FINANCE AND PROPERTY COMMITTEE – 6 MARCH 2018

5-YEAR FINANCIAL STRATEGY

1. Background

1.1. In March 2017 the Board approved a 5-year financial strategy to 2021-22, aimed at achieving a break even operating result and cash balances sufficient to support short-term working capital movements

1.2. The financial strategy will be refreshed annually on a rolling basis. An initial draft was considered at the January 2018 FPC meeting, and guidance was provided in relation to the base case assumptions and expectations around an action plan.

1.3. The assumption on the April 2018 cost of living award for academic and support staff has been amended to mirror the public pay policy recently announced by the Scottish Government. A list of actions has been added to each section of the strategy document.

1.4. This paper sets out the final draft of a proposed financial strategy for the years 2018-19 to 2022-23 to achieve the above targets. Projected operating cash and balance sheet, along with sensitivities, are set out in the appendices to this paper.

1.5. FPC is asked to recommend to the Board that the strategy is approved, subject to any amendments advised.

2. Assumptions

2.1. Credits.

In 2017-18, the College credit target is as follows:

	Credits
Core	103,232
ESF	5,101
Additional Childcare places	629
Total	108,962

The College continues to lobby for a higher credit allocation and has indicated in its Quarter 1 FES return that we would be in a position to deliver additional credits through in-year redistribution. However, there are no guarantees if or when they might become available and therefore the strategy assumes the continuation of the current level of core credits.

The indicative allocations from SFC include a credit target of 107,808 for 2018-19 as follows:

	Credits
Core	103,314
ESF	4,494
Total	107,808

There has been a small increase of 82 in our core credits, but this now **incorporates** the increased childcare credit target, so there is a net reduction of 0.5%. The increased childcare credits over baseline are required to be at HNC (level 7), which we would be unable to deliver, with a shortage of placements and insufficient demand for places. Discussions are ongoing with SFC around the same issue relating to the 2017-18 additional credits and the scope of these discussions will be expanded to include 2018-19.

The ESF credit target has reduced by 12%. This is the result of the Youth Employment Initiative in west Scotland coming to an end in July 2018. Although our ESF activity is under the Developing Scotland's Workforce programme which covers east Scotland, the impact of YEI is felt across all ESF programmes. This 12% reduction in credits translates into a 5.5% reduction in ESF funding.

For subsequent years, we are assuming that the 2018-19 credit target will continue. Until there is some clarity over Brexit, we are assuming that £1.15m of ESF credits will be converted to core activity at the point we leave the EU. An additional risk to ESF credits comes from the downturn in HE recruitment, as these credits are specifically tagged as level 7 and above.

Actions

- Continue to lobby for additional core credits to be added on a permanent basis.
- Maintain pressure for ESF credits to be transferred to core to protect from the impact of Brexit.
- Continue to press SFC for clarification around the level of the childcare credits.

2.2. Funding uplift

The 2018-19 indicative allocations include the full costs of NPB (national pay bargaining - harmonisation, terms and conditions, job evaluation). In addition, there is a 1% increase to the unit of teaching resource, which increases our funding by £248k. However, after taking into account the reduction in ESF funding and an arbitrary reduction in the brought forward funding, this increase is reduced to £48k. Furthermore, the funding accounted for in 2017-18 includes retrospective allocations of £104k for prior year NPB costs and £20k from a final reallocation of ESF funding. Once these are also taken into account, funding has **fallen** by £76k, before targeted NPB funding.

We assume that funding for 2019/20 will reflect the additional national bargaining for that year but at this stage assume no further increases.

SFC have indicated very clearly that funding will return to a simplified 'price x volume' model. Additional funding for national bargaining costs will be retained in the sector but will be withdrawn in stages from specific college allocations and redistributed on a volume basis. Our assessment is that we sit somewhere in the middle of the table in terms of specific college allocations and so the assumption used in this strategy is that subsequent years will be 'flat cash'.

