AUDIT COMMITTEE

Tuesday 28 June 2005

Session 2

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AUDIT COMMITTEE

12th Meeting 2005, Session 2

CONVENER

*Mr Brian Monteith (Mid Scotland and Fife) (Con)

DEPUTY CONVENER

*Mr Andrew Welsh (Angus) (SNP)

COMMITTEE MEMBERS

*Susan Deacon (Edinburgh East and Musselburgh) (Lab)
*Margaret Jamieson (Kilmarnock and Loudoun) (Lab)
George Lyon (Argyll and Bute) (LD)
*Mrs Mary Mulligan (Linlithgow) (Lab)
*Eleanor Scott (Highlands and Islands) (Green)

COMMITTEE SUBSTITUTES

Chris Ballance (South of Scotland) (Green)
Mr Ted Brocklebank (Mid Scotland and Fife) (Con)
Marlyn Glen (North East Scotland) (Lab)
Mr John Swinney (North Tayside) (SNP)

*attended

THE FOLLOWING ALSO ATTENDED:

Mr Robert Black (Auditor General for Scotland)
Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP)
Mary Scanlon (Highlands and Islands) (Con)

THE FOLLOWING GAVE EVIDENCE:

Brian Baverstock (Scottish Funding Councils for Further and Higher Education)
Riona Bell (Scottish Funding Councils for Further and Higher Education)
Eddie Frizzell (Scottish Executive Enterprise, Transport and Lifelong Learning Department)
Mr David Green (Lews Castle College)
Dr Tony Kinder (West Lothian College)
Professor John Little (Inverness College)
Mr Kenneth Mackie (Inverness College)
Mr Roger McClure (Scottish Funding Councils for Further and Higher Education)
Aileen McKechnie (Scottish Executive Enterprise, Transport and Lifelong Learning Department)
Mrs Sue Pinder (West Lothian College)

CLERK TO THE COMMITTEE

Shelagh McKinlay

SENIOR ASSISTANT CLERK

David McLaren

ASSISTANT CLERK

Clare O'Neill

LOCATION

Committee Room 6

Scottish Parliament

Audit Committee

Tuesday 28 June 2005

[THE CONVENER *opened the meeting in private at 09:31*]

10:13

Meeting continued in public.

Interests

The Convener (Mr Brian Monteith): I welcome our guests and members of the public and press to the 12th meeting in 2005 of the Audit Committee. We have a full agenda today. We have already taken agenda item 1 in private and there are a number of other agenda items before we come to our evidence session on colleges. I welcome the college representatives and those from the funding councils and the Executive. I shall say that informally at the moment, rather than reading out everyone's names, because I shall be doing that later and there is no need to repeat a long list.

Our first item was taken in private and item 2 is a declaration of interests. We welcome our new committee member, Eleanor Scott, whom I invite to declare any interests that are germane to the committee.

Eleanor Scott (Highlands and Islands) (Green): I was about to say that I did not have any interests to declare, but I realise in the light of the business that is before the committee that I do have a relevant interest to declare. As a legacy of my previous employment, I am still a member of the British Medical Association. I shall amend my entry in the register of members' interests accordingly.

The Convener: Thank you. That declaration is noted.

Items in Private

10:15

The Convener: We move on to agenda item 3, which is to seek the committee's approval for taking agenda items 6 and 7 in private. Agenda item 6 is to enable the committee to consider the evidence taken under agenda item 5 on our inquiry into section 22 reports by the Auditor General for Scotland on the 2003-04 audits of West Lothian College, Inverness College and Lews Castle College. Agenda item 7 is to enable the committee to consider a draft report on the committee's inquiry into the Auditor General for Scotland's report "A review of bowel cancer services: An early diagnosis". Do we agree to take agenda items 6 and 7 in private?

Members *indicated agreement*.

Audit Scotland (Annual Report and Corporate Plan)

10:16

The Convener: Agenda item 4 is a briefing from the Auditor General for Scotland on Audit Scotland's annual report for 2004-05 and its corporate plan for 2005-08.

Mr Robert Black (Auditor General for Scotland): It is now some five years since Audit Scotland was created and our work now covers more than 200 public bodies in Scotland and spending of more than £26 billion a year. We recently published Audit Scotland's annual report and the corporate plan looking forward—one of today's committee papers summarises the main elements of our work over the past year and considers the key priorities in our corporate plan for the next three years.

In the past year—2004-05—I made 12 performance audit reports to the Parliament and 20 reports to accompany audited accounts. I shall talk about the performance audit reports first. The year started with a follow-up report on day surgery in Scotland. There was then a report on local economic forums, followed by a report on account management services delivered by Scottish Enterprise to high-growth businesses.

Those three reports were followed in late June 2004 by my third report on the management and control of the Holyrood building project. I had been asked by both the Presiding Officer and the First Minister to work closely with Lord Fraser's inquiry, which they had independently commissioned. I reached an agreement with Lord Fraser that my audit would concentrate on the project management and control, subsequent to the first report that I made back in September 2000, and that Lord Fraser's inquiry would cover all other aspects of the project, from its inception before devolution through to the summer of last year.

By working together in that way, we were able to avoid duplication and reduce the amount of information that we needed to seek from project management. I also believe that we made good and effective use of the analytical strengths of Audit Scotland in complementing the inquiry that Lord Fraser undertook, which centred on taking evidence from witnesses. I am pleased to say that the audit of project management was available to Lord Fraser just in time for his report, which was published in September 2004. I am equally pleased to say that Lord Fraser agreed with the analysis and conclusions of my report.

As members know, the committee took preliminary evidence on my report. However, in view of the debate in the Parliament on Lord Fraser's report, the committee decided in late September not to conduct a further inquiry or to make findings of its own. That is clearly understandable, but it had the consequence of leaving a few loose ends that were not tied up. One of those related to whether my report was factually accurate. Audit Scotland checked that out in great detail over the summer of 2004 and I welcome this opportunity just to record the fact that I am satisfied that there were no errors of any significance in the report that I made to the Parliament, which was considered by the committee.

Last summer was a busy period. Following the Holyrood report, we published the report "Commissioning community care services for older people". That was followed by our first Audit Scotland report on the overall performance of the national health service in Scotland. The rest of the year saw reports on the management of community equipment and adaptations, on the contract for the provision of prison escort, court and custody services by the Scottish Prison Service and on maintaining Scotland's roads. In December, I produced the report "Overview of the financial performance of the NHS in Scotland 2003/04".

In the early months of this year, there were two more performance audit reports: the report on correctional opportunities for prisons in the SPS and the review of bowel cancer services, which is on today's agenda. Throughout the year there were 20 reports on audited accounts. It is fair to say that by far the most significant of those related to the 2003-04 audit of Argyll and Clyde NHS Board, which led the committee to take extensive evidence and make its own report.

I turn briefly to the Audit Scotland corporate plan for 2005-08. I have always been of the view that the first priority of Audit Scotland is to support democratic scrutiny and that view is reflected in our corporate plan. We provide the objective evidence that enables the Scottish Parliament, principally through this committee, to hold the Executive to account for the proper, efficient and effective spending of public money. Our latest corporate plan provides for a performance audit programme of 12 reports during the autumn and winter of 2005 through to 2006 and 14 reports from the spring of 2006 onwards.

In that context of supporting democratic scrutiny, I mention the new best-value regime for local government, because it, too, helps to strengthen democratic scrutiny. The integrated reports on the overall performance of individual councils that will be produced in a three-year cycle by Audit Scotland for the Accounts Commission are intended to provide not only the public but, equally important, local councils and ministers with objective evidence on the performance of an individual local authority in the round. I like to think that the best-value regime will strengthen democratic scrutiny by providing a further source of objective evidence on how councils are performing.

The first four best-value reports were delivered to the Accounts Commission in 2004-05. The target in the corporate plan is to deliver best-value audits of 11 councils and one police authority in 2005-06 and of a further 14 councils and two police authorities in 2006-07. That will be a challenging programme, but that is the commitment that we have given in the corporate plan.

A second priority in the corporate plan is to maximise the value of the significant resources that go into audit. We are modernising the audit processes to support improvements in the management and performance of public bodies. For example, in the NHS, this year's audit concentrates on clearly identified key priorities and risks. We have identified those systematically and they will be the focus of audit analysis and reporting. That risk-based approach will be applied across the whole public sector from 2005-06.

For the strategy that I published in the spring of last year, I used the title "Holding to account and helping to improve". Five years after the creation of Audit Scotland, I am satisfied that public audit can fulfil the two roles of holding to account and helping to improve without compromising the independence and objectivity of the audit process.

On the theme of holding to account, Audit Scotland endeavours to provide support to effective democratic scrutiny of how public money is spent and what it achieves. One of the most significant benefits of having the Scottish Parliament is that the process of holding public servants to account has become much more transparent, robust and comprehensive than it was before devolution.

On the related theme of helping to improve, we have been able to produce reports that have challenged but also supported improvements in public services in Scotland. The unique practice that we have in Scotland, with the support of the Audit Committee, of sometimes having baseline reports that identify the scope for improvement and then producing a follow-up report to the Parliament on whether improvements have taken place provides a real incentive for management to address areas of weakness quickly and effectively.

In parallel with that approach, I now require all the auditors of the individual 200 public bodies, as part of the annual cycle of audit activity, to work closely with management in those bodies without compromising their independence to address areas of weak management and poor performance.

I am happy to answer questions that committee members might have.

The Convener: Thank you. I add for the benefit of committee members that the report and corporate plan have already been considered by the Scottish Commission for Public Audit, with particular reference to budgeting for Audit Scotland in pursuit of its aims and objectives. Do members have questions for the Auditor General, or are there are points on which they would like to seek clarification?

Susan Deacon (Edinburgh East and Musselburgh) (Lab): In your comments, Auditor General, you referred to modernising the audit process. The corporate plan contains a number of specific references to a new modernised audit—a pilot is to be run in two councils. Can you elaborate on what that means and on the stage of development that the modernised audit has reached?

Mr Black: I would be pleased to do that. I will take the health sector as an example. For the current audit year—the financial year that has just ended—Audit Scotland has developed a priorities and risks framework, in which we have attempted to capture the major priorities for the health service and the major risks that we think the health service faces. We have done that in consultation with partner firms and have involved interests in the health service, to ensure that the document is accurate and focused on the real issues.

The document is made available to all the auditors and guides the work that they do in individual health boards. That means that the range of major issues—for example, all the work that is being done on pay deals and so on—is being addressed consistently in all audits. I hope and expect that that will have two beneficial consequences. First, the audit reports that are produced locally for individual health boards will be helpful in addressing and reporting on the issues of real concern to the local NHS management. Secondly, they will help to provide a more consistent framework for Audit Scotland, on my behalf, to produce overview reports that address consistently across the whole health service the key issues of the day in the service. We are rolling out our priorities and risks framework in the health service as we speak. We are piloting it in local government and, from next year, the approach will be rolled out across the whole NHS.

