fund essential maintenance and routine asset replacement, or to fund minor works that were needed to make their premises accessible for people with disabilities.
- 2.17 Colleges' ability to fund capital expenditure from other sources is constrained by static or falling reserves and general financial constraints which make it more difficult to borrow commercially in order to finance major projects. Some colleges have secured significant commercial investment (notably Cardiff and Vale College, which borrowed £20 million to help fund the construction of its city-centre campus) while some colleges own land and property that could be sold to help finance redevelopment. Many colleges, however, are concerned that borrowing to renew the estate would overstretch them in a period of core-funding reductions. The cost of servicing loans would not be met by increased income from rising student numbers. The position is compounded by uncertainty about future funding settlements. Such considerations might also deter commercial investors from lending.

- 2.18 We have not examined the detail of colleges' capital investment plans or asset management arrangements as part of this review. In response to the Welsh Government's release of capital funding in 2016, the colleges we visited commented on the short timescales involved and that this did not allow for a more considered assessment of needs and better-quality proposals to be submitted. This indicates that colleges could possibly strengthen their capital planning and asset management so that, in the event of capital funds becoming available, they are better placed to respond.

Financial management is generally sound but colleges believe they will be unable to continue to protect 16 to 19 year olds if further cuts are made, progress in developing non-grant income is variable, and medium-term financial planning is not well developed

The sector has regular reporting and a reasonable quality of financial information but medium-term financial planning is not well developed

- 2.19 Financial management is generally sound with regular reporting and a reasonable quality of financial information. The quality of colleges' short-term forecasting is generally good, with most colleges reporting total income and expenditure in 2014/15 at or close to the figures projected at the start of the year. Three colleges reported that shortfalls against their projections were due to timing differences in the award or payment of European Social Fund grants, which came in later than they expected, and which had a significant financial impact on one of these colleges.
- 2.20 Colleges appear to have the necessary capacity and skills to manage finances, although some smaller colleges expressed concern to us that their finance departments were becoming stretched and could not be reduced further without a move to shared services with other colleges or other organisations.

- 2.21 Most of the colleges we visited had made limited progress towards the kind of comprehensive medium-term planning outlined in **Box 14**. A common view from colleges is that the Welsh Government's annual funding allocations, and the uncertainty of other funding streams, make medium-term financial planning very difficult. Colleges were reluctant to forecast more than a year ahead without the Welsh Government providing indicative financial allocations or specific guidance on the revenue assumptions they should adopt. In their most recent forecasts for the Welsh Government, colleges have assumed that core grants will remain stable. While we acknowledge the uncertainties faced by colleges, these are not unique to the sector and medium-term planning is adopted across many public-sector bodies.

Box 14: Medium-term financial planning

The Auditor General recently reported on the financial resilience of local authorities²⁸ and found that the majority of authorities:

- Model key expenditure drivers (for example, population changes and demand for services), sources of income (for example, income and government grant forecasts), revenue consequences of capital and resource requirements and the use of balances; and
- Modelling is based on reasonable predictions and assumptions around inflation, income levels, demographics, future demand for services and the costs of delivering services.

The Auditor General's report on Natural Resources Wales²⁹ established that future budget reductions, in-year cuts in core funding and further financial pressures were increasing the risks of reductions in services and of Natural Resources Wales failing to achieve its outcomes. But that Natural Resources Wales models a range of budget scenarios to plan for these fluctuations in budgets.

- 2.22 While the sector faces a number of uncertainties, it is likely to face a continuing period of financial constraint in the current period of austerity and colleges should still be able to plan for the potential impact of funding cuts, by modelling on a range of assumptions. This would provide an indication of the medium-term financial resilience for both individual colleges and the sector.

²⁸ Auditor General for Wales, Financial resilience of local authorities in Wales 2015-16, August 2016

²⁹ Auditor General for Wales, The development of Natural Resources Wales, February 2016

Colleges have responded effectively to smaller funding settlements by cutting costs and changing course delivery, but believe they have limited scope to make further savings without cutting provision for groups that have been protected to date

- 2.23 Over recent years, colleges have planned and delivered substantial savings mainly through reducing staff costs. In addition, savings have been delivered by reducing the cost of back-office or support services and through procurement savings. Most colleges use purchasing consortia (including the National Procurement Service) and some colleges are now sharing procurement services with their local authority (Pembrokeshire College) or within their merged organisation (Coleg Ceredigion and Coleg Sir Gâr), which have helped to deliver savings. The scale of savings from such initiatives has been relatively modest, and the opportunity for procurement savings is limited by having a relatively low proportion of discretionary spending in the sector. The Auditor General is currently undertaking a review of the procurement landscape in Wales, which will cover the further-education sector.
- 2.24 Reductions in the cost base are mainly permanent but have had to be planned on a short-term basis due to funding horizons. This carries some risks, for example, the potential need to re-recruit staff in the future. Colleges have also changed the nature of course delivery. Several colleges have reduced teaching hours, although the scope for further reductions is limited by the minimum tuition times required by accreditation bodies. Most colleges are also developing e-learning materials to complement traditional teaching methods. Most colleges were developing e-learning materials independently although some were working with colleges outside Wales. The development of blended learning materials (which incorporates e-learning as part of a balanced portfolio of teaching methods) might offer a good opportunity for joint working, given the scale of initial investment needed to develop good-quality materials. As part of the Creative Solutions programme, the sector has proposed several measures to promote the development of blended learning materials, including financial support from the Welsh Government. Officials have agreed to hold further discussions to explore aggregated loans, staff training and encouraging innovation through quality and inspection regimes.
- 2.25 Some colleges told us that the funding reductions, while difficult to deal with, had also had beneficial effects. For example, Grŵp Llandrillo Menai had undertaken a major curriculum review that it believed had helped the college to focus much more on the effectiveness of courses it offered and the value to learners. The funding constraints have also prompted a more commercial approach towards part-time provision in particular, and the college was now satisfied that it had the right level of provision, focussed in the right areas.

- 2.26 Upward pressure on costs has partly offset some of the saving gains. Most notably increases in National Insurance and employer's pension contributions, and contractual entitlements under the Common Employment Contract ([Box 15](#)).

Box 15: Upward pressure on costs explained

The abolition of the contracted out rebate in April 2016 has increased employers' National Insurance contributions by 3.4 percentage points. Employers' contributions to the Teachers' Pension Scheme and the Local Government Pension Scheme have also increased considerably in recent years to help meet the rising cost of pension provision.

All colleges are bound by the common employment contract negotiated between the trade unions and ColegauCymru, which has harmonised staff terms and conditions across the sector. The contract came into force on 1 September 2016 and applies a common pay scale to all staff. Each pay scale has a number of incremental points, and staff move up one increment each year until they reach the maximum for their grade. The cost of these contractual increments is additional to the cost of annual increases in the value of each pay scale, and in itself is a significant upward pressure on costs.

Colleges estimate that the overall impact of these changes have added around 5% of total pay expenditure to their cost base. The sector expects continuing cost pressures from rising pension costs and from the common employment contract. Colleges are likely to face additional increases in employers' contributions for the Local Government Pension Scheme from April 2017 ([paragraph 2.11](#)). Colleges also face rising costs as a result of the UK Government's Apprenticeship Levy, which will be payable by colleges from April 2017.

- 2.27 There was a consensus among all colleges we visited that any further cuts to funding would require cuts to full-time provision for 16-19 year-olds, the age group which the Welsh Government has sought to protect. This is because most part-time provision has already been cut and colleges consider that the readily obtainable efficiency savings have already been made. Colleges highlighted a range of potential actions that they would need to take to respond to further funding cuts, such as further consolidation of provision at fewer locations in rural areas, withdrawing or reducing subsidised transport, and scaling back the range of courses offered.

