Dear Convener

**College Sector Cash and Reserve Levels 2011-12**

As was mentioned in your evidence session with college principals on Tuesday 5 February 2013 on the Post 16 Education (Scotland) Bill, Colleges Scotland has been putting together an analysis of the financial situation of colleges, based on their fully audited 2011/12 accounts as at July year end.

We received a 100% return, with all the 41 colleges in Scotland providing their financial information, including the three FE colleges involved in the recent merger into SRUC.

This information has enabled us to provide an updated and complete sector profile in terms of cash available and the reserves position. We also asked colleges to provide information on any known spending plans against their cash reserves and an opportunity to provide background information on their financial position.

We have used this information to inform the key findings paper attached, which we hope will be of interest to the Committee. We have also included the detailed financial information. We have agreed with colleges to provide only the sector position, rather than details for any particular institution, but these individual accounts will be laid before the Scottish Parliament in due course.

Yours sincerely,

John Henderson
Chief Executive

Enc: College Sector Cash and Reserve Levels 2011-12 Paper
Colleges Cash and Reserve Levels 2011/12 – Key Findings
Thursday 7 March 2013

The Report of the Review of Further Education Governance in Scotland by Professor Russel Griggs is frequently quoted as suggesting available college reserve levels of around £200m. Recent analysis of the college sector July 2012 year end accounts has updated this position, and indicates that the sector is operating in a very tight cash position, with reserves far lower than previously stated – with most of these reserves being held with specific plans for future investment in the colleges estate.

Funds which colleges have to spend have to be understood in terms of both cash and reserves. Cash is the money in hand and in the bank that the college can access. This is expected to meet all the day to day costs of operations, as well as have some extra flexibility should there be any additional costs not known when budgeted – such as urgent repairs to buildings or equipment, to meet obligations on paying invoices on time, or to ensure there is enough to manage if there is unexpected loss of income, as almost 30% of income comes from non-government sources.

For 2011/12 colleges had £178m in cash, to cover £131m of short-term liabilities – leaving £47m. In responding to Colleges Scotland, members indicated that a further £5.1m is committed for spending in the future. The Scottish Funding Council (SFC) provides guidance that colleges should aim to have, as a minimum, the equivalent of two months cash available to cover expenditure. The £42m remaining would equate to roughly 19 days. These funds can be a cushion, and having that cushion is prudent and good practice.

Reserves, on the other hand, are not cash. They cannot be withdrawn like funds in a bank account. Some are expected to be used to fund certain future commitments, such as pensions, and some are restricted. Also, of the total reserves in colleges, £230m is showing the increased value of estates – to access that money would only be possible through colleges selling their buildings. This is commonly known as the revaluation reserve.

The remainder is just over £100m – which has been accumulated for different reasons: for long-term loan repayments, or to be put towards planned large projects such as new campus buildings or student accommodation. Reserves can only be accessed if a college plans to spend more money than it will make, and has cash available to do so.

Colleges told us that of that £108m reserves, £38m is earmarked for future spend on new facilities or other investment in their estates. That leaves around £70m. Two other colleges indicated they will spend reserves on meeting the costs of mergers, but were not able to specify the exact figure yet.

Further funds will likely go towards the nine mergers expected to take place over the next two years – involving 20 colleges. Some reserves have already been spent in mergers that have taken place, often matching central funding support. The cost of these future mergers is expected to be partly met by SFC and Scottish Government, who will contribute around £54m. Costs will exceed that, and will likely be met from remaining college reserves.

Audit Scotland, when reviewing college accounts from 2010/11, stated colleges were operating in very tight margins, and the accounts from 2011/12 show these margins are
going to be tighter still, with very little flexibility. Reserves are not a sustainable source of funding.

Some facts:
- 100% of colleges provided their financial information for 2011/12, 41 colleges in total (including the three land-based colleges now forming SRUC).
- Of these, 38 had positive reserves.
- Three had negative reserves. Taking account of pension liabilities, this number rises to 13.
- Only four colleges had reserves above £10m.
- The total value of the sector is just under £1bn, held mostly as land and buildings.
- The total reserve position is made up of revalued assets (£230m) and income and expenditure reserves (£108m).
- Deferred capital is (£627m) which has already been spent on assets, is released to offset depreciation.
- The sector had long-term loan and provision liabilities of over £160m.