It is important that I mention the fact that we have reorganised Audit Scotland into specialist groups. We have teams of people, both in performance audit activity and in financial audit, who are expert in health service matters and local government matters. We will also have a team that is dedicated to central Government and agency work. That will give us a much better basis of understanding and knowledge and it will enable us to interact well and positively with local management, because auditors will understand their issues better. In turn, that will lead to more informed reporting to the committee. I like to think that the committee saw some of the initial benefits of the new approach in the briefing that it received a few months ago on the situation in Argyll and Clyde NHS Board, which was based on the pilot in Argyll and Clyde. I am confident that that level of rich information and knowledge will be available in the future.

The Convener: As there are no further questions, I thank the Auditor General for his briefing. The committee will note the annual report and corporate plan.

Section 22 Reports

10:28

The Convener: The next item on the agenda is on section 22 reports. I welcome Fergus Ewing and Mary Scanlon, who have joined the committee this morning because they have a particular interest in the item. I also welcome the witnesses to the meeting and thank them for the written evidence that they submitted prior to it.

The format of the evidence-taking session will be as follows. First, we will hear evidence from the colleges. West Lothian College is represented by Mrs Sue Pinder, the principal and chief executive, and Dr Tony Kinder, the chair of the board of management. Inverness College is represented by Professor John Little, the principal and chief executive, and Ken Mackie, the chair of the board of management. Lews Castle College is represented by Mr David Green, the principal. We will take evidence from the witnesses in the order that I have just set out. Later, after a suspension for a comfort break, we will hear evidence from the Enterprise, Transport and Lifelong Learning Department and the Scottish funding councils for further and higher education. I invite Mary Mulligan to begin by asking questions of West Lothian College.

Mrs Mary Mulligan (Linlithgow) (Lab): I will begin from what might seem to be the opposite of where you would expect me to begin, because I want to look to the future. Committee members have before them information regarding the financial difficulties that you have been experiencing. My colleague Margaret Jamieson will deal with the private finance initiative settlement, but I want to consider where we go from here. I am aware that the college has engaged Partnerships UK and that a project board has been established to consider the intricacies of the settlement and how it can be taken forward in a financially viable fashion that does not leave the college with deficits of one sort or another. What do you expect to come out of the on-going deliberations? What are your hopes for taking the situation forward?

Mrs Sue Pinder (West Lothian College): We hope that the work that is being led by Partnerships UK will lead to a mutually acceptable settlement that meets the requirements of all parties. As you are aware, the Partnerships UK board comprises members from the Scottish Executive, the Scottish funding councils for further and higher education, West Lothian College and HBG PFI Projects Ltd, the PFI provider. It is important to say that, whatever comes out of the Partnerships UK work, it has to be a resolution that meets everybody’s needs. We would like to arrive at a situation that enables our college to operate on a level playing field with every other college in Scotland. Whatever resolution emerges, it must not end up financially disadvantaging the college in a different way.

The work of the Partnerships UK board has been far reaching and we have considered the college's long-term strategic plans. You will be aware that West Lothian College has vision and ambition. Over the past four years, we have worked hard to manage the college effectively. We are trading at an operating surplus and have plans for the future. Indeed, we have imaginative plans for the way in which we would like to develop the infrastructure of the college and, this year, we have been supported by the Scottish funding councils for further and higher education in terms of capital allocation that will allow us to do that. All those issues are to be factored into the solution. We are talking not simply about a resolution of a financial contract, but about a future plan that will allow West Lothian's only college to move forward strongly and positively.

Mrs Mulligan: What are the barriers to your being able to take forward your ambitious plans?

Mrs Pinder: Obviously, the college has problems with the affordability of the PFI. It is no secret that the college has struggled to manage its contractual obligations to HBG. We regret that.

We have two barriers. One relates to cash flow, with which we have difficulties in relation to the PFI contract. The other barrier concerns the changes that will occur in 2007 to the funding support that the college receives from the Scottish funding councils for further and higher education, which will start to decrease their contribution to the availability charge—which is, effectively, the rent on the building—and cease to pay the VAT element of the facilities management charge.

Those figures come to around £4.2 million a year, which is a significant outlay. The gap that emerges, which the college has to meet, will be £11 million over the rest of the lifespan of the PFI contract. The original concept underlying the PFI contract was that the college would grow sufficiently to enable it to develop different areas of work that would generate surpluses to bridge that gap. Unfortunately, current further education funding policy has meant that the college has had no funded growth in line with that model, so there is limited potential for that to happen in future. That is a major barrier.

Mrs Mulligan: We will come on to discuss the funding of student numbers. I note from the college's written submission that it has already made changes to staffing and courses so that it can address the issues that have arisen. How might staffing, courses and student numbers be affected one way or another by the decisions that might be made in the future?

Mrs Pinder: On the staffing changes that we have made, it is fair to point out that we are now a very efficient college. The recent Scottish Further Education Funding Council publication shows that we made efficiency gains of 7 per cent in our staffing performance indicators. Although our premises costs as a percentage of total expenditure are running at a parlous 35 per cent, on all other indicators we are performing well.

Significant changes were made to our staffing profile not just to generate efficiencies but, primarily, to deliver a better service to our students and our client group. It is important to put on record that the college has at no time made staff redundant, although staff have left the college. We have undergone a significant restructuring, which was supported by the funding council, but we have not made staff redundant and we have no plans to do so in future.

Rather, we have tried to change the curriculum and the way in which it is delivered to make it much more flexible and accessible to people in the community. We have introduced a whole range of staff to facilitate learning and we have significantly developed our work with the inclusion sector. As Mary Mulligan will know, when the college was situated in Bathgate, the college building made it difficult to accommodate people with different abilities, especially mobility difficulties. Today, we have 550 students with learning needs. We have widened the curriculum and we have widened access. We will continue to do that.

A further barrier to developing the college's ambitious plans for such areas is the inflexibility in changing the college estate. That is because of the way in which the PFI contract is structured. That has been a difficulty, but the capital allocation that we received will help with that. We have ambitious plans to develop some of our teaching areas over the summer.

The Convener: Before I allow Margaret Jamieson to ask her question, I want to clarify something. You mentioned an £11 million gap over the remaining years of the contract. How many years are we talking about?

Mrs Pinder: The PFI contract runs for 25 years. We are just going into year 5.

The Convener: So we are talking about an £11 million gap over 20 years.

Mrs Pinder: Yes.

Margaret Jamieson (Kilmarnock and Loudoun) (Lab): My questions are also on West Lothian College's PFI contract with HBG. Does the contract contain any facilities for a refresh or update of the contract?

Mrs Pinder: Yes, but those can take place only at specific points within the contract life. For example, the first opportunity to refresh the facilities management charge, which is a significant charge of some £1.2 million to £1.3 million a year, will not come for another two or three years.

Margaret Jamieson: Is that built into the contract?

Mrs Pinder: Yes.

Margaret Jamieson: Does the contract allow changes to the estate? You said that the funding council had made funding available to make changes to the estate.

Mrs Pinder: We can make changes to the estate by working with West Lothian SPV Ltd, which is the special purpose vehicle that manages the college. We have a system whereby we put in a change request notice for work to be done, which is then carried out either by HBG or by one of its subcontractors. There was a successful example of that two or three years ago, when we developed an area in the college into what is now called the Hub, which is a one-stop shop for students. That was developed very well using that mechanism. Most recently, HBG has worked co-operatively with the college on costing our physical plans for new teaching areas. There is a process for doing that, but it is quite time consuming.

Margaret Jamieson: The briefing that we received advises us of the establishment of the project board, which includes the Scottish Executive, Partnerships UK and your PFI funder. It then indicates that, as you have said this morning, there might be a settlement or agreement later this year. Will you expand on what that settlement or agreement will be?

Mrs Pinder: It is difficult for me to go into detail, as the committee will understand, because the issues are commercially sensitive. However, we are considering a number of ways in which we might work more positively with the PFI, such as through cost savings, flexibility in the contract and different use of buildings. I hope that you will forgive me, but the issues are too commercially sensitive for me to go into any further detail and divulge any of the other options that we have discussed.

Margaret Jamieson: That discussion must be based on your reducing the amount of money that you have to pay.

Mrs Pinder: The discussion is based around best value to the public purse—that is an important point to make—so we need to explore what options for West Lothian College provide best value. Your point is right: the college does not wish to pay out more money than it currently does.

Margaret Jamieson: It was understood that a certain level of weighted student units of measurement would have covered the costs of the PFI but, since then, there has been a cap. What discussions took place with the funding council to identify what that would mean for your financial position?

Mrs Pinder: We have had lengthy discussions with the funding council since I took up my post as principal in 2001. It took me about six months to do the home study on the PFI contract but, once I understood what it meant for the college, I opened up discussions with the funding council. It is important to say that the people who are having the discussions—the current chief executive of the funding councils, Roger McClure, and I—were not around at the time that the contract was signed, so we came to it cold and had a steep learning curve.

I think that the funding councils fully understand the impact that the cap has had on the college from two perspectives: the financial perspective, which is the theme of your question, and, more significantly, the service that the college can offer to the people of West Lothian. We have a wonderful resource that has been extremely well constructed—the PFI procurement route has given West Lothian a first-rate college—but, on current levels of funding, the college is operating only to 60 per cent of its capacity. We have proven unmet demand in West Lothian and the funding councils know that. The college was built for growth; it was meant to be full and it is not. There are two sides to the debate: how the college can resource the payment profile of the PFI contract and how the college can be a thriving educational provider for West Lothian, which it should be.

Mr Andrew Welsh (Angus) (SNP): You seem to be saying that the PFI contract is a millstone round your neck. If that millstone were removed, what would the college be like?

Mrs Pinder: I am not so naive as to believe that simply removing the PFI contract would lessen some of the college's difficulties, because we would still have to resource and finance it. However, it would mean that the college would be able to plan more proactively. It is difficult for the college's board to undertake its strategic planning activity when there is significant uncertainty about how the college might be funded in the future. The removal of the PFI contract would also make a big difference to our flexibility to manage and change the estate. That would enable us to manage the college in the same way as every other college in Scotland. Unfortunately, at the moment our board meetings can be dominated by issues relating to the PFI contract, rather than to the strategic development of the college. The situation could be different.

10:45

Mr Welsh: Are you saying that if the PFI problem was resolved you could consider increasing the 60 per cent capacity and balancing your finances?

Mrs Pinder: We would be more able to do both, because we have demonstrated in our accounts that since moving to Livingston in 2001—when the college lost its only two major commercial clients, Motorola and NEC—we went from having no commercially funded activity to generating £1 million worth of commercial activity, which yields a significant surplus to the college. The answer to your question is yes; we would probably have a fighting chance of doing both.

The Convener: It is clear that the assumptions underpinning the PFI deal and the people involved in it have changed. What is your view on the PFI deal and what it has achieved? Are there lessons that other colleges might draw from the experience that you have had, given that you were trailblazers in that field?