Expenditure cuts have resulted in large reductions in the workforce and with many remaining staff having wider or different responsibilities

- 2.28 Staff costs are the main category of expenditure for colleges, accounting for around 65% of total expenditure. Colleges have needed to reduce staff numbers to manage within reduced budgets. Most colleges have undertaken voluntary redundancy programmes, particularly in 2013/14 and 2014/15. Some colleges also transferred staff (on a voluntary basis) from full-time to part-time posts.
- 2.29 Staff numbers fell from a peak of 9,332 full-time equivalent posts in 2012/13 to 7,756 in 2015/16, a decline of 16.9%. The greatest reductions have been in teaching and learning support (37%), catering and residences (36%) and administration and central services (29%), with teaching staff cut by around 12% (Figure 14).

Figure 14 – Staff changes by category at all colleges, 2012/13 to 2015/16

Category	FTE posts in 2012/13	FTE posts in 2015/16	Change as % of 2012/13
Teaching	5,418	4,794	(11.5)
Teaching and learning support	1,150	722	(37.2)
Other support services	383	423	10.5
Administration and central services	1,343	960	(28.5)
Premises	338	288	(14.9)
Catering and residence	173	110	(36.3)
Income generating activities	445	379	(14.8)
Other	83	80	(4.0)
Total	9,332	7,756	(16.9)

Note: FTE = full-time equivalent posts. The total number of staff will be higher because some staff work part time.

Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

- 2.30 Colleges have also reduced tuition time and combined some managerial and teaching posts. During our fieldwork visits, college leaders acknowledged that these changes had resulted in a loss of highly experienced staff, with the remaining staff often having increased responsibilities and workloads. This came at a time when the profession was having to deal with changes to working practices arising from policy reforms, such as the greater emphasis on teaching literacy and numeracy in vocational courses. Colleges indicated to us that severance programmes had facilitated the departure of some staff who were uncomfortable with these changes.
- 2.31 We consulted the trade unions representing staff in the sector to establish their views about the impact of funding reductions and industrial relations generally. The two trade unions that responded (Association of Teachers and Lecturers and the University and College Union) expressed concern about the loss of experienced staff and the resulting increases in workload for remaining staff, which they felt had placed management grade staff in particular under severe pressure. They were also concerned about increased job insecurity and a lack of career progression. The unions did not attribute these problems to college managers, but to the financial constraints on the sector.
- 2.32 Both unions believed that industrial relations were generally good for the sector as a whole, with constructive dialogue on important issues and an effective all-Wales forum to negotiate on terms and conditions. They welcomed the introduction of the common employment contract, subject to the swift implementation of outstanding agreements such as time off in lieu for managerial staff. The unions believed that the national approach to terms and conditions in Wales, coupled with a constructive working relationship, had helped avoid industrial disputes. The unions reported to us that relations with individual colleges were more mixed, although generally favourable.

Colleges have made variable progress in developing non-grant income, with some better placed than others to increase commercial income and borrowing

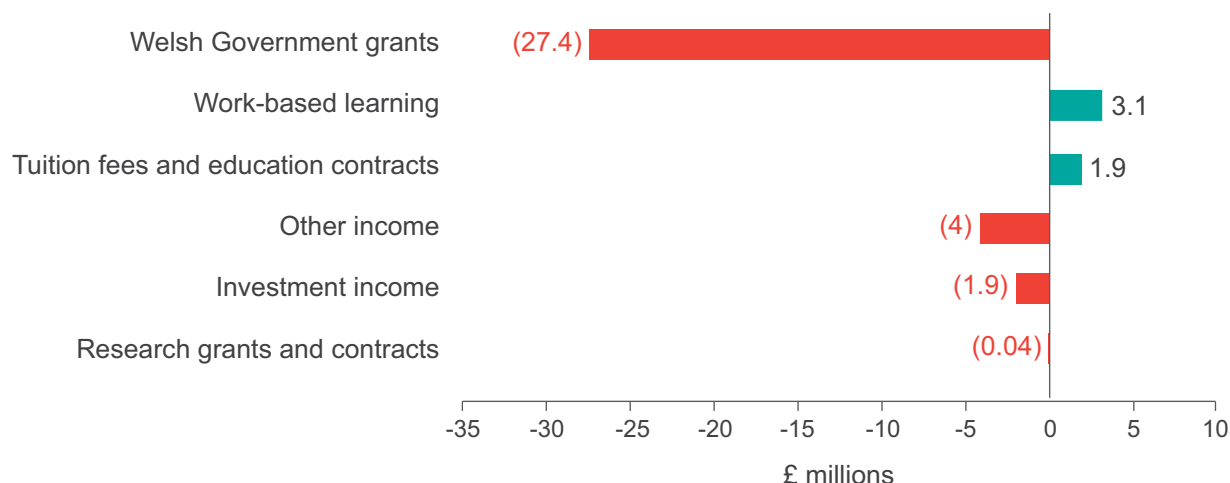
2.33 In response to the reduction in core Welsh Government funding, colleges are seeking to increase other income sources. Three are the main sources of non-grant income, each accounting for between 8% and 12% of the sector's gross income in 2015/16:

- Work-based learning contracts funded by the Welsh Government;
- Tuition fees and education contracts; and
- Other income streams such as contracts that colleges have secured on a competitive basis, and income from colleges' own operations, such as catering, conferences and residential venues, and farms.

Income from contracts secured on a competitive basis often comes from public-sector bodies, and although colleges do not separately report income from private-sector training contracts to the Welsh Government, they informed us that such income is relatively low at present.

2.34 To date, the decline in Welsh Government grant funding has not been matched by an increase in the other sources of income as a whole (Figure 15). Income from other public-sector bodies has come under pressure as budgets have been cut, for example, for training and education contracts or transport subsidies.

Figure 15 – Change in sources of income between 2011/12 and 2015/16



Note: 'Welsh Government grants' include work-based learning contracts, net of sub-contracting between colleges. 'Other income streams' includes contracts that colleges have secured on a competitive basis, and income from colleges' own operations, such as catering, conferences and residential venues, and farms.

Source: Wales Audit Office analysis of financial returns from colleges to the Welsh Government

- 2.35 The colleges that we visited were concerned about the reduction in funding and the longer-term outlook for the sector, and thought that the Welsh Government had protected funding for schools whilst funding for further education was unprotected and had, they felt, been targeted for savings in recent years. However, some areas of further-education funding have been protected, and it is only part-time provision and ring-fenced funding that have been subject to cuts.
- 2.36 **Work-based learning contracts**, funded by the Welsh Government, have been protected from cuts and the Government has a policy of expanding apprenticeship numbers ([paragraph 1.9](#)). Colleges work in consortia with each other and private-sector providers to bid for work-based learning contracts from the Welsh Government, and this provides a potential source of income growth. Six of the 19 lead contractors in Wales are colleges (Coleg Cambria, Cardiff and Vale College, Grŵp Llandrillo Menai, Gower College Swansea, NPTC Group of Colleges and Pembrokeshire College).
- 2.37 The proportion of the available work-based learning funds secured by colleges increased from 36% in 2011/12 to 40% in 2016/17³⁰. This resulted in an increase of 19% (cash terms) in the amount of funding secured for work-based learning over the period. Net income (after paying subcontractors) increased by £1.2 million or 4% between 2011/12 and 2015/16.
- 2.38 Work-based learning net income (after paying sub-contractors) as a proportion of total income varies across colleges, from 3.0% to 12.8%, with an average of 7.6%. There is also significant annual variation at college level, with some colleges expecting to increase their income significantly in 2015/16 while others have seen declines in the value of contracts secured. The Welsh Government currently receives around £25 million of European funding each year towards the cost of work-based learning contracts so the sector is exposed to any reduction in this funding following the UK's decision to leave the European Union. The Welsh Government also benefits from EU funding for several other skills-related projects, some of which will feed through to colleges.
- 2.39 The UK Government's announcement of a mandatory apprenticeship levy on employers, to apply from April 2017, also has the potential to increase revenues for the sector by encouraging increased investment in training by employers. However, the scale of the opportunity is unclear at this early stage. In addition, colleges themselves will be subject to paying the levy.