Colleges Scotland
March 2013
## College Sector Cash and Reserve Levels 2011/12

<table>
<thead>
<tr>
<th>College: Total Sector</th>
<th>2010/11</th>
<th>2011/12</th>
<th>Narrative</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£'000</td>
<td>£'000</td>
<td></td>
</tr>
<tr>
<td><strong>Cash at bank and in</strong></td>
<td></td>
<td></td>
<td>A balance sheet will change daily. It is important to understand the commitments within an organisation and the timing of those commitments.</td>
</tr>
<tr>
<td><strong>hand</strong></td>
<td>190,477</td>
<td>177,739</td>
<td></td>
</tr>
<tr>
<td>Total Current Assets</td>
<td>265,567</td>
<td>245,126</td>
<td>This cash balance of £178m is a decline on the previous year. This balance will be required to cover the current liabilities in the year of £131m (see below line re Total Current Liabilities). Some of the cash is in advance from SFC for estates development. This cash level represents approx 1-2 month of trading activity. Cash is required for working capital commitments; to contribute to merger expenditure; to prudently cover long-term commitments and future capital investments.</td>
</tr>
<tr>
<td>Total Current Liabilities</td>
<td>149,120</td>
<td>130,557</td>
<td>There are some large commitments not only to merger funding, but also estates campus developments e.g. student accommodation developments.</td>
</tr>
<tr>
<td>Net Current Assets</td>
<td>116,447</td>
<td>114,569</td>
<td>Positive value of the college sector - just under £1billion. The bulk of the value is held as fixed assets (land and buildings).</td>
</tr>
<tr>
<td>Total Assets - Current Liabilities</td>
<td>1,284,837</td>
<td>1,276,845</td>
<td></td>
</tr>
<tr>
<td>Net Assets (including pension)</td>
<td>1,052,130</td>
<td>997,418</td>
<td></td>
</tr>
<tr>
<td>Reserves</td>
<td></td>
<td></td>
<td>Commitments for current capital projects, new campus developments and other estates developments e.g. student accommodation.</td>
</tr>
<tr>
<td>a) Income &amp; Expenditure Account (excluding pension reserve)</td>
<td>208,565</td>
<td>219,746</td>
<td></td>
</tr>
</tbody>
</table>
This is an accounting calculation of the pension liability for defined benefit pension schemes. This does not take account of those colleges with defined contribution schemes, nor will it cover those colleges who have no formal pension scheme.

| b) Pension Reserve | -67,439 | -111,943 |
| c) Income & Expenditure Account (including pension reserve) | 141,536 | 108,213 |
| d) Revaluation Reserve | 237,577 | 230,631 |
| e) Restricted Reserves | 17,408 | 18,238 |
| **Total Reserves** | **396,521** | **357,082** |

Loan and Provisions | -165,268 | -167,484 |
Deferred Capital and Endowments | 660,073 | 645,032 |
Fixed Assets | 1,168,390 | 1,162,276 |

This is not cash. This is the cumulative operating position of the sector, after pension liabilities (valued under FRS17). These reserves have commitments of new campus developments and other estates developments against them. Such reserves will also be used to address a back-log of estates maintenance in some cases. To access reserves, the organisation will be required to operate in a deficit position i.e. spend more than is earned. Furthermore, cash is required for expenditure. Banks may not wish to lend cash to organisations who are operating in a deficit position.

This is purely an accounting adjustment wherein an asset, usually a building, has been revalued by an external advisor and the college is required to recognise any increase or decrease in value in its balance sheet. Therefore, this is a theoretical value which cannot be realised unless such assets are sold. The decrease is due to a revaluation.

There are specific restrictions against these reserves, meaning they must be released for the stated purpose e.g. estates or the environmental research institute (ERI). Some restrictions apply to estates build already underway.