Dr Tony Kinder (West Lothian College): We are grateful that West Lothian has a marvellous new college. We do not believe that it is the college board's job to make public policy or enter into debate for or against a PFI. Our experience is that we used to have a building that was failing and which was a major constraint on attracting students and serving the needs of local businesses. We now have a building that is potentially highly successful in meeting the needs of local businesses and students.

Many lessons have been learned. The first difficulty is that the size of the PFI contract has left no room for West Lothian College to manoeuvre within the contract to derive the efficiencies necessary to meet its financial obligations under the contract. The size of the contract is a major difficulty. Secondly, the structure of the contract was over-burdensome and, in effect, was the old model of public-private partnership that would not be entered into today.

Having said all that, we used to have a college that nobody would come to and we now have an attractive college that is capable of serving the needs of people in West Lothian.

The Convener: Mrs Pinder, you mentioned proven unmet demand. How did you ascertain that?

Mrs Pinder: We have done that in two ways. We now have an efficient recruitment and admissions policy; everything is tracked and we capture all the data. We know that every full-time place that we advertise could be given to at least four or five students and we have evidence of that.

When the college opened in 2001 it was difficult to predict what the impact would be. Some board members were nervous and wondered whether people would come—whether we would attract anybody at all—and whether we would be able to meet the 43,000 weighted SUM target that we were given as part of the strategic funding that the funding council gave us at the time of the move. I do not think that anybody anticipated what would happen. We had induction days and evenings and on one famous occasion I addressed about 800 people, although we had expected only between 50 and 100. You will understand that we were literally stowed out. We stopped recruiting that year when we hit 50,000 weighted SUMs; we were funded for only 43,000. We outturned at just under 54,000 WSUMs, which meant that roughly 10,000 WSUMs were unfunded. The college board took the view that we would live with that, because the alternative would have been to go round the classrooms and say, "You, you and you will have to leave, because we have no funding for you." We could not do that. The new building in Livingston had been much vaunted and the public had looked forward to its opening and received it extremely well, so we took the hit.

That is how we know that there is unmet demand. I have spoken to principals who have opened new buildings since we opened ours and there seems to be an interesting phenomenon in such circumstances whereby significantly more people than anticipated are attracted to the college. In our first year in the new building we overtraded by 10,000 WSUMs, because the board decided to honour the commitment that the college had made to those students.

As I said, we know about current demand because we have an efficient admissions system. The college is capable of delivering about 55,000 WSUMs in the forthcoming session and it has the physical capacity to take up to about 60,000 WSUMs, depending on how individual students approach their learning.

The Convener: You are currently funded for a little more than 43,000 WSUMs. What are your current numbers?

Mrs Pinder: If you are asking about current student enrolment, there are probably about 7,000 full-time equivalents, but that figure represents about 12,000 individuals, because some people attend part time or study through open learning.

Susan Deacon: You gave a full explanation of how you identify that there is demand for places. Will you comment on any discussion that has taken place, particularly with other agencies, about the need for further education provision? There is significant growth and expansion in the Lothians and skills needs are emerging in different sectors of the economy. Do you factor such matters into the discussions that you have with the funding council and others?

Mrs Pinder: Absolutely. The fact that we do so is reflected in the composition of the college board of management, because we have sought to include key members from different sectors. The college's curriculum portfolio is unrecognisable from the portfolio that it had when it was in Bathgate. At that time, the college had a strong reputation for its work with the semiconductor industry, but regrettably that industry is dead. As you can imagine, the industry's demise had a great impact on areas such as engineering and technology. We had to re-engineer the college, so we started by running a strong marketing campaign. We work in close partnership with West Lothian Council and the West Lothian Chamber of Commerce and we have advisory groups and employers' sessions for all the college's curriculum areas. We changed our curriculum portfolio and do far more workforce development, through work-based learning and work in the community. We introduced programmes in retail and logistics and developed support for service industries. We significantly developed our creative industries section, which includes music technology. Our approach to all those areas is based on well-gathered market knowledge and liaison with the various agencies. The current curriculum bears no resemblance to the curriculum in 2001.

Susan Deacon: How do you feed that information into your discussions with the funding council?

Mrs Pinder: The funding council receives the college's strategic and operating plans every year and we produce on CD-ROM full documentation of everything that happens in the college, which includes the specific objectives that the college has met and examples of the college's work. The evidence is available for everybody to see.

The Convener: I thank Mrs Pinder and Dr Kinder for their evidence. If the committee wants to clarify any matter with you—or any of the witnesses—we will write to you.

We move on to consider Inverness College.

Eleanor Scott: Good morning. You have a recovery plan. You predicted that in 2003-04 there would be a surplus of £94,000, but that turned into a deficit of £526,000. What is your position with regard to your current recovery plan and how can we be sure that there will not be another deficit?

Professor John Little (Inverness College): You have the briefing paper. It is regrettable and unfortunate that the college was not able to meet its budget in 2003-04, the year in question. The briefing paper provides the background to the very difficult financial situation that the college was and largely still is in. The briefing paper refers to the financial recovery plan, which was instituted with SFEFC in 2000. I came into post in 2002-03 to a college that at that time had somewhere between a third and a quarter of the entire further education sector debt on a turnover of £12 million. In 2000, the debt was largely historical. There was an accumulated debt of £5.26 million and an advance of grant-in-aid of £1.5 million from SFEFC, which, compounded, produced a total debt of £6.76 million. That was a huge challenge for a new principal coming into post.

A recovery plan was and is in place. It is structured to eradicate the debt over a period of 10 years. There are another four or five years to go. The recovery is predicated on producing an operational surplus annually that will meet the target repayment for the year. Depending on whether it is a low or a high payment, we talk about being on the floor or at the ceiling of the debt programme. In the year in question, 2003-04, with the outturn being disappointing, we fell behind in respect of meeting our recovery commitments.

You have also asked how we can guarantee that the situation will not deteriorate. It is regrettable that we are in this situation. Perhaps it would be helpful if I explained the reasons behind the disappointing outturn in 2003-04. I describe those briefly on page 2 of my briefing paper to the committee. There are two aspects. First, there was an unanticipated strong in-year demand for non-advanced craft programmes, particularly in construction but also in care. Those two areas have experienced incredible growth at Inverness College. In construction, the growth has been 50 per cent over the past three years and in care the growth has been 30 per cent. It is becoming very difficult to plan provision for subjects in areas of such high growth, particularly when the demand comes in-year. That is especially the case in construction, and it was especially the case in 2003-04, although I have to say that that is continuing this year and if it were left unaddressed it would continue in the future. As a responsive college, in 2003-04 we met the demand. We recruited supply staff in order to teach the programmes and that obviously had an impact on the staffing bill for that year.

11:00

The second and more fundamental issue about financial performance in 2003-04—it would continue to be an issue if something were not being done about it, which I will describe—is the college's historically relatively low levels of efficiency in the deployment of staff, particularly academic staff. The staff themselves are not inefficient, but the way in which they have historically been managed and deployed has been inefficient. When we make comparisons across the sector, it is clear that Inverness College has much ground to make up.

Since 2003-04 we have addressed both issues and we continue to do so. First, on our in-year response to unplanned demand for courses in construction and care, for example, we have had to learn to say no—it is as simple as that. I am afraid that unmet demand must remain unmet until there is greater flexibility above the cap in relation to the unfunded activity that the principal of West Lothian College described. Inverness College is in the same position as West Lothian College in that regard.

Secondly, on the more fundamental point about efficiency, our staffing budget approaches £10 million, so in order to meet our efficiency targets on the deployment of academic staff I have had to consider academic staffing levels very carefully. We will enter 2005-06 with a reduced academic staffing complement, which is more in line with the activity for which the college is funded. The financial forecast that we are preparing to submit to the funding council reflects that and shows an outturn of an operational surplus in 2005-06, with respect to meeting the depreciation charge. The outturn this year is still a prognosis, because we have not reached the end of the financial year, but the prognosis is that the historical cost surplus—without taking depreciation into account—will show about a five-fold improvement on the 2003-04 outturn, so improvement is already coming through.

In my paper, I said that the college and board are optimistic for the longer term. That optimism is based on sound financial management, prudence and planning, which will go hand in hand to help the college to meet the financial targets that we outline in our financial forecast to the funding council. However, there is a considerable challenge ahead for the college.

Eleanor Scott: Colleagues who represent Highland constituencies will probably want to pick you up on some of your comments. Before they pile in, I want to ask about the effect that the UHI Millennium Institute is having on the college's finances.

Professor Little: It is important that Inverness College is a partner, along with Lews Castle College and 12 other colleges, in the UHI Millennium Institute and that those partners are working together towards achieving degree-awarding powers and university title. The project is ambitious, but I would not have chosen to be the principal of Inverness College if that had not presented a challenge. Some people might regard the aim to create a university from a number of incorporated FE-HE colleges as preposterous, but we are in danger of succeeding and I genuinely believe that we will deliver university title in 2007.

Inverness College has had to transform itself from what was a few years ago an FE college that delivered higher national qualification work, into an FE-HE college that runs undergraduate and postgraduate degree programmes, so a transformation in the curriculum had to take place. Our curriculum is quite different from the curriculum that the college had just three years ago. There has also been a transformation in perceptions and expectations and in how staff are developed to take on the new challenges. There will always be challenges and tensions as we work on one matter while trying to deliver another. The greatest challenge for Inverness College is how we manage with what we are allocated, given what we are expected to achieve in a few years' time.

Eleanor Scott: You talked about the different nature of what is offered at the college and about the need to reduce the number of staff to achieve the financial position that you want to be in. As you know, I am a Highlands and Islands MSP and one part of the college about which I have had correspondence is the Scottish school of forestry. There is a perception that a blanket reduction in staff is taking place, although staff do not want to go, stakeholders do not want them to go and staff seem to be offering something that is unique and valuable. Will you comment on that?

Professor Little: I do not want to go into too much detail on individual departments, because discussions are continuing with staff members in some departments to secure the savings in staffing costs that I indicated. However, as I have indicated on a number of occasions, forestry has a very good future at the college. We are the course leader in delivering the BSc in forestry and conservation. It is an important academic component of the UHI curriculum and I have given assurances that it will continue.

However, I had to see where the greatest efficiencies need to be made. I had to look throughout the college's broad curriculum areas in both further and higher education. I assure you that we spent a lot of time looking carefully at what is delivered and what will continue to be delivered so that there is minimal damage to the curriculum, not just in the UHI and higher education but in further education as well.

Mr Welsh: You said that your financial forecasts were knocked askew because of unplanned demand. Why were you taken by surprise? What information systems do you have about potential growth areas?

Professor Little: That is an interesting question. We were taken by surprise, even though we have good market intelligence. We have to own up to that. I give an example. This year, there was a north Highland construction forum initiative, which involved a number of the UHI colleges that deliver construction programmes. We were unaware of that initiative at the beginning of the planning cycle. It came to us as a funding council initiative—the funding council should be applauded for that. However, it is not something that we could have built into a three-year forecast. We had to think carefully about whether we could afford to take part in the initiative, given that it involves appointing staff for the funding period of one year. We had to take a view on that and engage in a discussion with the funding council about the prospects if we did take part.