³⁰ Excluding the effect of Cardiff and Vale College's purchase of ACT, the largest work-based learning provider in Wales, which increases the proportion to 58% in 2016/17.

- 2.40 Some colleges have sought to increase **tuition fees**, but the scope to raise significant revenue is limited by the inability or unwillingness of potential learners to pay the full cost of their tuition. Across the sector tuition fee and education contract income increased by £1.9 million or 3.9% between 2011/12 and 2015/16, with an £8.2 million increase in higher-education income offsetting a reduction of £6.3 million in other tuition fees and contracts. Higher-education fees (which are typically much higher than those for further-education courses), together with contracts secured from universities to supply higher-education courses, account for a significant proportion of income at some colleges (**Box 16**). The Welsh Government aims to expand level 4 and 5 provision in further education, and this could provide a potential source of increased funding for the sector.

Box 16: Colleges providing higher-education courses

Four colleges (Bridgend, Coleg Sir Gâr, Grŵp Llandrillo Menai and Merthyr Tydfil) obtained 10% or more of their total income from higher-education courses in 2015/16, compared with an average of 6.2% for the sector as a whole. Coleg Sir Gâr and Merthyr Tydfil College have been aided by merging with universities in their vicinity, while Bridgend College has developed a strong position through the successful growth of its franchised provision with both the University of South Wales and Cardiff Metropolitan University.

- 2.41 Colleges also generate income from a range of **other sources**, such as European Social Fund grants and a variety of commercial activities. The total income from these other sources has reduced by £4.7 million or 9.6% between 2011/12 and 2015/16.
- 2.42 Colleges work with each other and with higher-education institutions to bid for European Social Fund grants, which are typically awarded to collaborative projects. This European Union funding for training and education has provided a considerable revenue stream for many colleges. Income fell from £9.5 million in 2013/14 to £4.8 million in 2015/16, but is expected to rise to £11.6 million in 2016/17 and remain at around that level until 2020. The UK's forthcoming withdrawal from the European Union will bring an end to this funding stream, although the UK Government has committed to guarantee funds for all projects approved before the date of the UK's withdrawal. The Welsh Government has stated that it will be seeking to secure replacement funding from the UK so that regional economic development goals can continue to be pursued after the UK leaves the EU, but the scope and amount of any replacement funding are inevitably uncertain at this stage.

- 2.43 All the colleges we visited were keen to generate more commercial income from the private sector. However, the number of learning programmes funded by employers or learners themselves decreased between 2012/13 and 2014/15, falling from 21% to 15% of total learners, indicating that, overall, colleges have not been successful in replacing publicly funded with privately funded provision. Nonetheless, the sector as a whole is making progress in developing new commercial income streams. The amount of income from 'other income generating activities' grew by £2.9 million to £19.5 million in 2015/16 from the previous year, double the £9.5 million recorded in 2011/12.
- 2.44 Several colleges have recruited dedicated staff to develop commercial income (Box 17), usually through wholly owned private companies to conduct their business operations, since these entities could recruit staff on more flexible terms and at a lower cost than the college itself.

Box 17: Commercial revenue case studies

NPTC Group of Colleges – has made considerable progress through its acquisition of income-generating businesses such as a language school, and by targeting international students. The Group started this work in 2010 with the acquisition of Language Specialists International Ltd (LSI) and has therefore made greater progress than other colleges in Wales. LSI runs a language school in Portsmouth and posted net profits of £415,000 in 2013/14 and £737,000 in 2014/15. The company has made donations to the college totalling £3 million between 2010/11 and 2014/15. The level of donations has varied over the period, but the college believes that there are good prospects for growth by establishing an overseas language school and to expand courses in executive English. The college has more recently acquired three other businesses, one of which was profitable in 2014/15, and the College's external business interests have contributed £592,000 to its reserves in 2014/15.

Cardiff and Vale College – has stepped up its efforts more recently, establishing a team with sales and commercial development experience to exploit new opportunities presented by the relatively buoyant local economy. The College has established partnerships with several employers in the area and is exploiting opportunities presented by its new campus in central Cardiff for retail operations and venue hire. The college has a target of raising commercial income from £3.4 million in 2014/15 to £8.6 million in 2016/17, and secured £6.3 million of commercial income in 2015/16 against a target of £5.4 million.

2.45 Progress in generating commercial income elsewhere in Wales has been mixed. Most colleges obtain some income from employer-funded health and safety courses, for example. However, most colleges have found it more difficult to develop long-term specialist provision for employers, which is likely to be more lucrative, secure, and less susceptible to price competition. Such provision is largely dependent on the presence of large employers with specialist training needs, but such firms are in short supply in most of rural Wales. For example, Grŵp Llandrillo Menai is developing collaborations with the major firms involved in the Horizon Nuclear project in Anglesey, but has few opportunities elsewhere in its mostly rural catchment area. Coleg Ceredigion likewise reported that it was difficult to develop commercial income in its geographical area, where public-sector employers and smaller businesses dominate. Some large firms had also cut back on training contracts with colleges. More generally, colleges noted that many employers were reluctant to co-invest in developing their employees' skills (paragraph 1.11), especially small companies and those in West Wales and the Valleys which had benefited from extensive subsidised provision for many years.

Mergers were intended to ensure financial resilience and quality of provision, and while there has been limited formal evaluation there is some evidence that these benefits have been realised

- 2.46 Between September 2008 and August 2015 the number of colleges in Wales was reduced from 25 to 14 through a series of mergers (Appendix 3). These mergers were driven by strategic considerations and in particular ensuring financial resilience and quality of provision.
- 2.47 The Welsh Government has not systematically evaluated the benefits arising from the mergers and, with the exception of Coleg Sir Gâr, nor have individual colleges. Generally, we found that when reporting benefits, colleges had not quantified these in financial or other terms. Nevertheless, there is some evidence that the mergers have met the strategic objectives.
- 2.48 The mergers have led to fewer, larger colleges, which has helped to strengthen the financial resilience of the sector by reducing the vulnerability of smaller colleges to financial pressures (a profile of each college can be found in Appendix 4). Improved financial resilience is evident in the overall profile of the financial health ratings attributed to colleges by the Welsh Government over time. The effect was particularly pronounced for smaller, financially weak colleges merging with a larger and financially stronger institution.

- 2.49 However, Coleg Ceredigion is facing particular financial challenges due in part to being by far the smallest main college. Coleg Ceredigion and Coleg Sir Gâr currently remain separate and financially independent institutions although they have both merged into a single group with the University of Wales Trinity St David.
- 2.50 Our site visits indicated that the college mergers have been delivered in line with financial plans and expectations, with no significant unplanned merger costs reported to us. The majority of colleges we visited confirmed that the mergers had also secured savings, although several colleges did not quantify these and those that did were unclear on the timeframe of the saving or whether it was long term.
- 2.51 The views of the colleges we visited on the extent of benefits varied depending upon the type of merger. Mergers between colleges are seen as delivering more benefits than mergers between colleges and higher-education institutions, although for the latter there were no reported significant adverse financial outcomes (Figure 16).

Figure 16 – Further-education sector views on merger benefits

Type of merger	Benefits reported to us
Merger between colleges	• Widely reported financial benefits. • There is some scope for further financial benefits as the new organisations mature – particularly in the back office. • Some colleges have consolidated provision at one site, for example, through a centre of excellence model, particularly for higher-level qualifications and/or those with significant capital investment requirements (eg workshops). • Consolidation of campuses has provided some benefit, but generally this is limited by the need to continue to deliver provision to local populations centred on the component college sites.
Merger between further education and higher education	• The financial benefits are more limited – there is no direct cross-subsidisation of revenue and the further-education group members are held to be self-funding in terms of revenue. • Most of the benefits have come from back-office efficiencies although progress has been limited in some cases and benefits slow to materialise. • Improvement to the student experience – particularly the opportunity for life-long learning – is also cited as an advantage.