In the 2017 financial strategy, it was assumed that the College would lose c£750k over 3 years as a result of changes to the methodology for funding access and inclusion and up to £300k as a result of a reduction in associate student numbers. We have removed these funding changes from the base model and added to the list of sensitivities, on the basis that SFC would not seek to add further de-stabilisation into the funding system at this time. The indicative allocation paper states that there will be no change to the associate places scheme for 2018-19.

See below for a summary of changes to SFC grants:

	2018-19	2019-20	2020-21	2021-22	2022-23
	£'000	£'000	£'000	£'000	£'000
Prior year funding	27,880	29,812	30,493	30,493	30,493
NPB funding	2,008	681			
Other changes	-76				0
Funding for year	**29,812**	**30,493**	**30,493**	**30,493**	**30,493**

Actions

- Monitor the actual impact of NPB and compare with the targeted funding provided to meet these additional costs.
- Exert pressure on SFC for additional funding, if the funding allocated is considered to be lower than the actual costs.
- Continue to support the sector's case for an increased unit of resource.
- Monitor proposals for changes to funding methodology and lobby against anything which disadvantages Dundee & Angus College.

2.3. Non-core income

Price levels are assumed to rise by 1.5% annually from 2019/20, with no increase in 2018/19. In addition, an annual 2% volume increase for commercial income from 2019/20 has been included. It is worth noting the potential risk to non-core income posed by the Flexible Workforce Development Fund, as companies switch activity to the latter.

Once the current financial position has been stabilised, we will look to set an aspirational target for transfers into the Foundation to fund future infrastructure investment. These are permitted if the College is able to demonstrate that it has generated a commercial surplus on a "full cost" basis and has also delivered an overall increase in cash in the year.

See below for a summary of in-year increases to non-core income:

	2018-19	2019-20	2020-21	2021-22	2022-23
	£'000	£'000	£'000	£'000	£'000
Tuition fees – price	0	56	57	57	58
Other income – price	0	67	69	72	74
Other income – volume	0	89	93	96	99
Total non-core increase	**0**	**212**	**219**	**225**	**232**

Actions

- Analysis of the reasons for Tuition Fee income being c£500k lower than budget in the current year will continue and, once this is complete, an action plan will be put in place to seek to recover the budgeted position in 2018-19.
- Utilise Stakeholder Advisory Boards and strategic engagement with businesses to expand our reach, supported by interventions including Flexible Workforce Development and Innovation Funds.
- Continue to enhance existing customer relationships through targeted broader Future Talent Services to Business.
- Mitigate any reduction in EU sources of funding as a result of Brexit through targeting international commercial opportunities and broader Trust or Donor sponsored sources.
- Expand partnerships with public and third sector organisations to increase range of employability based contracts.
- Progress the development of the Service Design Academy.

2.4. Pay costs

Once fully implemented by April 2019, the annual cost of unpromoted lecturing staff is estimated to be c£600k higher than it would have been under current pay scales (including incremental progression).

It has not been possible to agree mapping of Dundee and Angus College promoted staff to national role profiles and therefore this will be settled through national arbitration. The additional annual cost once fully implemented will be either c£300k or c£650k, depending on the outcome. The lower value has been assumed at this stage.

The reduction in the number of teaching hours per week for unpromoted staff from 24 to 23 is estimated to cost c£500k, with changes for promoted staff costing either c£130k or £770k, depending on mapping to role profiles: if Course Lecturers are mapped to Level 1, there is a loss of 1 teaching hour per week (18 to 17); if mapped to Level 2, there is a loss of 6 teaching hours (18 to 12). Again, the lower value has been assumed. It is assumed that the early cost will be lower, on the basis that the "lost" hours are likely to be initially filled through part-time variable resource.

Cost of living increases for academic and support staff are also agreed nationally. The April 2017 award for support staff has been settled at a flat rate £425, which equates to around 1.8%, with an additional 0.2% for the impact of the change in annual leave entitlement on term-time post salaries. The total increase of 2% is reflected in the 2017-18 forecast.