Mr Welsh: How well do you know your potential markets? You say that you have good market intelligence, but how exactly did you produce that? Clearly, it went wrong in the past.

Professor Little: How did we produce what, exactly?

Mr Welsh: How did you produce market intelligence and understanding of where your actual and potential clients are?

Professor Little: We know where our clients are, not just in construction and care but in other areas too. The college has been operating successfully for 40 years. The market is relatively local and is found in Inverness, although it has a national dimension, particularly in construction and care, on which we deliver throughout the Highlands and Islands. Market intelligence is gathered formally through a linkage between the academic managers, the heads of school, ourselves as the senior management team and the director of marketing. Formal curriculum reviews are undertaken every year for part-time and full-time courses in both further and higher education. Those reviews are gathered together annually and we take a forward look on the curriculum. In 2003-04, because of the buoyant employment and training situation in construction and care in the area that we serve, we were taken by surprise.

The Convener: I compare some different points of evidence that we have before us with regard to Inverness College. In 2003-04, the college received grants in connection with UHI of £2.3 million. That funding was expected to support 1,029 full-time equivalent students. However, the level of activity that was achieved was 970 students. In the same year, you attracted the equivalent of 2,000 weighted SUMs more, which you say caused you an opportunity cost of £300,000. Is it the case that the college is orientated towards meeting the wrong demand?

Professor Little: No, what you are talking about relates to the competitive tension that I was alluding to earlier. Now that we are funded through two funding councils, we have lost the flexibility that we had to meet any unplanned in-year demand for further education or higher education. Previously, if demand for higher education increased and we were in danger of exceeding our capped target numbers, we could adjust the FE side or, if it were the other way around, we could adjust the HE side. We are funded through two streams—FE activity is funded by the Scottish Further Education Funding Council and HE activity is funded by the Scottish Higher Education Funding Council—with quite different funding methodologies. Further, the two councils describe the unit of resource differently; there is a weighted SUM for FE and an FTE for HE.

The figure that you have referred to relates to the position at the beginning of the academic session around August and September. We have since pulled back from that position and the resource-allocation model that is operated through the UHI executive office has been recast and remodelled to reflect that gain in terms of our position. However, even when you know your market and have a good record of planning, as we have—especially in relation to higher education numbers—you can be caught unawares. Everyone in the higher education sector is aware of that because of the sector’s volatility and the cyclical nature of demand.

Eleanor Scott: You say that you know about the demands in terms of higher education, but there have been problems in that regard. For example, students have started their degree courses and then found that they were not being validated and have had to have places deferred. Further, there has been a lack of development for the proposed forestry degree, which was held up for about 18 months, as I understand.

Professor Little: With respect, I would take issue with that to a degree. As part of the challenge that we face in moving from the further education sector to a situation in which a quarter of our business is from HE courses, we are being asked to develop quite a bit. We have to be absolutely sure not only that we meet the market needs and have staff who have the necessary expertise and qualifications, but that everything is properly quality assured. The hold-up that you are referring to could well have been a quality-assurance issue that has now been rectified.

Mr Welsh: You said that the FE sector can be caught unawares. However, having worked in that sector, I know that it can also plan ahead properly. It worries me that not only have there been problems with student recruitment but that you will be unable to clear the accumulated deficit by 2009 under present estimates and that, since 2003, income has risen less than expenditure has. You have said that your financial forecast for 2005-06 will be all right but, compared to past forecasts—which you got wrong—how robust is your financial forecasting now?

Professor Little: As Sue Pinder said about West Lothian College, we could take a lot more FE students. Unfortunately we are not being funded for that and, if we took them, we would be moving into an overtrading situation, which we need to avoid doing.

A financial forecast has to be based on the establishment of robust financial management systems, which we are confident are now in place. At the heart of the issue is a reduction in the staffing bill, as I have indicated. When we get that right, the financial forecast will turn out right as well.

The Convener: Check against delivery, as they say.

11:15

Susan Deacon: We appreciate that the situation at the college has quite a lengthy history, much of which you have clarified for us this morning. You inherited some challenges and a big job of work must be done to turn the situation round.

What is being done within the college to build the capacity, both at executive and non-executive level, to address some of the challenges that you have set out. The challenges are partly to do with financial management, but they also involve significant organisational change and require significant managerial issues to be addressed to ensure that the financial situation is turned round. How are the managerial capacity and the skills within the management team and the board being developed to address the challenges? I have a second question in a similar vein: how are you working with staff and the student body to work through this period and into the future?

Professor Little: Ken Mackie will pick up the question as it relates to the board. On the capacity of the executive, what can I say? I took a long, hard look at the executive team when I came in during session 2002-03 and I made the changes that I believed were necessary then. There have been a few adjustments since then. As I mentioned, those include a more recent appointment of a director of marketing and a new appointment of a director of finance and commercialisation. We see the exercise as one in which we have to not only make cost savings but develop other income streams. I believe that there are some commercial income opportunities that, in the past, the college has not taken. We intend to address those issues as the next stage of the process.

Ultimately, the students are the most important thing. I try to meet and consult students formally and informally. I meet them informally whenever I can and formally on committees on which I serve. I consider their contribution and input to be important and valuable, and I always take note of it. Perhaps we ought to consult the students more, but rest assured that the best interests of the student are always at heart.

Susan Deacon: You have not commented on how the staff are helping to shape the process and to develop and deliver solutions.

Professor Little: You are right that I did not mention them—I am sorry; I should have done.

I will give the example of the recent exercise, which started at the beginning of the year, to deliver a staffing profile that is consonant with the levels of funding of which the college is in receipt for both further and higher education. The exercise has taken as long as it has because we have been scrupulous in involving staff in a proper, full review and consultation process at every stage. We have been assured formally and informally by other college principals and by the funding council that the process has been proper and full and that it was necessary.

Eleanor Scott: You say that you have scrupulously involved staff. Is it not the case that the staff passed a vote of no confidence in the management in May?

Professor Little: The vote of no confidence was from one of the four recognised trade unions at a branch meeting at which somewhere between 5 and 10 per cent of the total staffing complement were present. I do not know who voted for or against the motion. I was not invited to attend.

The Convener: You talked about having a smaller academic staff complement. Will that be achieved by redundancies or through natural losses as people move jobs? What, if any, are the implications for pension costs and how might that affect the balance sheet?

Professor Little: We have had to consider that carefully. Your first question was about redundancy and retirement. A combination of the two will be used. In the current exercise, I am pleased to say that following full consultation with staff, we have by and large attracted the required number from those who have expressed an interest in retiring or being made voluntarily redundant. The cost of that will be borne from money that the funding council has provided to ensure financial security. That is in a designated reserve and has been fully costed for our financial forecasts and affordability.

The Convener: What about the pension impacts?

Professor Little: We have had to examine the age profile, because that has a financial implication, as the committee will appreciate. It is more expensive if those in whom we have an interest in releasing are just 50, rather than 59, but the impact is minimal.

Mr Welsh: Provided that the college makes operating surpluses from one year to another and thereby meets its pension liabilities, the pension provision will not be a major concern in considering the college's viability. Will you make such operating surpluses?

Professor Little: Yes.

Mr Welsh: How can you improve college services by reducing staff, unless you have a major reconfiguration of services for customers? Reductions in staff have been mentioned several times. How will they improve the services that the college offers?

Professor Little: I hope that I have argued that the staff reductions are necessary because we are out of kilter with the efficiency norms for the sector.

Mr Welsh: What does that mean?

Professor Little: The sector measures efficiency in the deployment of academic staff as a ratio of the weighted SUM to the full-time equivalent academic staff member and Inverness College is well down the league table for that.

Mr Welsh: I thought that the aim was to put teachers in front of students.

If your director of marketing succeeds, will that create a headache for your director of finance?

Professor Little: Possibly.

Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP): As Professor Little knows, I have met him and Roger McClure—who I see is here this morning—as well as the principal of UHIMI and other staff for about 15 hours in the past three months. I know how complex and difficult the problems are. That said, although a financial formula must be applied, we all recognise that we are dealing with the futures of young people and families. The victims of any mismanagement would be students, staff and courses.

I will follow up four aspects. Professor Little just said that the college's performance has been out of kilter with efficiencies in the sector. Did you not inherit in 2002 a figure for weighted SUMs per FTE of 330? Has that efficiency benchmark deteriorated in your period of office to 284? Furthermore, has that not been contrary to the trend in the average, which has been to increasing efficiency in the same period?

The Convener: Do you intend to put all four points now?

Fergus Ewing: I would prefer to make them one at a time, which would be easier.

Professor Little: It is true that the measure of efficiency was 330 weighted SUMs per FTE in the year that I came into my post and it is currently 284. When we have completed the current improvement exercise, the figure efficiency will be in the order of 310, but we will still have a way to go. That is a measure of how far we fell behind, historically. Such figures fluctuate year on year. However, as I said, there has been an historical trend, which goes back a number of years. You mentioned one year, but I could mention other years from further back. The issue is difficult.

Fergus Ewing: I appreciate your candour in admitting that the figures that I have obtained from staff are correct. Do the figures prove that, although the rest of the sector is becoming more efficient on average, Inverness College's performance, as measured using the efficiency benchmark, has, unfortunately, become less efficient in your period of tenure?

Professor Little: In the short time that I have been in my post, I have made it my duty to ensure that the college is efficient. However, it is clear that we need to make ourselves more efficient, which is exactly what is being done.

Fergus Ewing: I will move on. You said that you have been "scrupulous in involving staff". Why did you therefore suspend the joint body that dealt with consultations between academic staff and management?

The Convener: I do not think that that question is germane to our inquiry. You should move on to your next question, please.

Fergus Ewing: I thought that the question was germane, as Professor Little said what I quoted in giving evidence. The information that I have received from staff is that that was not the case.

The Convener: We are not here to deliberate on the principal's scrupulousness in involving staff.

Fergus Ewing: Professor Little said that in his evidence, convener, but I will move on.

Eleanor Scott raised the issue of the financial relationship between Inverness College and UHIMI. Of course, that body's aim, which we all support, is to become Scotland's next university—the university of the Highlands and Islands—which is a challenging and difficult task that nobody underestimates; indeed, the task is perhaps more difficult than people realise. Currently, HE colleges in the UHIMI area are contributing expenditure towards UHIMI's administration, running, developmental and other costs. In other words, contributions are being made from your income. It seems to me that such contributions are not being matched by other colleges in Scotland, as there is no other aspirant university body such as UHIMI. As Professor Little knows, I have spent many hours trying to unravel exactly what the contribution is, including in a helpful meeting with

Mr McClure, but we do not seem to have got to the bottom of the matter. Auditing is a nitty-gritty process and I thought that we would try to get at the facts. Therefore, I have a fairly simple question for Professor Little. What percentage of your budget goes towards UHIMI and establishing Scotland's next university rather than the running of your college per se?