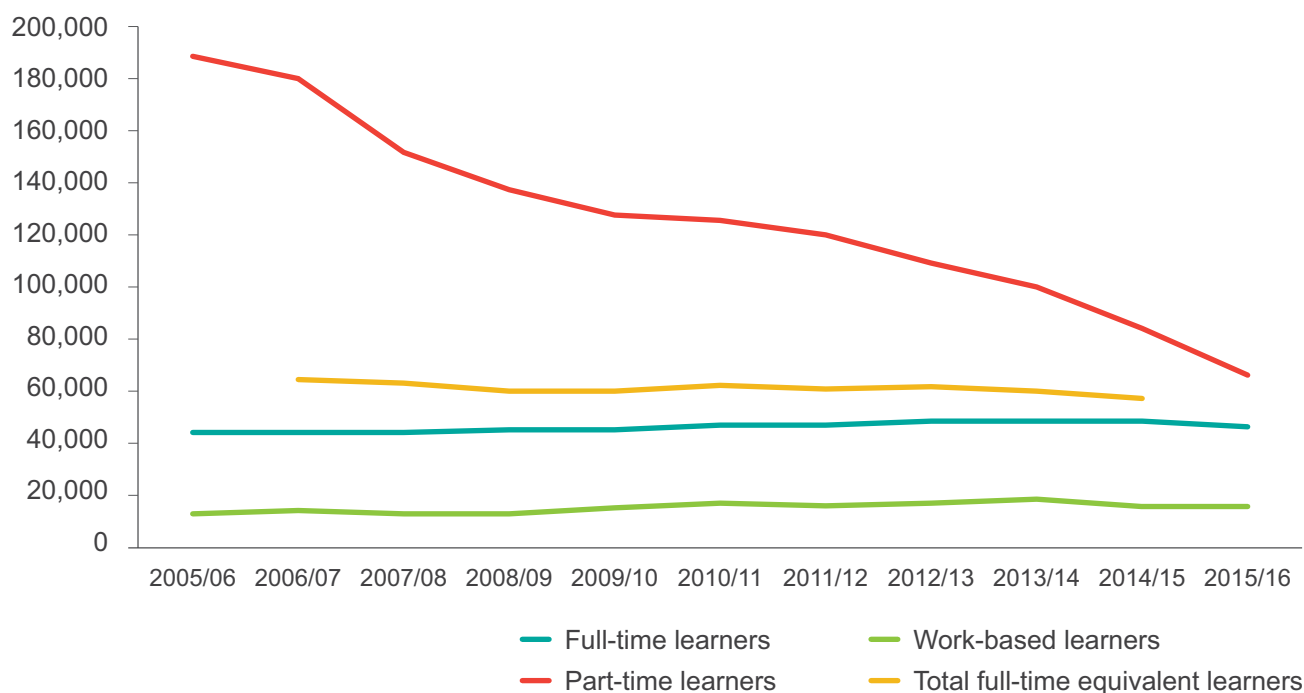
Source: Wales Audit Office and Grant Thornton fieldwork, March to April 2016

There has been a sharp fall in the number of learners, mainly due to cuts in part-time provision, and while the sector has maintained its performance on quality and outcome indicators to date the impact of more recent funding reductions is not yet clear

Welsh Government funding reductions have led to a sharp fall in the number of part-time learners although full-time provision for 16-19 year olds has been protected

2.52 Based on provisional data, in 2015/16, 130,850 learners were enrolled at further-education colleges, of whom 47,870 were on full-time courses, 67,090 on part-time courses and 15,890 on work-based learning programmes. Between 2010/11 and 2015/16, the number of full-time learners has increased by 1.9% while the number of part-time learners has reduced by 59,230 or 46.9% (Figure 17). The number of full-time equivalent students fell by 7.7% between 2010/11 and 2014/15 (figures for 2015/16 are not yet available). These changes reflect Welsh Government funding decisions and its protection of full-time provision for 16-19 year olds (paragraph 1.4). The reduction in part-time learners continues a trend evident since 2006/07.

Figure 17 – Number of learners at further-education colleges, 2005/06 to 2015/16



Note: Data for full-time equivalent learners was not available for 2005/06 or 2015/16. 2015/16 data is provisional.

Source: Welsh Government

- 2.53 The total number of learners has reduced by 58,845 (31%) between 2010/11 and 2015/16, almost entirely due to a reduction in the number of part-time learners. The 50% reduction in Welsh Government funding for part-time provision in 2015/16 (paragraph 1.4) resulted in a fall of 21% in the number of part-time learners, on top of a 16% reduction in the previous year.
- 2.54 Colleges have withdrawn many part-time courses, and higher tuition fees (made necessary by the withdrawal of public funding) have reduced demand for many other part-time courses. Colleges have mostly maintained the number and range of full-time courses throughout the period of funding reductions. However, practice does vary. Some colleges have not withdrawn any courses unless the relevant qualifications have been withdrawn or replaced. But other colleges have reduced the range of subjects offered, or have reduced the number of sites that some courses are provided from. Colleges in rural areas face particular challenges in maintaining full-time provision (Box 18).

Box 18: Challenges facing colleges in rural areas

Coleg Ceredigion has found it difficult to handle reductions in funding because of its small size, which has limited its scope to reduce overheads. The college primarily provides vocational courses with a small A-level provision and one higher-education programme, and has very little part-time provision. As a result, the college has had to adjust full-time vocational provision in order to live within lower real-terms budgets. However, the college is anxious to keep as many courses as possible in order to maintain student numbers, on which its income depends.

Ceredigion is a rural area with poor transport links and the college has sought to maintain accessibility by continuing to run as many courses as possible at the locations that have hitherto been used. The low and geographically dispersed population base has meant accepting smaller class sizes than would be the case in many less rural areas of Wales. However, some classes have been combined and are now run at only one or both of the college's two main campuses, with the college providing subsidised transport. The college has also combined level 1 and level 2 for some courses, which are typically taught in successive years, into a single class; and combining some similar courses such as IT Skills and Business Skills into a single course.

Other colleges operating in rural areas have not faced the same scale of difficulties. However, Grŵp Llandrillo Menai, Pembrokeshire College and NPTC Group of Colleges (which covers Powys) all have a policy of maintaining provision in order to avoid long journeys for learners, even if this results in relatively small class sizes. Grŵp Llandrillo Menai has also consolidated some provision at fewer locations for efficiency reasons, and provides joint classes for some courses in rural areas to ensure a breadth of curriculum offer.

The large reduction in part-time provision has, as the Welsh Government expected, had a negative impact on equality by restricting access for some groups

2.55 The Welsh Government undertook equality impact assessments when considering funding reductions to the further-education sector in October 2013 and November 2014. The assessments identified that, given the focus of the cuts, two groups would be negatively affected:

- people aged over 18 – provision for 16 to 18 years olds being protected; and
- females – the funding cuts focussed on part-time and adult community learning provision, both of which have a higher percentage of female learners.

2.56 In order to mitigate the impact on particularly vulnerable groups, the Welsh Government protected adult basic education, English for speakers of other languages, and learners with moderate or profound learning difficulties from the cuts to part-time provision. The impact assessments stated that the impact of the changes would be monitored and the Welsh Government would work with stakeholders to develop measures to mitigate any remaining negative impact on people over 18 and women, and the 2012/13 impact assessment stated that the Welsh Government would use funding from the employment and skills budget to support provision where appropriate. Officials told us that colleges had not raised any specific concerns with the Welsh Government, and therefore additional mitigating action was not required.³¹

2.57 The view from colleges is that the reduction in part-time courses has had a detrimental effect on low-income adults, particularly low-income females, who would benefit from access to further education but struggle to pay the higher fees that colleges now charge for courses. Colleges also identified the adverse impact on single parents who tend to rely more on part-time courses. Data is not available to identify the impact on these specific groups. Overall, however, there was a marked decline in the number of learners over the age of 19 on part-time courses between 2012/13 and 2015/16 – 27.7% for men and 37.0% for women – indicating that women have been affected more to some extent.