Negotiations around an April 2017 settlement for academic staff continue: the gap between ask and offer remains wide, and uncertainty remains around fundamental matters like whether this will be a single or a multi-year agreement, and whether any increase would be on a consolidated basis. In light of the level of uncertainty, this version of the strategy includes a 1% uplift, which is consistent with the 2017 strategy and with our Financial Forecast Return.

The April 2018 cost of living award has been assumed in this strategy to be in line with the recently announced Scottish public sector pay policy, which guarantees a minimum 3% for staff earning up to £36.5k and a maximum 2% for staff earning over that, capped at £80k. This would add around £650k to the annual paybill. For subsequent years, we have retained a planning assumption of annual 1% increases for both staff groups, which would add c£300k each year.

In line with the rest of the public sector, there is no expectation that there will be funding to cover cost of living increases and that the excess over any general funding percentage increase has to be met through savings.

See below for a summary of changes to pay costs, before VS:

	2018-19	2019-20	2020-21	2021-22	2022-23
	£'000	£'000	£'000	£'000	£'000
Prior year	28,196	30,456	31,445	31,758	32,073
Lecturers' harmonisation*	383	383			
Teaching hours	425	212			
Support job evaluation	934	85			
Cost of living	518	308	313	315	318
Current year	**30,456**	**31,445**	**31,758**	**32,073**	**32,391**

*Please note that these are not the total costs of harmonisation, as higher costs have been progressively incurred since April 2016.

Action plan

- VS applications received by 31/1/18 have now been considered. To date savings (including on-costs) from applications with final approval total c£400k. It is estimated that those applications currently requiring further information may yield further savings totalling c£100k. There would be a small saving in the current year, with a full year effect in 2018-19.
- Other structural staffing changes have been proposed which would generate a total additional saving of c£750k if fully implemented. Further work is required in order to confirm the viability of these changes and identify how to achieve them. Due to lead times, it is unlikely that these changes would generate a full year saving in 2018-19.
- Following release of the "current challenges" paper to staff and the Principal's briefings, teams have been asked to develop their own ideas on potential efficiencies in the operation of support services. In many cases, these involve cross-team conversations and/or liaison with the curriculum to identify what might work best for learners.
- Support staff have been invited to consider whether a change to their terms and conditions might suit their individual circumstances, for instance through

reduced hours per week, term-time contract, phased retirement, or buy-back of holidays.
- A longer timeline has been agreed for curriculum staff savings, as these will be largely predicated on the curriculum review, in particular the portfolio, with efficient class sizes the primary driver for savings. The reconfiguration of the course portfolio will be largely complete by 2019-20. An overall increase in the average class size will generate savings of 3-5% in academic staff costs by the end of that financial year. Timelines and savings forecasts will be firmed up as we progress with implementation of the review and regular updates will be provided to FPC.

2.5. Non-pay costs

It is assumed that operating costs will rise in line with general inflation but that price increases will be off-set by efficiency savings. Over the long term, the annual cost of unfunded early retirement will fall from its current level of £400k per annum but the strategy assumes continuation of this level throughout the planning period.

As annual capital repayments of £571k are made on our outstanding loan, interest charges fall by c£20-30k per year. The term loan with Santander will be fully repaid by July 2028.

Action plan

- A review of all non-pay functional lines has been carried out and reviewed by the Executive in order to identify the efficiency savings which may be generated to off-set general inflation.
- Staff across the College are actively involved in exploring ideas for reducing non-pay spend.
- The areas identified for further exploration include the following:
    - Staff mileage: achieved through rationalised meeting structures, full utilisation of college vehicles, car-sharing and alternatives to face-to-face meetings (eg Skype).
    - Foreign travel: shifting focus from international to local regional commercial activities
    - Organisational Development: tightening central control over spend, clearly linking it to strategic drivers
    - ICT equipment: refocus annual investment round so that it supports the curriculum strategy
    - Photocopying: the new contract for Multi-Function Devices will generate some savings, along with removing non-contract printers

2.6. Capital expenditure

It is assumed that capital expenditure will be fully-funded, principally through the SFC capital grant and bids to Dundee & Angus Foundation, although other external funding will continue to be sought. The Foundation has awarded £2.55m to the College for capital projects since 2014, including the recent award for the Tower windows. Once we have a clear indication of funding for the Kingsway redevelopment project, this will be built into the financial strategy.