Mr Kenneth Mackie (Inverness College): Perhaps I could deal with that question. The funding of the college changed some two years ago—I think that that matter was discussed earlier. The further education element of the college's funding now comes from the Scottish Further Education Funding Council and the higher education funding part comes through the UHI Millennium Institute. I think that the change that has taken place has led to confusion about the funding elements.

I would not concede that there is a contribution from the college for the development of the UHI. An increasing level of funding has been made available for the UHI through the Scottish Higher Education Funding Council, and it is now at full level with other higher education institutes. The issue is beginning to resolve itself, but there is a lack of clarity about which elements are being funded. Of course, staff in the college work between FE and HE and therefore it is difficult to break down the costs between the two.

Fergus Ewing: That is helpful. Ken Mackie says that more clarity is required. I did not ask about income, which I accept has been met by increases—I asked about the expenditure position, which we need clarity about. Will Professor Little confirm that, over the past three months, the college and UHIMI have not reached a common view on the contribution from expenditure that is being made by the college to UHIMI? Is it factually correct to say that there has been no consensus on that matter yet?

11:30

Professor Little: We have only recently formally established a budget for next year, if that is what you are alluding to.

Fergus Ewing: No. I seek clarity where Ken Mackie said there is none. Have you or the principal of UHIMI established a common figure for the college's contribution to UHIMI?

Mr Mackie: There is no contribution from the college to the UHI Millennium Institute. The UHI Millennium Institute funds the higher education students whom the college delivers and the Scottish Further Education Funding Council delivers the cash for the further education element of the college. We are trying to deliver the two from within one area, but the college is not funding UHIMI.

Fergus Ewing: Perhaps I can bring evidence to the committee about that later.

The question of the new build came up at my meeting with Professor Little, when I believe that he stated that it is the aim—an ambitious one, I think—to relocate the college to a green-belt site perhaps by 2009. That aim has broad support, but the staff have put it to me that that would be financial suicide given the financial position of the college. The college has taken on an estates manager to oversee the project at a cost of around £30,000. You say that the staff have been consulted scrupulously, but they say that the city centre site could be used—it has development potential and it is cheek by jowl with the learning resource centre. Might it not be sensible to think again about the move and the timing? Do you think that the estimated £2.3 million that you are going to spend on the current building is justified if you are planning to move out within four or five years?

Mr Mackie: The college is working out of four sites in Inverness city. One is a building in the commercial centre of the city that was built in the late 1960s and now needs quite a bit of maintenance. One is an old school that dates back to the late 19th century and another is a building that is used as a management centre. That building is being closed and the business is being transferred to the other buildings. For the efficiency of the college, we feel that a new build will be beneficial and will lead to revenue savings in the running costs and maintenance of the buildings and because we will not have to move staff and facilities between two sites. We have gone through that issue.

The Longman site is within the commercial centre and does not have a lot of room for expansion. The only way in which we could expand would be by buying up land round it that is occupied by other commercial buildings, or by building over the car park. Whichever way we did it, it would be difficult to maintain services within the other buildings. The concept therefore has to be to move to a new site that could absorb all the occupants of the current buildings.

Fergus Ewing: I mentioned to Ken Mackie and Professor Little in previous discussion that my understanding is that there is to be expenditure of £2.3 million, which is far in excess of the savings that are being sought from staff redundancies. If that expenditure is not necessary, not making it might alleviate some of the pressure on staff and courses. I asked that at my meeting with Professor Little and I have not really had an answer. I am told that that £2.3 million is necessary because of health and safety measures, but it is for expenditure on a building that you have said that you hope to vacate in the next four or five years. I do not know all the ins and outs but from a commonsense, layperson's point of view, I think that spending £2.3 million on a building that you intend to vacate in four years is something that should be avoided.

The Convener: Can you get to the point, please? We are running out of time.

Fergus Ewing: Have Professor Little, Ken Mackie and the management team looked at the issue again? If not, will they do so to see whether staff jobs can be saved by cutting down some of the expenditure involved?

Professor Little: The programme has been looked at again, not just following the meeting that I had with Mr Ewing, and it has been discussed and approved by the board. A programme of only essential capital works to maintain the estate, as described by the chairman, will be enacted over a period of two or three years. The cost is not the £2.3 million that was indicated, and it will be borne by funding that is now available from the funding council for capital maintenance and repair, which was not available at the time the plan was formulated.

Mary Scanlon (Highlands and Islands) (Con): One of the problems, or benefits, of coming last is that all the questions that I wanted to ask have already been asked. Susan Deacon has asked my main question. I will be brief. First, I declare an interest. I was a lecturer in economics in further and higher education at Inverness College. I was one of the voluntary redundancies in 1994—

Margaret Jamieson: They are still paying for it, Mary.

Mary Scanlon: Fortunately, I found another job. I put on record that Inverness College received one of its best Her Majesty's Inspectorate of Education reports recently for its excellent standard of teaching. This is the third call for redundancies in the past 10 years, which does not help the morale of staff, many of whom are my friends.

I have two points to put to the convener before asking my question. First, the lecturers at Inverness College who teach university degrees and higher national certificates and diplomas teach 24 hours a week. No other university lecturers in Scotland are expected to teach 24 hours a week, so the commitment that is required of those members of staff is horrendous. Many of them are studying for masters degrees on top of their commitment to teaching. Convener, should the committee examine funding for colleges such as Inverness College, it should be aware that they will never achieve the economies of scale that colleges in major cities will achieve, particularly given that one or two outreach centres have closed recently.

Secondly, where there is huge demand for courses, for example in construction and social care, there seems to be little flexibility within the college to find the funding to meet the level of demand. That has been a problem not just for Inverness College but for West Lothian College.

I am not sure whether I missed it when Susan Deacon and Andrew Welsh asked their questions—I will read the *Official Report* carefully—but as an individual I find it difficult to understand how a successful recovery plan can be based on fewer lecturers offering fewer courses to fewer students, which results in less income. I have never been able to square that. Many people in Inverness and the Highlands are concerned that many other training providers may come in to fill the gap, but the provision in, for example, construction will not be of the quality that the college provides, given the excellent report that Inverness College received.

It is essential that there is good will and a positive partnership with the staff in order for the college to move forward and be successful and financially viable in future. I am not going to pursue Fergus Ewing's line of questioning, but I want to ask Professor Little what has been done to build bridges with staff and the trade unions following the vote of no confidence in the college principal and management last month. That is crucial to moving forward.

The Convener: Of course, as a committee we are not giving evidence; we are seeking evidence, so it is not for us to answer the points that you put to us. However, they are on record and you have brought them to the fore for our deliberations.

Mary Scanlon: I was not asking you to answer.

The Convener: We will park that and note that information. You have raised two issues that I will give Professor Little the opportunity to address. The first issue is how the recovery plan—which seems to suggest that less is more—can deliver. The second issue is the extent to which the plan is reliant on staff good will and what is being done to achieve that.

Professor Little: We are doing everything that we can. As I stated earlier, we have genuinely engaged in a full consultation with staff. Because of its fullness, the consultation has taken a long time. However, we believe that the process has been necessary to achieve the engagement, the buy-in and the good will of staff.

As in all difficult exercises such as this, some staff will feel threatened and will not be able to see the benefits of what is being undertaken for the long-term financial viability and health of the college. They will have a point of view and will usually be willing to express it. However, we have done, and will continue to do, everything that we can to work with staff to ensure the good will and positive partnership to which Mary Scanlon has alluded.

On how successful recovery can be based on fewer staff delivering fewer courses, although I said that the recovery would have to be predicated on fewer staff, I also said that we have taken a careful look at the curriculum and that the measures that are being implemented have regard to the health of the curriculum and its continuation, not its demise.

The Convener: Thank you. With the committee's agreement, I draw to an end the evidence from Inverness College. Thank you for that evidence. We will seek further information from you on several points.

I welcome the very patient David Green, who is the principal of Lews Castle College. He is here to give us evidence on the predicament that Lews Castle College faces. We have received significant evidence concerning how the current financial position has come about.

Margaret Jamieson: In your written submission, you talk about the significant additional and unavoidable costs that are attributed to the provision of university-level education. You also mention your estates, your library, your learning resource and staffing. How do such matters impact on the issues that you believe are specific to Lews Castle College in terms of remoteness, and how did that influence your discussions with the funding council?

Mr David Green (Lews Castle College): There are significant additional costs. As has been alluded to this morning, the delivery of university-level education brings a number of costs that are unavoidable if the quality of provision for the students is to be comparable to provision in the rest of the sector. I have outlined some of those costs in my submission. The key cost is staff costs. In order to permit the teaching of courses up to and including degrees, masters degrees and, increasingly, PhDs at Lews Castle College, we must ensure that staff have time for the research and scholarship that allows them to do that job. That is a major issue for us, but against that we must weigh the benefits of our being part of the UHI, both to the institution and to the community that we serve. The benefits are huge. As has been alluded to, they are so significant that everything that we can do to ensure that the UHI is successful must be done.

11:45

Historically, funding in respect of remoteness has been an issue in further education only in as much as there are, by any current definition, no universities in remote areas in Scotland. It has not previously been an issue. However, there are colleges that serve a lot of remote areas of Scotland, whether they be islands or other remote rural areas. There are 12 colleges that receive some element of remoteness funding from SFEFC, but no universities receive such funding. Until recently, with the bringing of the UHI into the formula of funding for higher education and the merging of the two funding councils later this year, it has not been an issue.

At Lews College Castle, 35 per cent of our teaching is in higher education, so only 65 per cent of our business receives any kind of remoteness funding. Were the rest of our business to receive a similar or equivalent level of funding, we would be a great deal better off and able to offer much better services.

Margaret Jamieson: Your submission says that you made an application to the funding council for additional remoteness funding. What was the basis of that and how did you define the term "remoteness"?

Mr Green: The process was very complex and it has been a long time since we started the dialogue with the funding council. Probably the best way to refer to it is within the framework of the remoteness review that the funding council initiated some 18 months ago to try to identify, as closely as possible, the factors of cost that are genuinely attributable either to remoteness or to serving a very sparse population, in the context of social inclusion and other issues that relate to that.

We have done a considerable amount of work in the local context on behalf of the island colleges, which include Shetland College, Orkney College and, increasingly, Argyll College, to identify those costs. We have done that by comparisons with other public sector costs. There are obvious comparative costs for secondary education, but there are also comparators in health and other services. We have engaged consultants to advise us on the true costs of delivering a public service in an area that is both remote and, more important, rural with a very scattered population. We also contributed to the short-life working group that the funding council convened—I was a member of that group—the outcome of which has been a review and, more recently, decisions on additional remoteness funding specifically for the island colleges.

Margaret Jamieson: You are saying that there will be specific funding for island colleges.

Mr Green: Yes, in recognition of their extreme remoteness—I think that is the term that is used.