³¹ The Welsh Government has allocated significant sums from the 2014-2020 ESF programmes to help disadvantaged groups access the labour market, but these projects do not necessarily involve skills training and are not a direct substitute for the loss of part-time provision.

- 2.58 Colleges told us that the impact of the changes also makes it harder to help address the employment and poverty agendas, and some of the wellbeing goals outlined in the Well-being of Future Generations (Wales) Act 2015. More generally, some colleges commented on the benefits of adult community learning for community cohesion, even if many of the courses provided ('interest' or 'hobby' courses) did not directly contribute to economically valuable skills. For example, Bridgend College commented that community learning kept the college visible and accessible in the community, and these intangible benefits were largely lost once this provision was withdrawn.

The sector has maintained its performance on quality and outcome indicators over recent years, but the impact of the more recent funding reductions is not yet clear

- 2.59 The Welsh Government commissions an annual survey of further-education learners³², known as the Learner Voice survey, to assess their opinion on the education they receive. The first survey was carried out in 2009 on a sample basis, and full surveys took place annually from 2013 to 2015. The sample and full surveys contained largely different questions, limiting the comparisons that can be made back to 2009. However, both asked learners to rate the overall satisfaction with their learning experience, with the proportion deeming this to be 'very good' or good' ('extremely satisfied' or 'very satisfied' in the first survey) increasing from 74% in 2009 to 80% in 2015.³³
- 2.60 Since 2013, the surveys have been issued to all full-time and work-based learners and a 25% sample of part-time, adult community learning and Welsh for Adults learners. The participation rate (response rate from those who were included in the sample) was 68% on average across the three years. The survey findings show that the sector has maintained or slightly improved satisfaction levels between 2013 and 2015 (Figure 18). These findings indicate that, to date, financial constraints have not resulted in any deterioration in the quality of education as perceived by learners themselves.

³² The survey is currently suspended but was carried out annually between 2013 and 2015.

³³ The first survey in 2009 had 5,742 respondents sampled from the full population of FE learners. Subsequent surveys were of the whole learner population with between 53,000 and 62,000 respondents.

Figure 18 – Selected indicators from the Learner Voice Survey, 2013 to 2015

Question	% answering 'very good' or 'good'		
	2013	2014	2015
Opinion on overall learning experience	78	78	80
Opinion on:			
- Quality of teaching	81	81	81
- Information and advice	73	72	79
- Health and wellbeing	77	77	81
- Responsiveness	70	69	71
- Help and support	75	75	75

Note: Opinion on overall satisfaction with learning experience covers all full-time and part-time learners in further education for 2014 and 2015 and full-time learners only for 2013.

Source: Welsh Government, Learner Voice Wales Surveys

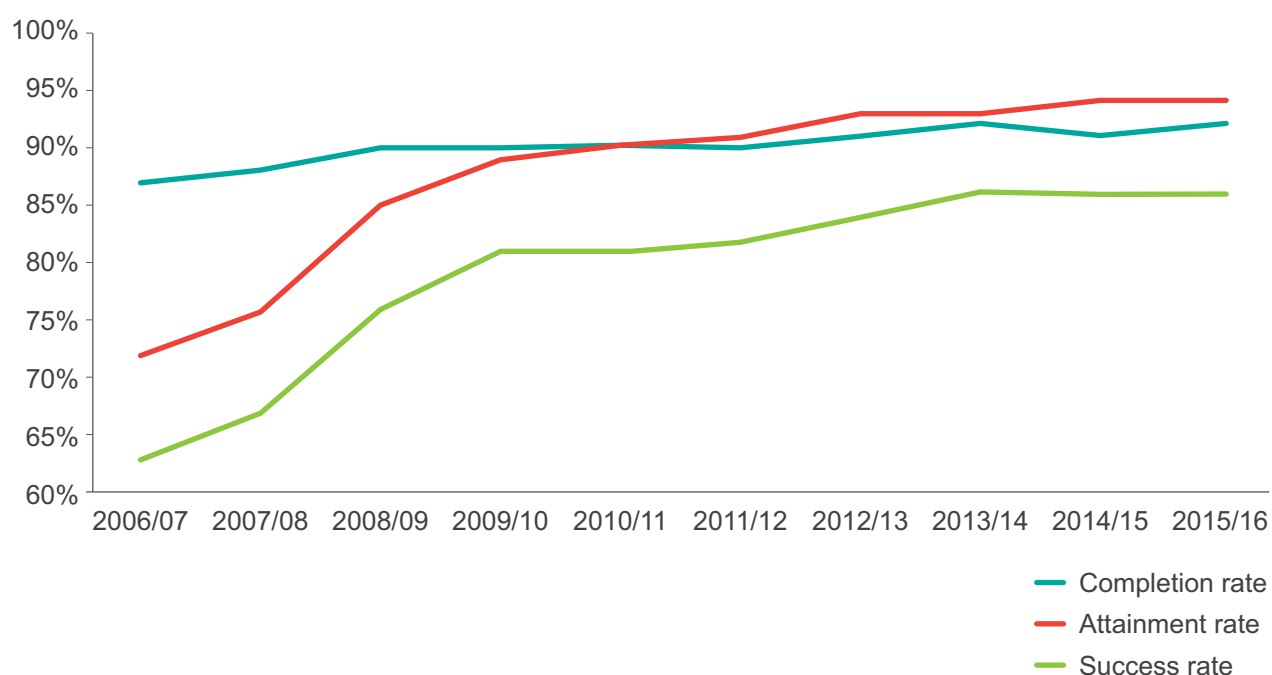
- 2.61 Recent inspection reports by Estyn indicate excellent or good standards for the three colleges inspected in 2015 and 2016 (Box 19). Estyn's annual performance reviews in 2014 (Box 9 on page 32) also reported favourably on standards at colleges with none presenting particular cause for concern.

Box 19: Estyn inspection findings

Estyn has inspected three colleges since full inspections of colleges resumed in 2015: Cardiff and Vale College (March 2015), Coleg Cambria (November 2015) and Bridgend College (March 2016). Bridgend College and Coleg Cambria were rated as 'excellent' for current performance and prospects for improvement, while Cardiff and Vale College was rated as 'good' on both aspects. All three colleges were rated as 'excellent' or 'good' across the key areas of outcomes, and learning provision.

2.62 The sector has improved its performance on key outcome measures between 2006/07 and 2015/16, with completion rates increasing overall by five percentage points, attainment rates by 22 percentage points, and success rates by 23 percentage points (Figure 19). Most of this improvement occurred before 2010/11, but there has been a small improvement in all three indicators in subsequent years, and Welsh Government officials believe some of the earlier improvement may have been due to improvements in data quality. These results indicate that financial constraints have not had a negative impact on outcomes up to 2015/16.

Figure 19 – Performance on learner-outcome measures, 2006/07 to 2015/16



Source: Learner-outcome reports published annually by the Welsh Government from data submitted by colleges

- 2.63 Some heads of curriculum have concerns about the reduction in tuition times for many courses ([paragraph 2.24](#)), which they felt would reduce time for practising vocational skills in particular, given that the academic content had to be covered in full. They were concerned that, over time, this situation would cut the proportion of learners achieving merits and distinctions in their courses. Data on achievement is not currently collected at this level of detail by the Welsh Government (although it plans to do so in future – [paragraph 1.63a](#)) so the impact will be difficult to evaluate.
- 2.64 The learner-outcome and satisfaction results are encouraging. However we, and Estyn, consider that it is too early to fully evaluate the impact of funding reductions on standards or outcomes, given that funding reductions are quite recent with the most severe cuts taking place in 2015/16; and given that many learning programmes take one year or two years to complete. Many of the changes in programme delivery described in this report were introduced in 2014/15 or 2015/16 and any impact will take time to feed through into outcome or satisfaction measures. Nevertheless, early signs for those colleges that have focused strongly on quality improvement, as recognised by recent Estyn inspection reports, are that they have made some changes to their course delivery to mitigate against changes in funding.