3. Financial Recovery Plan

3.1. Savings required

Based on the above assumptions, without any ameliorative action, the cash balances at each year end would be as follows:

Financial Year	Year end cash balance
	£'000
2017-18	958
2018-19	(195)
2019-20	(1,274)
2020-21	(2,428)
2021-22	(3,651)
2022-23	(4,941)

As additional income generation and non-pay savings have already been factored into the above cash balances, the savings required in order to remain cash positive will come from reduced head count.

The assumption is that the current voluntary severance (VS) terms will continue to apply and that 75% of the staff savings will be achieved through VS, with the balance coming through natural turnover and redeployment. Based on the average cost per full-time equivalent member of staff as shown in the most recent annual accounts, the required savings would equate to c25 posts in 2018-19.

The following table sets out the savings targets required each year, along with the resulting year end cash balances:

Financial Year	Savings required	Year end cash balance
	£'000	£'000
2017-18		471
2018-19	1,000	317
2019-20		126
2020-21	250	243
2021-22		302
2022-23		308

3.2. Action being taken

Please see the boxes at the end of each section above for specific actions being undertaken to generate the required savings.

Initial restructuring proposals for support services were considered at a meeting of the Senior Leadership Team in early February. These will be developed further through consultation with teams and more detailed implementation plans brought back for review before the end of March.

In the meantime, the curriculum review continues to be progressed. The expectation is that this will naturally generate savings through greater efficiency but the lead time for realising these is inevitably longer, with curriculum portfolio changes requiring significant forward planning. Where efficiencies result in curriculum areas being removed, tracking the cash savings will be straightforward. Where that is not the case, we will estimate the financial impact from proxy indicators such as class sizes, number of streams etc.

4. Projections

4.1. Projections for five years to 2022/23, along with the current year forecast as at Month 3, are set out in appendices as follows:

Appendix 1 – I&E and cashflow
Appendix 2 – balance sheet

4.2. The impacts of a range of alternative assumptions are set out in the sensitivity analysis in Appendix 3.

4.3. The approved financial strategy will provide the parameters for the 2018/19 budget-setting exercise.

5. Recommendation

5.1. FPC is invited to consider the financial strategy and, subject to any amendments, recommend that the strategy approved at the Board meeting on 20 March. This will then provide the parameters for the 2018-19 budget-setting exercise.

Catriona Blake
Vice Principal Corporate Services
27 February 2018

Appendix 1

INCOME & EXPENDITURE / CASH FLOW

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
INCOME						
Funding council grants	27,880	29,812	30,493	30,493	30,493	30,493
Tuition fees and education contracts	3,714	3,714	3,770	3,826	3,884	3,942
Other income	4,473	4,473	4,630	4,792	4,959	5,133
Total income	36,067	37,999	38,892	39,111	39,336	39,568
EXPENDITURE						
Staff costs before VS savings	28,196	30,456	31,445	31,758	32,073	32,391
VS savings (cumulative)	0	(1,000)	(1,010)	(1,270)	(1,283)	(1,296)
VS costs (in-year)	488	0	122	0	0	0
Other operating expenses	7,797	7,797	7,797	7,797	7,797	7,797
Interest payable	208	178	158	138	118	98
Total expenditure	36,689	37,431	38,512	38,423	38,705	38,991
Surplus/(deficit) before depreciation	(622)	568	380	688	630	577
Depreciation - existing assets	(4,507)	(4,507)	(4,507)	(4,507)	(4,507)	(4,507)
DCG release - existing assets	2,795	2,795	2,795	2,795	2,795	2,795
Net depreciation	(1,712)	(1,712)	(1,712)	(1,712)	(1,712)	(1,712)
Operating surplus/(deficit)	(2,334)	(1,144)	(1,332)	(1,024)	(1,082)	(1,135)
Surplus/(deficit) before depreciation	**(622)**	**568**	**380**	**688**	**630**	**577**
Working Capital / Provision movements	(650)	(150)				
Loan repayments	(571)	(571)	(571)	(571)	(571)	(571)
Cash movement	**(1,843)**	**(153)**	**(191)**	**117**	**59**	**6**
Cash balance b/f	2,313	471	317	126	243	302
Cash movement	(1,843)	(153)	(191)	117	59	6
Cash balance c/f	**471**	**317**	**126**	**243**	**302**	**308**