Margaret Jamieson: Are you saying that there are two levels of remoteness allowance, with the island colleges receiving the higher of those because there is an assumption that they are the more remote, and a group of colleges that are remote and are receiving the lower level? There are also the colleges in conurbations.

Mr Green: Yes. There are, in fact, three levels of remoteness.

Margaret Jamieson: Oh, there are three. Right. Explain that to me.

Mr Green: The levels are remote; very remote; very remote and island.

Margaret Jamieson: In other words, the money is not enough to address the particular issues. You are serving a very remote, sparsely populated area of Scotland, which brings certain difficulties. Do you believe that the funding council wholly understands the difficulties that your college faces?

Mr Green: That is difficult to say. I am confident that the funding council has done a great deal of work to understand the difficulties. In doing so, it has covered all the issues that need to be addressed in considering remoteness funding. From the position of somebody who is trying to manage a college that is in the geographical and social position that Lews Castle College is in, I would say that what we get is never quite enough; however, somebody like me would always say that.

We could do more if we had more. We could provide better quality services if the funding was a bit more comfortable than it is even under the new arrangements. Certainly, we would always question the level of remoteness funding that we receive, given the job that we are trying to do. In particular, trying to deliver a part of a university in waiting is a challenge that nobody has had to undertake before, and the costs of that are considerable.

Margaret Jamieson: In terms of the university provision that you are providing, is there a link with mainland universities via remote access or whatever? Is there a sharing of that? That may well assist.

Mr Green: We work closely with other universities, sometimes through formal arrangements but also through less formal ones, and we benefit from shared expertise. The Open University is one of those universities and the universities of Aberdeen, Strathclyde and Edinburgh are also part of the partnership. We benefit as much as we can from those arrangements in terms of shaping UHI.

In terms of how we deliver courses and learning to students in remote communities, it would not stretch the point if I were to say that there is probably more expertise in UHI and specifically in Lews Castle College, which I run, than there is in any other university in Scotland other than the Open University. Given that we are the only people who have to do things in the way that we do them, we have had to grow the expertise. It is difficult and complicated to do so; considerable infrastructure is required to teach students remotely.

Margaret Jamieson: Okay. Thanks.

Susan Deacon: I have some information on which you may or may not feel able to comment. I stress that I raise it in the interests of contextualising the comments that you have made this morning.

I am continually struck by the particular issues and challenges that very remote and island communities face in the delivery of a range of different services. Of the three island colleges, I note that Lews Castle College is the only one to become incorporated; the others remained under local authority control. I am interested to know how that affects the context in which you operate and the college’s decision-making processes.

For example, I note that

“Lews Castle College began to alert the Scottish Office to future funding problems in 1997.”

If the relationship had been closer and more localised, would the communication have run more smoothly? Would things have moved to a conclusion more quickly?

Mr Green: I think that that would have been unlikely. Benefits have accrued to Lews Castle College as a result of its becoming an incorporated college in 1993. I draw that conclusion partly because I have seen how we have been able to develop since then. Before incorporation, we were already somewhat larger than the other island colleges in terms of scale, student numbers and so on. Since incorporation, we have developed considerably. Although we have had to face very real problems because of incorporation, we have also benefited from it. We are the smallest general further education college in Scotland, which brings all the challenges that a very small institution finds it difficult to meet.

I am not in a position to judge whether we could have reached an arrangement on funding if we had been part of a local authority—I can only guess at that. In order to ensure that the needs of the community that we serve were met, we have done a good job of lobbying and working effectively, first with the then Scottish Office and subsequently with the funding council and the Executive. I am afraid that that is all I can say in response.

Susan Deacon: That response is helpful. Given that the three island colleges operate in different environments, what level of liaison and communication do you have with the other two colleges? I assume that a fair amount of sharing of experiences and learning can be done despite the different ways in which you operate.

Mr Green: We have an informal group—the island colleges group. It is a select group, as the member will understand. The group meets regularly and frequently to discuss issues that are common to each college as separate institutions and because we are part of the UHI Millennium Institute.

Until recently, one of the issues on which we lobbied and worked together was remoteness funding. In other work, we seek to maximise the benefits from, for example, European funding. Currently, we are working on collaborative projects that draw together the island colleges group into an application for future European structural funds. We see benefit in doing that.

We also work closely together by sharing courses. We have students in Stornoway and elsewhere in the Western Isles who are students of Shetland College or Orkney College and vice versa. Although we would do that anyway as part of the UHI Millennium Institute, there is close collaboration among us.

The Convener: I have just one question in closing. I understand from evidence that, in December 2003, the college's poor financial position led the college's bankers to withdraw your overdraft facilities. Do you still operate under that constraint?

Mr Green: Yes, partly because we have not been back to ask for the constraint to be lifted. The cash position of the college is currently healthy. If we were to go back to the bank, I think that it would restore our overdraft facilities. We have not pressed the bank on that point, however.

The Convener: Thank you. As committee members have no further questions, I thank you for your evidence, Mr Green. Indeed, I thank all the witnesses for their perseverance under fire. I suspend the meeting for just over five minutes; we will reconvene at 12 o'clock.

11:56

Meeting suspended.

12:07

On resuming—

The Convener: I welcome the witnesses for the second part of our evidence session. Our first three witnesses are from the Scottish funding councils for further and higher education. Roger McClure is the new organisation's chief executive, Brian Baverstock is deputy director of governance and management appraisal and policy, and Riona Bell is director of funding. Eddie Frizzell is head of the Scottish Executive's Enterprise, Transport and Lifelong Learning Department and is accompanied by Aileen McKechnie, who is head of the Executive's further and adult education division. Thank you for attending today's meeting and for providing us with written evidence. We intend to go on until 12.30 or perhaps a bit later, depending on how we get on with questions. Most of the questions will be about what we have been told today rather than about the written evidence. I invite Eleanor Scott to ask the first questions.

Eleanor Scott: In your submission, you say that you have had "frequent discussions" with Inverness College

"about actions to put its financial recovery back on track."

Will you share with the committee what you talked about in those discussions? Are you confident that the college is back on track and that its financial position can be recovered?

Mr Roger McClure (Scottish Funding Councils for Further and Higher Education): Those discussions involve our accountancy staff, who work in detail on financial forecasts and the recovery plan. In addition, the director of that directorate has visited Inverness College to discuss the detail of the plan and how it will be managed with the finance director, the principal and—I believe—the chair of the finance committee. That is the nature of the discussions that we have had.

On whether we are confident that the college is back on track, my answer would be a guarded, "I think so." The case has been long running. As is true of all further education colleges, the issue comes down to tight management. Together, the governing body and the senior management must ensure that they manage the affairs of Inverness College tightly.

Eleanor Scott: We had a projection for the last financial year that was far off the mark. Are you confident that that will not happen again next year and in subsequent years?

Mr McClure: We are assured by the college that it has taken steps to tighten its control on expenditure, which was a particular problem. Obviously, we will monitor the situation closely to see whether that is effective. Professor Little assured you earlier that he now has the systems that will enable him to control expenditure more effectively.

Mr Welsh: I asked Professor Little how robust the college's financial forecasting is. Are you confident that it has robust forecasting systems?

Mr McClure: We are satisfied that our monitoring of the financial forecasts suggests that they are as reliable as any forecast can be, based on the evidence that is available to us now and on the assumptions that one must always make in a forecast. However, we will monitor closely. The important thing is for the college itself to monitor its budgets carefully and to be prepared to take action if it sees that it is departing from its plans.

Mr Welsh: I presume that you monitored the college in the past but it got it wrong in the past, so why are you more sure now that it has the robust systems that are essential?

Mr McClure: There has been a learning process.

Mr Welsh: We have had different colleges and different problems, but similar financial problems. How do you expect to get people out of the private finance initiative problem in West Lothian College? What light is there at the end of the tunnel? What can be done?

Mr McClure: As you heard from West Lothian College this morning, the funding council has been closely engaged with it on that question. The outcome is not clear, except that we will not give up the work until we have reached a satisfactory resolution for the college. We have assured the college that, whatever the model says, the funding council will not withdraw or in some way curtail the college's funding until the situation has been fully resolved, as Mrs Pinder said, to the satisfaction of all the parties involved. Unfortunately, as she indicated, because we are now at an advanced stage of a commercial negotiation—which it has to be—it is hard to give details of what might emerge.

Margaret Jamieson: I fully understand the commercial sensitivity. However, if you continue along that road by providing further support to West Lothian College, what impact will there be on other colleges with PFI contracts and colleges that have not gone down that road? Will their funding be adversely affected because the pot is still the same size?

Mr McClure: I do not think so. So far, we have not had to give special funding beyond the arrangements that were inherited for West Lothian College. It has been funded within the formula in the same way as other colleges, hence the discussion about whether its SUMs target should have been higher or lower. We have not followed the model in setting its SUMs target; it has been set in the same way as for all other colleges.

As it happens, until now increases in the unit of resource have meant that the cash that has been supplied to the college has not fallen behind the position that was predicated in the model. As you will see from the table in our submission, the cash has actually kept significantly ahead of that position. That is where we are now. If the problem continued much further into the future, we would have to consider whether special funding was required, but we hope that later this calendar year we will have resolved the issue. That is the timetable to which we are working. We will then be able to see where we can go from there.

Margaret Jamieson: I have a question on PFI or public-private partnerships—whatever term we are using at the moment. I am aware that other colleges are looking for new build. Does the SFCFHE have a say in whether they take that route? Obviously such funding decisions come back to the SFCFHE. Is there also discussion with the department that implements the policy? The committee does not question policy, but such a decision obviously has policy implications.

12:15

Mr McClure: Again, as became apparent from earlier evidence, a great deal more has been learnt about PFI than was known when it was started—the world has changed very significantly. In those days, no capital funding was available to support capital projects. As I am sure you know, the Scottish Executive has provided substantial capital funding to the FE sector. That programme has been running for a while and I have no doubt that if that funding had been available when the West Lothian College project was introduced, we would have had a different kind of arrangement.

We are not the only ones, but the funding council has done work on the appropriateness of PFI in the FE sector because most of the projects in that sector would be seen as being small compared to the mega-projects in the health service and so on. On top of that, the key benefit of PFI has always been assumed to be that if a private contractor runs the facilities and makes efficiencies in the running costs, that will offset the extra profit element and so on that is built into the contract. As it happens, there is not much scope for that in FE colleges. As a result of the work that we have done and discussions with Parliament—to which you referred—we have either written, or are about to write, to the FE sector saying that unless a project is pretty substantial, there will no longer be a requirement to go all the way through the PFI calculations, which can be very onerous and long-winded, only to find that it is not really a viable deal for a relatively small project.

Margaret Jamieson: What do you mean by relatively small?

Mr McClure: If the project costs in the region of £20 million to £30 million, PFI is not really worth considering, but there might be gains for projects of £30 million to £50 million and upwards. I have to qualify my answer by saying that there are different circumstances and one set of circumstances might suit a particular developer or there might be something fortuitous in the arrangement that would make a smaller deal perfectly satisfactory. We should not rule PFI out at any stage, but colleges can waste an enormous amount of time if they are forced to test everything when experience shows that it does not really work. We discussed that with the unit that is responsible for PFI in the department and it agrees with the decision.