Appendices

Appendix 1 – Audit methods

Appendix 2 – Further-education colleges' governance and the role of the Welsh Government

Appendix 3 – College mergers by local authority area

Appendix 4 – Further-education colleges key data

Appendix 5 – Financial-health categories for colleges



Appendix 1 – Audit methods

Scope of the review

The scope of our work encompasses the 14 colleges located in Wales that exist specifically to provide further education on a not-for-profit basis. It includes A levels and the Welsh baccalaureate qualification, but sixth-form provision in schools is not included in the scope of our review. However, St David's Catholic Sixth Form College is included as it provides further education primarily for post-16 learners and is regulated as a further-education college. Also excluded from the scope of the review are work-based learning providers other than colleges, and private education providers.

Colleges appoint their own external auditors and fall outside the Auditor General's statutory audit regime. However, the Wales Audit Office has access rights to the colleges for the purpose of auditing public funds provided to colleges by the Welsh Government or its sponsored bodies.

We engaged the audit firm Grant Thornton to support our review.

Document and data review and analysis

We reviewed a range of documents and data relating to the sector as a whole, including:

- The main policy and strategy documents affecting the sector: **Qualified for Life**, the **Youth Employment and Progression Framework**, the **Policy Statement on Skills** and the **Skills Implementation Plan**;
- Independent reviews or research reports recently commissioned by the Welsh Government into post-16 education and training and sixth-form provision in Wales;
- The Welsh Government's **Guide to the Post-16 Planning and Funding Framework** for education and training and other guidance and regulations for the sector;
- Annual funding allocation letters and Ministerial letters setting out priorities for the sector; and
- Welsh Government budget documents and capital expenditure allocations for further education.

Colleges publish and provide the Welsh Government with a broad range of data and information including financial statements and estimates, governance statements, business plans, and a range of data on courses and learners. The Welsh Government produces some analysis of this data and information. We obtained and reviewed all this information, and undertook our own analysis, to assess the financial health of individual colleges and the sector as a whole and to review the effectiveness of the arrangements the Welsh Government has to monitor and support the sector.

We sent an information request to each college to obtain their perspective on cost reduction, joint working and communications with the Welsh Government. We also requested some supplementary information from individual colleges, for example feasibility studies on mergers, merger evaluations and cost-saving plans.

Interviews and meetings

We explored issues raised through our document and data review in interviews with Welsh Government officials and meetings with representatives of the further-education sector, including attendance at a sector Directors of Finance meeting.

We visited nine colleges as set out below and met with senior college leaders, including the Principal or Chief Executive Officer, the Director of Finance and senior managers in charge of curriculum planning. With one exception, the college visits were undertaken on our behalf by auditors from Grant Thornton. Bridgend College was visited by Wales Audit Office staff to avoid a possible conflict of interest because Grant Thornton provides the college's external audit function.

Colleges visited as part of the review

Bridgend College
Cardiff and Vale College
Coleg Ceredigion
Coleg Gwent
Grŵp Llandrillo Menai
The College Merthyr Tydfil
NPTC Group of Colleges
Pembrokeshire College
Coleg Sir Gâr

We also engaged with HEFCW in relation to their oversight of the three colleges controlled by universities and to compare Welsh Government oversight of colleges with the approach taken by HEFCW for higher-education institutions (as summarised previously in our 2013 **Higher Education Finances** report).

Finally, we discussed with the National Audit Office and Audit Scotland their recent reports on further education (**Overseeing Financial Sustainability in the Further Education Sector, published in 2015**, and two reports both entitled **Scotland's Colleges**, published in 2015 and 2016) to identify any common issues and notable differences.

Appendix 2 – Further-education colleges’ governance and the role of the Welsh Government

The Further and Higher Education Act 1992 established further-education corporations and designated Colleges in Wales from April 1993. This meant that Welsh colleges were no longer under local-authority control and became legally separate corporations. Initially colleges received funding through FEFCW. Under the Learning and Skills Act 2000, the National Council for Education and Training for Wales was established, which became known as Education and Learning Wales (ELWa). ELWa took over the remit of planning and funding post-16 learning. In 2006, ELWa merged into the Welsh Government and the Welsh Government took over funding of colleges directly.

Following the Further and Higher Education Act 1992, colleges were classified for national accounts as ‘non-profit institutions serving households’ (NPISH) and in national account terms were part of the private sector. In October 2010, the Office for National Statistics announced it would reclassify colleges to the general government sector rather than the NPISH sector. The UK Government and the Welsh Government felt this would have a negative impact on the further-education sector. The Education Act 2011 made amendments to the governance of further-education corporations in England sufficient for the Office for National Statistics to reclassify them as outside the public sector.

In 2014, the Welsh colleges returned to NPISH status following the Further and Higher Education (Governance and Information) (Wales) Act 2014. The Act amended previous legislation to increase colleges’ autonomy and independence with a college now able to:

- Modify or replace its instrument and articles of government, provided they always contain certain minimum requirements.
- Decide to dissolve itself and transfer its property, assets and liabilities to another institution, subject to consultation requirements.
- Borrow funds without the prior consent of the Welsh Government.
- Establish subsidiary arrangements (such as a company) to carry on any part of the college’s business.
- Appoint all its own governors except for two members elected by a college’s staff and two by its learners. Previously, the Welsh Government had the right to appoint two members of the governing body. However, the Act introduced enhanced intervention powers that allowed the Welsh Government to require a governing body to dissolve itself in certain circumstances.

Ten colleges are Exempt Charities Further Education Corporations, three colleges are now controlled by higher-education institutions and the newly merged WEA YMCA Community College Cymru (since renamed as Adult Learning Wales) operates across the whole of Wales.

In Scotland, colleges are now classified as part of the public sector and therefore have less autonomy and flexibility over their finances than colleges in England and Wales. For example, they are required to plan to break even on a resource basis each financial year, cannot accumulate cash reserves (which have been donated to arm's-length foundations) and are required to report more regularly to the Scottish Funding Councils.

The Further and Higher Education (Governance and Information) (Wales) Act 2014 reduced the powers of the Welsh Government. However, the Welsh Government acts as Principal Regulator of the 10 exempt charities in the sector. This role requires the Welsh Government to promote and monitor compliance with charity legislation and to notify the Charity Commission in the event of a breach.

The oversight of colleges is different from that applying to higher-education institutions with HEFCW having a significant role which has focused on funding arrangements but under the **Higher Education (Wales) Act 2015** will include some regulator functions which will be transferred from the Welsh Government. As a consequence HEFCW will have some regulatory functions for the three colleges that are part of higher-education institutions and also has a responsibility for funding and regulating approved higher-education courses that may be delivered at colleges. Transitional arrangements started on 1 September 2015, and the new Act will be fully implemented on 1 August 2017.

The Welsh Government's arrangements for monitoring the financial health of colleges were set out in Circular 24/2006 (Financial Health Monitoring for Further Education Institutions) and more recent guidance 006/2015 ('Accounts Direction to Further Education Institutions for 2014/15'). These documents set out the reporting and governance expectations the Welsh Government has of colleges and the role of the Welsh Government in monitoring the institutions. Regular meetings are held between college directors of finance and the Welsh Government facilitated by ColegauCymru.

Colleges' use of public funding is governed by the **Financial Memorandum**, issued by the Welsh Government in 2014. This document:

- Sets out the general responsibilities of the Welsh Government's accounting officer and colleges' governing bodies;
- Requires the college to use public funds only for the purposes for which they were allocated, and to repay funds not used for such purposes;
- Requires the governing body to approve and monitor a financial strategy designed to ensure the solvency of the college, and to manage finances prudently; and
- Provides guidance on accounting requirements.