BALANCE SHEET

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Fixed assets						
Existing assets	64,380	59,873	55,366	50,859	46,352	41,845
Total fixed assets	**64,380**	**59,873**	**55,366**	**50,859**	**46,352**	**41,845**
Current assets						
Stocks	20	20	20	20	20	20
Debtors	2,052	2,052	2,052	2,052	2,052	2,052
Cash at bank and in hand	2,313	471	317	126	243	302
Total current assets	4,385	2,543	2,389	2,198	2,315	2,374
Creditors < 1year	6,800	6,150	6,000	6,000	6,000	6,000
Net Current Liabilities	**(2,415)**	**(3,608)**	**(3,611)**	**(3,802)**	**(3,685)**	**(3,626)**
Total Assets less Current Liabilities	**61,965**	**56,266**	**51,755**	**47,057**	**42,667**	**38,219**
Bank loans > 1 year	5,682	5,111	4,540	3,969	3,398	2,827
Deferred capital grants - existing assets	33,007	30,212	27,417	24,622	21,827	19,032
Net Assets excluding pension liability	**23,276**	**20,943**	**19,798**	**18,466**	**17,442**	**16,360**
Net pension liability	20,621	20,621	20,621	20,621	20,621	20,621
NET ASSETS	**2,655**	**322**	**(823)**	**(2,155)**	**(3,179)**	**(4,261)**
Income and expenditure account	11,524	10,091	9,846	9,414	9,290	9,108
Pension reserve	(20,621)	(20,621)	(20,621)	(20,621)	(20,621)	(20,621)
Revaluation reserve	11,752	10,852	9,952	9,052	8,152	7,252
TOTAL RESERVES	**2,655**	**322**	**(823)**	**(2,155)**	**(3,179)**	**(4,261)**

SENSITIVITIES

Element	Base case	Change	July 2019 cash balance	July 2023 cash balance	July 2019 - change from base	July 2023 - change from base
Base case			317	308		
Voluntary severance	2018-19 £1m saving	Target missed by 30%	164	-1,076	-154	-1,384
Voluntary severance	2018-19 £1m saving	Target missed by 6 months	-183	-212	-500	-520
SFC core funding	Flat cash 2020-21 onwards	0.5% reduction	317	-603	0	-912
ESF credits	100% replaced with core	50% replaced with core from 2020-21	317	-1,423	0	-1,731
Increase in total credits	No increase	1% increase from 2019-20	317	1,386	0	1,078
Non-core income	1.5% price, 2% volume (other)	Zero growth	317	-1,879	0	-2,187
Promoted lecturers	Mapped to levels 1/2	Mapped to levels 2/3 but SFC funding at 1/2	-226	-3,724	-543	-4,033
Cost-of-living pay awards	1% academic / support	0% academic until 2020/21	836	3,170	518	2,862
Cost-of-living pay awards	1% academic / support	2% academic / support	21	-4,318	-297	-4,626
On-costs	Current rates	Increase by 2 percentage point from 2018-19	-127	-1,912	-444	-2,220
Funding model changes	No change	£1.2m reduction 2019/20	317	-4,492	0	-4,800