Margaret Jamieson: It would be interesting to hear Mr Frizzell confirm that.

Eddie Frizzell (Scottish Executive Enterprise, Transport and Lifelong Learning Department): Yes.

Margaret Jamieson: Does that definition of what is not PFI-able go right across the Executive?

Eddie Frizzell: I cannot answer that question because I do not work in the PFI unit, but I do know that there has been quite a lot of learning about PFI during the past five to 10 years, and that policy in that respect has been modified.

Margaret Jamieson: Okay. Thank you.

Mrs Mulligan: Evidence was given earlier that West Lothian College now has a building that is fit for purpose, which is the advantage of having acquired the finance through PFI. However, Mr McClure said that further education colleges do not necessarily fit the facilities management model. Can you say more about that? Is it about the role of further education colleges? Do you think that the facilities management side of the West Lothian College project has worked to the detriment of the college providing the kind of service that it seeks to provide?

Mr McClure: I am not sure about your final question. The main issue is that most of a college's expenditure goes on teaching and support staff who are specialists in their areas, which is not something that a private contractor can come in and do more efficiently. That is the basic model and the service with which we are dealing, so there is much less scope to make savings in running costs through involvement of the private sector. Such an approach has worked in schools, for example, because a large number of schools may come under one local authority's responsibility, all the projects can be bundled up and made into a big project and there can be a big facilities management project, but that approach is not as easy in FE, particularly when each college is an independent autonomous institution.

On whether the college has had value from its facilities management, Principal Pinder referred to difficulties in organising small changes. For example, bureaucracy is involved in trying to get things done that might be done more easily in other colleges. However, something must be set against that. When different procurement methods are being compared, it is often forgotten that one of the key aspects of PFI is that the full life-cycle costs are built into the procurement. Therefore, in theory, the apparently large amount of money that is paid out will result in a college being in pretty much the same condition in 25 years' time as it was when it was started.

However, we know that when colleges, and universities for that matter, run their own affairs and budgets are tight, maintenance—particularly longer-term maintenance—tends to be the first thing to go, which is true of any organisation. When people compare costs, they often do not compare like with like. One cost is a fuller life-cycle cost for the whole period and the other cost involves managements making judgments as they go along about how much they think they can afford to spend to maintain their buildings.

Susan Deacon: I want to ask Roger McClure and Eddie Frizzell a few overarching questions. Today, and with the various pieces of documentation to which we have had access, we have considered in depth three specific cases in the FE sector, each of which involves a different set of circumstances and problems. By common consent, the problems are challenging and need to be resolved. Can you help us to understand how such situations can be brought to a conclusion? We understand issues to do with the respective roles of, and relationships between, the Scottish Executive department, the funding council and the governing bodies, as the committee has explored such issues in detail before, but I ask you to go beyond the letter of the roles and relationships, if you like, and to explain to us in practical terms the solutions that can be reached and whose job it is to ensure that they are reached, so that we do not have the same people getting round the table six months or however long from now.

Mr McClure: I am glad that you ask about the bigger picture. I first appeared before the committee when a large number of FE colleges were reporting deficits. The colleges were nearly always noticed in the media because of those deficits. Therefore, working with principals—there is a principals' forum, so it is possible to meet principals and to get a collective commitment—we came up with the so-called financial security campaign in 2002. We have included figures that relate to that campaign in our evidence to the committee.

The campaign's impact has been quite dramatic. That comes down to the principals' acceptance that financial security is a high priority and that they must ensure that they get a grip on their finances. The real conundrum for the principal and staff of any FE college is that their instinct is to bring in anybody who presents themselves at the door, as they see that such people need support and help—members heard that again twice this morning. That is the FE ethos. However, we have limited funding to distribute and inevitably, because we have a fixed budget, a point will come when colleges and their management, in particular the management board, have an important role to play. They must say that they have exhausted the college's financial capacity and that—regrettably—students must be turned away. At that point, the Scottish Executive must decide whether it wants to expand the total volume that the sector can cater for or feels that the existing volume is correct. There is no getting away from that.

I am convinced that the sector is very efficient. This morning, the committee has heard from Sue Pinder from West Lothian College and John Little from Inverness College. Both of those colleges could take many more students if they had the resources to do so. They are not exceptions—that situation is replicated throughout the land.

As the principals agreed back in 2002, sorting out the basic financial management problems is a high priority; hence we had the financial security campaign, the results of which can be seen. I am cautiously optimistic that when we get to our target date at the end of next year, all colleges will be financially secure or very nearly so. The three colleges that are represented here have particular, long-running problems within that bigger picture, but I am confident that those problems are now being brought to a head pretty rapidly.

Susan Deacon: Everything that you have said is interesting and germane to the question I asked, but I am not sure whether it answers it. Given the different levels of responsibility and decision making, where does ultimate responsibility lie? I stress that I do not just mean from an accountability point of view. Who is the person who all players recognise as being the person who can really fix things? Where would the responsibility lie for ensuring that solutions are reached? All of us round the table have grappled with that question in relation to other sectors as well, so you are not alone in being asked that question.

Mr McClure: Forgive me for not picking that up. The answer is clear: the institutions are autonomous and the boards of management are responsible for their solvency. Whatever level of income is available to a college in a particular year, or over a period of years, the board of management has responsibility for ensuring that the college remains solvent.

Susan Deacon: Let us take West Lothian College as an example. Does the fact that the funding council and the Scottish Executive are around the table and part of the discussion mean that you see yourselves as contributing to rather than leading the process?

Mr McClure: I think that it is a mixture. Certainly we contribute to the process and are no doubt involved in the solution, but we also represent the taxpayer. We have an interest in how colleges manage themselves because we want to be satisfied that they are not getting into difficulty. Mismanagement tends to consume more and more resources. If there is a need for temporary help or subventions, that is a cost to the system, so ideally we would like all colleges to manage themselves competently and not to get into financial difficulty. Our role is not just statutory; there is a public interest as well.

Susan Deacon: Before Eddie Frizzell answers my question, I cheekily interject to raise another related dimension. I have emphasised solving problems, on which I guess much of our thinking has been today, but what about the flip-side—the wider question of building good practice? What is the Executive's role—relative to the funding council and individual governing bodies—in establishing who has ultimate responsibility for driving the good practice and management practices and so on that will lead to the financial solutions that we all seek?

Eddie Frizzell: Is that question for me?

Susan Deacon: It is indeed.

12:30

Eddie Frizzell: What Roger McClure said is important. At the end of the day, the responsibility lies with individual colleges. It must be that way in any part of the public sector. The same applies to me in my department. I get a budget for running costs and if ministers' demands exceed what I can deliver from the budget, I just have to get on with it; I have to prioritise and do my best. The situation is similar to the situation in a college: demand potentially exceeds supply.

When I first appeared before the committee in the first session—even before Roger McClure appeared before it—things were in a really parlous state. After incorporation, we had a huge competition among colleges to get extra numbers in. There were real issues about viability, and ministers took a policy decision to consolidate and to stop that unfettered, essentially damaging, competitive growth.

The overall funding that ministers have provided has made a contribution to stabilising the situation and it is important that we do not lose sight of that. In 1999, we were funding about £289 million or £290 million a year. Ten years after that, we will be funding £619 million a year. The financial situation is more benign than the situation that was inherited, which undoubtedly helps, with or without good management in colleges.

When Roger McClure took over, he and I had a conversation in which I made it clear that one priority that we needed to address was reducing the financial deficits and not taking as long over that as was being forecast. At the time, it was being forecast that some colleges would take a decade or more to get through and that there would be some quite lengthy periods before financial viability would be reached. The funding council took that message on board, and Roger McClure has described the importance of doing that.

Putting together a team of people to consider and help to spread best practice was a high priority for the department that we wanted the funding council to take on, and we are seeing the fruits of that now. Although the responsibility for responding to what we know about best practice and taking tough decisions lies with governors and principals, the funding council and the Executive have an obvious interest in ensuring that that is given priority and that the circumstances are created in which efforts can pay off.

Susan Deacon: May I ask another question on the back of that, or is my time up, convener?

The Convener: Is it related?

Susan Deacon: I can make it related.

The Convener: We know that.

Susan Deacon: I am trying to understand how good and effective decisions will be reached apropos the specific colleges. I asked Sue Pinder about the particular circumstances in West Lothian and the wider needs of the local economy. The same question could be asked of any individual college. There are bigger, strategic questions about the distribution of colleges, not to mention student numbers, funding allocations and so on. For the purposes of our discussion, can our witnesses factor in a sense of how those aspects—which I am sure must fall primarily to the funding council—will feed into decisions about future funding for individual institutions?

Mr McClure: I cannot answer that precisely, as I do not know the answer yet, but I can tell you about the demand-and-supply survey that the funding council has carried out. When I appeared before the committee previously, we had undertaken one survey, which was okay but was not wide enough. As you know, the post-16 area is complicated, with all the voluntary sector and local authority sector involvement. We have just completed a second version of that demand-and-supply survey. The report, which has just been published, illustrates just how complex the field is. The consultants identified a large number of indicators that they bring to bear not only in the national report, but in reports for each area of Scotland.

We have embarked on a series of public seminars and conferences—some of which have already taken place—to bring together all the stakeholders to make sense of it all. In the light of the information that is received, the new funding council will have to make a decision about the extent to which we should use and rely on such data to drive funding. You will readily appreciate that funding is a zero-sum game: funding that is put preferentially into one area of Scotland is denied to another. One thing that everyone agrees on is that, if we are going to start making selective allocations, we will have to be pretty confident that our evidence is robust and that we understand it.

Part of the problem is that we find a range of conflicting issues in every area. Should we consider underparticipation and social inclusion issues in one area, or skills needs in another area? How do we give priority to those two conflicting things, which are both important but are not directly comparable? Those are very complex questions, but we are trying to grapple with them.

Susan Deacon: When might we see the conclusion of some of that work?

Mr McClure: The next funding round will start in the autumn and will lead to allocations to the FE colleges in April. We will have to factor in making sense of the study and the close consultation that we carry out with the sector. We work with the Association of Scottish Colleges and the principals because we want their views on how the process should work. They must have confidence in the decisions that we make.

Margaret Jamieson: You have talked about the pattern of funding and how, when one area gets an increase in funding, another area of Scotland gets less. However, David Green told us that Lews Castle College received extra funding because of where it is and because the area that it serves is sparsely populated. I understand that Lews Castle College is not alone and that other colleges have received a remoteness uplift. Can you explain the rationale behind that, how it was worked out and why 14 colleges now qualify for that funding?

Mr McClure: It is not an exact science. The funding council inherited funding patterns from the Scottish Office. It has built on those and has tried to refine them by collecting evidence that it tries to understand. The colleges have been receiving remoteness funding for quite a long time, and the recent exercise reviewed the position to see whether the amounts were appropriate. As a result of that review, the funding council decided to uplift most significantly the remoteness funding for the island colleges. Riona Bell knows more of the detail than I do.