Estyn is responsible for the inspection of individual colleges, currently on a three-year cycle. Inspections include an assessment of colleges' overall performance and quality of provision, a review of college leadership and management, and more detailed assessment of a sample of learning areas to assess teaching quality and management practice.

Appendix 3 – College mergers by local-authority area

Local authority	Colleges as at September 2008	Merger dates	Colleges as at August 2015 ¹
Blaenau Gwent Monmouthshire Newport Torfaen	Coleg Gwent	N/A	Coleg Gwent
Cardiff	St David's Catholic College	N/A	St David's Catholic College
	Coleg Glan Hafren	August 2011	Cardiff and Vale College
Vale of Glamorgan	Barry College		
Rhondda Cynon Taf	Coleg Morgannwg	August 2013	Coleg y Cymoedd
Caerphilly	Ystrad Mynach College		
Merthyr Tydfil	The College Merthyr Tydfil	May 2006 with University of Glamorgan (now University of South Wales)	The College Merthyr Tydfil ²
Bridgend	Bridgend College	N/A	Bridgend College
Powys	Coleg Powys	August 2013	NPTC Group of Colleges
Neath Port Talbot	Neath Port Talbot College		
Swansea	Swansea College Gorseinon College	August 2010	Gower College Swansea
Carmarthenshire	Coleg Sir Gar	August 2013 with University of Wales Trinity Saint David	Coleg Sir Gâr ²
Pembrokeshire	Pembrokeshire College	N/A	Pembrokeshire College
Ceredigion	Coleg Ceredigion	January 2014 with University of Wales Trinity Saint David	Coleg Ceredigion ²

Local authority	Colleges as at September 2008	Merger dates	Colleges as at August 2015 ¹
Anglesey	Coleg Menai	April 2010 – Coleg Llandrillo Cymru and Coleg Meirion-Dwyfor April 2012 – Coleg Llandrillo Cymru and Coleg Menai	Grŵp Llandrillo Menai
Gwynedd	Coleg Menai Coleg Meirion-Dwyfor		
Denbighshire	Coleg Llandrillo Cymru		
Conwy			
Flintshire	Deeside College Welsh College of Horticulture Coleg Llysfasi	August 2009 – Deeside College and Welsh College of Horticulture August 2010 – Deeside College and Coleg Llysfasi	Coleg Cambria
Wrexham	Yale College Wrexham	August 2013 – Deeside College and Yale College Wrexham	
Community-based	YMCA Community College WEA South Wales Coleg Harlech WEA	January 2014 – WEA South and Coleg Harlech WEA to form WEA Cymru August 2015 – WEA Cymru and YMCA Community College	WEA YMCA Community College Cymru (renamed Adult Learning Wales on 5 November 2016)

Notes:

- Colleges may have campuses in several locations within the area that they cover. Mergers do not necessarily imply that provision is centralised at one campus or a smaller number of campuses.
- The college is part of a group including a higher-education institution, but is largely autonomous and stands alone for financial reporting purposes.

Source: ColegauCymru briefing paper, March 2014 and college websites

Appendix 4 – Further-education colleges key data

Provisional 2015/16 for student numbers. Audited 2015/16 for financial indicators.

College	Number of full-time learners	Number of part-time and work-based learners	Total income (£000)	Operating surplus/ (deficit) (£000)	Liquidity (cash days) ¹
Bridgend College	2,470	3,050	26,416	360	39
Coleg Cambria	6,245	11,285	53,345	1,652	101
Cardiff and Vale College	4,325	5,445	44,600	(1,859)	62
Coleg Ceredigion	685	355	4,940	(429)	25
Coleg y Cymoedd	5,035	3,695	36,607	(1,390)	124
Gower College Swansea	4,510	6,760	36,472	115	89
Coleg Gwent	7,500	8,735	51,744	1,419	75
Grŵp Llandrillo Menai	6,445	15,085	70,303	(2,618)	58
The College Merthyr Tydfil	1,765	845	13,816	178	78
NPTC Group of Colleges	4,190	7,170	49,617	436	64
Pembrokeshire College	1,720	4,185	26,728	32	77
Coleg Sir Gâr	2,855	3,000	30,349	961	79
St David's Catholic College	1,320	20	6,646	(62)	46
WEA YMCA Community College Cymru ²	0	17,985	6,885	(490)	94

Notes:

- ¹ Cash days is a liquidity measure calculated as the number of days' total expenditure covered by short-term investments and cash, net of bank overdrafts. Total expenditure includes non-cash costs such as depreciation and certain pension charges.
- ² WEA YMCA Community College Cymru (since renamed Adult Learning Wales) was formed on 1 August 2015 by the merger of WEA Cymru and YMCA. The student numbers are the totals of the predecessor institutions.

Appendix 5 – Financial-health categories for colleges

Category	Criteria for allocating to the category
A – The institution's financial position and its financial strategy fully support the institutional plan	- Financial strategy fully supports the institutional plan with targets and actions to deliver sufficient cash and operating surpluses to finance ongoing activity, fund investment and produce a financial reserve. - Year-on-year operating surpluses and cash inflows from operating activities at a level consistent with the financial strategy. - Adjusted cash balances¹ equivalent to one month's expenditure. - Net current assets.² - Positive balance on general reserves before pension deficit. - Net deficits or cash outflows occur only because of planned investments or strategic decisions.
B – The institution's financial position and its financial strategy currently support the institutional plan but could be strengthened	- Financial strategy currently supports the institutional plan with targets and actions to deliver sufficient cash and operating surpluses to finance ongoing activity, fund investment and produce a financial reserve, and there is a plan to address any weaknesses in the financial position. - Year-on-year operating results and cash flows give a break-even position and there is a plan of how to return to the levels required by the financial strategy. - Adjusted cash balances equivalent to one month's expenditure. - Net current assets. - Positive balance on general reserves before pension deficit. - Net deficits or cash outflows occur only because of planned investments or strategic decisions and are fully funded from cash reserves.

Category	Criteria for allocating to the category
C – The institution's financial position or its financial strategy require improvement to support the institutional plan	- Financial strategy currently supports the institutional plan with targets and actions to deliver sufficient cash. - Financial strategy does not support the institutional plan or fails to identify targets and actions to deliver sufficient cash and operating surpluses to finance ongoing activity, fund investment and produce a financial reserve. - Recurring operating deficits or surpluses that do not meet the targets set out in the financial strategy. expenditure (current or forecast in next two years) - Forecast net current liabilities. - Forecast negative reserves before pension deficits. - Operating deficit or cash outflows occur otherwise than as part of planned investments or strategic decisions, or are not fully funded from cash reserves.
D – The institution's financial position is weak and does not support its financial strategy or the institutional plan	- Financial strategy does not support the institutional plan and fails to identify targets and actions to deliver sufficient cash and operating surpluses to finance ongoing activity, fund investment and produce a financial reserve. There is no effective plan to address this position. - Advance of grant or external loan is needed to meet liabilities as they fall due. - Operating results and/or net cash flows do not meet targets in the financial strategy or there is no effective plan to address this position. - Adjusted cash balances less than one month's expenditure (current or forecast in next two years). - Forecast net current liabilities. - Forecast negative reserves before pension deficits. - Improvements in financial position have yet to be confirmed in the annual audited financial statements.

Notes:

- Adjusted cash balances is defined here as cash in hand plus bank deposits less liabilities payable within one year.
- Net current assets: the amount by which debtors, liquid investments and cash (receivable or realisable within one year) exceed creditors and loans payable within one year. This is a key measure of liquidity or ability to pay liabilities as they fall due.

Source: Welsh Government, **Financial Health Monitoring Procedures for Further Education Institutions (Circular 24/2006)**, January 2007

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Huw Morris

Director, Skills, Higher Education and Lifelong Learning
Cyfarwyddwr, Sgiliau, Addysg Uwch a Dysgu Gydol Oes



Llywodraeth Cymru
Welsh Government

Mr Huw Vaughan Thomas
Auditor General for Wales
Wales Audit Office
24 Cathedral Road
CARDIFF
CF11 9LJ

Date: 20 March 2017

Dear Huw

**Response to the report 'Welsh Government oversight of FE colleges' finances and delivery'
(28 February 2017)**

I would like to thank you for this report. Whilst reductions in funding to the FE sector over recent years are acknowledged in the report, I am pleased that it highlights the good relationships forged between the sector and officials in Welsh Government which has minimised the impact on learners wherever possible.

The report recognises that the Welsh Government's funding allocation and oversight arrangements are sound, but would benefit from a more integrated and long-term approach. Many of the 7 recommendations in the report were already in progress and will be considered in further detail in line with the additional evidence highlighted in the report.

We accept the recommendations, but due to the Welsh Government wide implications of some of them, I am not in a position to be able to respond fully to each recommendation. I intend to send you our full response to each recommendation shortly.

The contents of the report will also be shared with lead officials responsible for considering the outcomes of the Hazelkorn review and the development of a single, overarching strategy for post-16 education.

Finally I would like to note that the engagement between WAO and Welsh Government officials from the initial interview stage through to the drafting of the final report has been active and constructive.

Yours Sincerely



Huw Morris
Group Director SHELL

c.c Cabinet and Plenary Mailbox
 The PAC Chair
 WG CGU Mailbox

Huw Morris
Director, Skills, Higher Education and Lifelong Learning
Cyfarwyddwr, Sgiliau, Addysg Uwch a Dysgu Gydol Oes



Llywodraeth Cymru
Welsh Government

Mr Huw Vaughan Thomas
Auditor General for Wales
Wales Audit Office
24 Cathedral Road
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Date: 08 June 2017

Dear Huw

**Response to the report 'Welsh Government oversight of FE colleges' finances and delivery'
(28 February 2017)**

I wrote to you in March in response to the above report with a commitment to respond fully to each recommendation at a later stage due to the Welsh Government wide implications of some of the recommendation.

I am now pleased to be able to share with you those responses at Annex A to this letter.

Yours Sincerely

Huw Morris
Group Director SHELL

c.c Cabinet and Plenary Mailbox
The PAC Chair
WG CGU Mailbox

Recommendation 1

While recognising the uncertainties facing the Welsh Government's own revenues, we recommend that the Welsh Government re-introduce three-year funding settlements at the earliest opportunity to assist colleges in their financial planning.

Response: Accept in principle

Recent years' funding settlements have been developed against the backdrop of unprecedented uncertainty with Welsh Assembly budgets only being laid on an annual basis.

Our aim is to publish a budget for a three year horizon, which would give our FE Colleges greater certainty in planning for a longer budget period. However, this can only be achieved with greater clarity about the revenue resources available to Welsh Government and therefore the funding settlements to colleges will mirror budgets laid by Cabinet.

It should be noted though that while the funding provided to FE Colleges through the Welsh Government is a very important component for budget setting, it is not the only source. FE Colleges have been asked to increase commercial income and increase fee income, via HE delivery for example. FE Colleges must take account of all the sources of funding available to them in preparing their short and medium term financial plans and the ability to do so should not be reliant upon the Welsh Government grant alone.

Recommendation 2

We recommend that the Welsh Government consider, as part of its institutional review process, how well placed colleges are to respond in the event of capital funds becoming available with tight timescales.

Response: Accept in principle

There will be occasions, such as the minor capital expenditure in 2016/17, where budget is available at short notice. In order to ensure FE Colleges are well placed to respond to capital budget coming available with tight timescales, consideration of the financial and estates position of each college is required as the ability to respond would depend on both the ability to match fund as well as having capital schemes ready to start.

Whilst officials accept this recommendation, in principle, it is proposed that this knowledge should be built into routine knowledge gathering of the finance and estates team to ensure an up to date position is always known rather than including it as part of an institutional review that may not look at each college on a regular enough basis.

This recommendation should not be limited to capital expenditure but should cover any scenario where a college might be asked to react to new project or funding stream.

Recommendation 3

We recommend that the Welsh Government requires colleges to prepare medium-term financial plans, including longer-term financial forecasts, and provide appropriate guidance and support, working with the sector to discuss any key underpinning assumptions.

Response: Accept

The Welsh Government is already taking action in this area. In recent years, financial forecasts have been requested from Colleges in Wales for the current academic year and also the next academic year. In June 2016, Welsh Government commissioned the financial forecasts from Further Education Institutions in Wales which were to be returned by the 31 July. These financial forecasts covered the current academic year (15/16) and a further three academic years from 16/17 to 18/19. The assumptions provided to Colleges for inclusion in the forecasts included assumptions on Welsh Government grant funding, pay, European income, capital, inflation and other grant income.

These assumptions will be reviewed on an ongoing basis so that the financial forecasting can be improved and give a more accurate position of the Colleges' financial health in the current financial climate.

Recommendation 4

We recommend that the Welsh Government develop a mechanism that links funding more closely to likely demand for further education in each area, while recognising the need to phase in significant changes in order to manage the financial impact on individual colleges.

Response: Accept

Growth funding has already been allocated in 2016/17 to reflect where colleges have seen growth in level 3 provision and a similar exercise is currently being undertaken for 2017/18. These have both been one-off recognitions of growth but a working group has already been set up, which includes college Principals and finance directors, to discuss and model several options of growth/decline which is anticipated to inform a revised funding mechanism beginning in 2018/19.

Recommendation 5

We recommend that the Welsh Government develop its institutional review framework to provide a comprehensive assessment of each college's performance and risks, and to report publicly on the main findings of these reviews each year.

Response: Accept

We will be piloting a new institutional review process during 2017, bringing together information from existing assessments and considering how other aspects of colleges' performance, including leadership and employer responsiveness, can be incorporated. This will be part of a wider 'FE resilience' programme to support the sector to meet current and future challenges. It is anticipated that this approach could provide the foundation for introducing outcome agreements in future, as part of the proposed establishment of a new oversight body for post-compulsory education and training in Wales.

We intend to work closely with the sector to develop the review framework and outcomes agreements. We do not anticipate publishing outcomes of reviews until this development and piloting has taken place.

Recommendation 6

We recommend that the Welsh Government provide focussed annual guidance for colleges, set in the context of longer-term, sector-wide strategic guidance.

Response: Accept

Welsh Government is committed to pursuing the development of an overarching strategy for post-16 education, building forward from the recommendations brought forward by

Professor Hazelkorn in her report “Toward 2030”. The Welsh Government recognises the important role which focussed annual guidance for colleges necessarily plays in supporting the emergence of a post-16 sector which bests supports the learning pathways and opportunities valued by employers and learners alike. We support the principle that planning guidance should be reviewed against the overarching ambition to deliver a more sophisticated approach to post-compulsory education governance which:

- enhances educational and career opportunities and quality, across the whole post-compulsory spectrum, and people’s lifetimes;
- anchors and underpin regional social, cultural and economic development; and
- boosts institutional and national global competitiveness.

In this context we are committed to strengthening the links between FE guidance and Ministerial strategies to support a Wales which is Prosperous and Secure, Healthy and Active, Ambitious and Learning and United and Connected.

Welsh Government will continue to review the annual guidance provided to institutions with a view to establishing a limited number of high level strategic goals able to guide both the wider sector and individual institutions.

Recommendation 7

Response: Accept

We recommend that the Welsh Government evaluate the impact of funding reductions on learners (including the impact on equality) once this data is finalised and use the results to inform future decisions on policy and funding.

Statistical data, once available, will be used to evaluate the impact of the funding reductions on the FE Sector. This will be used to identify the accuracy of the Equality Impact Assessments drafted at time of the reductions.

The results are unlikely to alter the policy decisions, as the statutory obligation placed upon provision for 16-18 year olds leaves little option but to continue to reduce part time adult provision should further budget reductions be enforced. The results will, however, be used to inform strategic budgeting decisions to highlight the impacts of previous reductions and the likely impact of future reductions prior to future budgets being laid.