We were supported in that review by various statistics, including better measures of sparsity of population than were available to us before. That is important because, when all is said and done, the funding methodology is driven by class sizes. Staffing is by far the biggest single item of expenditure of any college. The relation of that to the volume of education that is provided and the volume of students boils down to the average class size and how much funding must be provided for that number of students to pay for a member of staff.

In that respect, the sparsity indicators are relevant. If the island colleges try to offer a reasonably wide curriculum, it is difficult for them to muster class sizes that match the average in the rest of the country, especially the class sizes that can be got together relatively easily in an urban or semi-urban setting. The issue boils down to the sparsity of the population and the colleges' ability to get a big enough group to be viable under the general formula. They would not be viable under the general formula without the uplifts.

Margaret Jamieson: What method did you use to determine what the level of remoteness funding should be?

Mr McClure: I invite Riona Bell to answer that question, as she knows much more of the detail than I do.

Riona Bell (Scottish Funding Councils for Further and Higher Education): The new level of funding for the island colleges was based on two main bits of evidence. The first, which Roger McClure has described, relates to class size. You have already heard about the weighted SUM per FTE indicator, which is a proxy for class size. In looking at the sector, a clear distinction was made between the three island colleges and all the other colleges in Scotland in the weighted SUM per FTE statistic.

The second piece of evidence came from our examination of other public services, especially in health and school education. There is a specific premium for the islands in both those services. In comparing FE with other public services, we saw quite a similarity and felt that that was sufficient justification for increasing the island allowance.

Margaret Jamieson: I am happy that you looked across the public sector, given our long discussions in the first session about the Arbuthnott proposals. Later, could you give us the names of the other colleges that qualify for the extra funding?

Mr McClure: I can give you a list. It is all published in our allocation letter.

Margaret Jamieson: Thank you.

Mr Welsh: From your description, I understand the difficulties in searching for objective criteria to distribute scarce resources fairly, but I am a wee bit puzzled. Mr McClure described an apparent paradox earlier, saying that the field is complex yet the process is clear and apparently straightforward. He said that, with limited finance, it is up to individual colleges and that central finance stops when we have exhausted the financial capacity of the college. Is that an objective criterion? Is it easy to see and agree to?

Mr McClure: I do not recognise what you said.

Mr Welsh: You said that finance stops when we have exhausted the financial capacity of the college. Is that an objective criterion?

Mr McClure: I cannot remember the context in which I said that, but in the way you present it I do not understand the reference at all.

Mr Welsh: How do you decide to allocate resources between colleges? You seemed to say that, with limited finance, there has to be an allocation, but in taking its decisions, how does the college—

Mr McClure: I see what you are saying. Sorry, I have now registered it. That is not a criterion in the allocation of funding. The allocation of funding is driven by a formula that includes the sorts of things that Riona Bell spoke about. We have a tariff for how many weighted SUMs go with particular programmes and we work out a unit of resource per weighted SUM. That process is fairly well defined. I was saying that if someone is managing a college and they are trying to decide how many students to admit, once they have reached the point where their budget cannot afford any more students, they should not take any more in. That was the point that I was trying to make. It is not to do with the allocation between colleges.

Mr Welsh: Are the colleges happy with that concept? Do they agree with what you have described?

Mr McClure: You would have to ask them. As I said earlier, the wish to reach out to anybody who presents themselves for education is deeply ingrained in the ethos of FE lecturers and managers, but I am afraid that an unavoidable compromise has to be made. If a college goes on taking students beyond its means and cannot afford to provide for them, it will get into deficit and could run the risk of destabilising the whole college. It is for the board of management to make that judgment and to decide when the point has come at which it simply cannot afford to take more students.

Mr Welsh: How quickly can you pick up whether a college goes outwith the criteria that you lay down? How good is the monitoring of what goes on in practice?

Mr McClure: We do not lay down any criteria on how many students colleges should take; we expect them to remain solvent. The financial monitoring that we describe in our submission is the main way in which we find out routinely how the financial position of colleges is unfolding in the current year and looking forward, but we also find out information from their annual audited financial statements. Those are the main ways in which we identify the progress that colleges are making on their financial health.

Mr Welsh: Are you able quickly to pick up whether a college is overstretching itself?

Mr McClure: We are underestimating the ability of colleges to recognise themselves that they have got into difficulty. It is not that they get into difficulty and do not know it. They can get into difficulty for a variety of reasons that can arise in any complex organisation. They recognise pretty quickly when they are in difficulty. The challenge then is to take the decisions that are necessary to correct the difficulty. Often, those decisions can be painful, as we have heard this morning. That is where there is a challenge for the college management and the governing body.

Mrs Mulligan: My apologies, but I want to take you back to an issue that Susan Deacon raised. Both you and Mr Frizzell said that the colleges were responsible for ensuring that they were financially viable. You also went on to say that a policy decision was taken in 2002 not to continue to develop competition between our colleges but to consolidate student numbers in them. I understand the logic of that decision, but did you recognise at the time the impact that it would have on a college that was operating under a PFI on the basis of increasing student numbers? If you now do so, do you recognise that you have a responsibility to address the situation?

12:45

Mr McClure: From my personal point of view, I was engaged with West Lothian College and the PFI contract before we knew what the guidance from ministers would be on the next funding round. I came to the council in 2002. Sue Pinder wasted no time in bringing to my attention what she saw as the difficulties with the contract and we started work on it pretty well straight away.

The decision to consolidate was taken at sector level, not on account of any individual college. I understand that a decision was taken at that level because the rapid period of expansion had put a strain on colleges that was plain for all to see. Eddie Frizzell will correct me if I am wrong on that. When I arrived at the council, a large number of colleges were in financial deficit. Under the monitoring system that we used at the time, only one college in 46 was in good financial health. Clearly, something had to be done about that and a good decision was taken at sector level. As we have been explaining, it was then up to the council to determine how we would monitor and engage with individual institutions on any particular issues.

Mrs Mulligan: Mr Frizzell, will you comment on the advice that was offered when the policy decision was being made?

Eddie Frizzell: Roger McClure is absolutely right in saying that the decision was taken at sector level. PFI has a long gestation; it goes way back to the mid-1990s. In fact, it happened just at the point at which we transferred responsibility for the funding of individual institutions to the funding council. The decision on capping was very much sector wide. Clearly, some colleges would have found that policy difficult and others would have found it less so. It became an issue that had to be addressed in the on-going situation.

Mr McClure: If I may, I will clarify one thing. The word "cap" has been used quite frequently this morning. Yes, there is a cap on the funding that we allocate to a college. We have a fixed budget and each college gets a share of it. Associated with that allocation is a target number of WSUMs. If the college falls below the target number, it might expect us to explore whether we should recover some of the allocation because it did not deliver on its target.

There is no cap on the number of SUMs that a college can deliver, however. If a college feels that it can deliver above its target, it is free to do so. It may do so for a variety of reasons—for example, it may have generated other income or it may be particularly efficient. Each college will have its own special circumstances and objectives. In one way or another, most colleges deliver above their targets.

Mrs Mulligan: You said that, following that policy decision, some colleges might have found themselves in some difficulty because of the change in projected numbers. Did colleges other than West Lothian find themselves in difficulty for that reason? Was their situation exacerbated by the nature of the PFI deals?

Eddie Frizzell: I am not sure which one of us should answer the question.

Mrs Mulligan: Whoever thinks that they can do.

Mr McClure: The general answer is that the measure effectively recognised that colleges were under considerable financial strain. I saw it very much as a relieving measure. We were basically saying to the colleges that they did not have to expand and that we were going to give them above-inflation increases in their core funding to give them a chance to consolidate their position, to build in quality and to do a lot of the things that were probably being overlooked when the system was expanding so rapidly and people were competing so fiercely to expand. It is therefore unlikely that any college in normal circumstances would have found the situation a problem. West Lothian College was unique in having a model that tried to work out the sum of money that it would get for each of the 25 years. I think that we have dealt with that. As far as I am concerned, that model has been put on hold while we sort out the college's position and its funding will be sustained during that period.

Mrs Mulligan: That is helpful; thank you.

The Convener: You have repeated the commitment to supporting West Lothian College until the problem is resolved, but we heard earlier that resolution would mean that every party would have to come to an agreement. What if the problem is not resolved because agreement cannot be reached? Will you underwrite West Lothian College in perpetuity?

Mr McClure: Forgive me, convener, but that is a hypothetical question. In the circumstances, you can readily understand that I would not wish to say what the funding council would do. Perhaps I can fall back on statute, which requires the First Minister to secure adequate and efficient further education in Scotland. That legislation will be superseded by the Further and Higher Education (Scotland) Act 2005, but it seems to me that there will still be a requirement to secure appropriate further education in every area of habitation in Scotland—that will not go by the board.

The Convener: Thank you for that answer. I have a question about Lews Castle College. The final paragraph of its written evidence states that

"Remoteness funding currently only applies to 65% of our business",

because 35 per cent is to do with higher education and UHIMI. That was mentioned in oral evidence, too. The college looks forward to the possibility that remoteness funding might be considered in relation to the higher education funding that it receives, so that additional funds would again come to the college. There are difficulties with that and the committee is concerned about the extent to which remoteness funding carries across the further and higher education sectors. What would be the implications for the University of St Andrews, for example, or for the Crichton campus and the work that is done there with other institutions? I put that to you even though it is a hypothetical question. It strikes me that if the optimism about Lews Castle College's recovery relates to a possible shift in that area, that optimism might be misplaced.

Mr McClure: That is certainly a new issue and I am quite sure that it will be considered when the funding councils merge and the new council considers both sectors side by side. However, it is fair to say that the reason why remoteness has not been an issue in the past is because higher education has always been broadly considered as a national system, in which students will travel, whereas FE was clearly a local system, in which local circumstances had a bigger implication for the ability of the college to flourish. I would not have an awful lot of sympathy with the University of St Andrews—the example that you gave—because we know that people are very keen to travel to St Andrews to benefit from the university's education.

Lews Castle College and the other island colleges have created a special new circumstance that would be limited in scale. I remain to be convinced that institutions such as the University of Aberdeen or the University of St Andrews were being affected by the cost of taking students from remote areas. Funding allocations should primarily be driven by cost unless a policy issue lies over the top of that. That cost can be demonstrated in the case of remoteness funding for FE colleges. We will certainly consider the matter for higher education, but we will have to be convinced that extra costs can be demonstrated.

The Convener: I do not imagine that Mr Frizzell will want to comment on that, as it is a policy issue.

Eddie Frizzell: It is funding council territory.

The Convener: As there are no further questions, I thank our witnesses for their helpful evidence. I suspect that we might have some further follow-up questions, but information on the colleges that qualify for remoteness funding would be helpful in the meantime.

12:55

Meeting continued in private until 13:14.

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