

The funding gap

Funding in schools and colleges
for full-time students aged 16–18

Mick Fletcher and Glyn Owen

**research
report**

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1. Introduction and aims of the project

In December 2004, the Learning and Skills Council (LSC) asked the Learning and Skills Development Agency (LSDA) to investigate the relative levels of funding for learning for full-time 16-18 year-olds in further education (FE) colleges, sixth form colleges (SFC) and schools.

The background to the project is the widespread view, not confined to the FE sector, that FE faces relative under-funding.¹ The LSC was asked by the previous secretary of state to bring forward proposals for reform of the funding of its provision by March 2005, and consideration of the funding gap is part of the review process.²

In that context the specific aims of this project were to:

- assess the existence and scale of a funding gap between schools and colleges
- produce a best estimate of the size of any gap
- recommend how best to move towards a 'level playing field.'

The report is structured as follows:

Section 2	Summarises the methods used in our work: desk research, interviews with experts in the field, funding calculations undertaken at our request by the LSC and presentations to and discussions with the Funding Task Group established by the LSC.
Section 3	Sets out certain underlying principles on which our work relies.
Section 4	Presents an overview of the funding system as it applies to school sixth forms and to colleges.
Section 5	Presents the findings in detail. It covers first the various elements that we see as making up the funding gap, which we calculate as around 13%, and, second, other matters that have been suggested as part of the gap. For some of these other matters we believe that policy needs to change or that further investigation is required, but in no case do we consider that there is a decisive case for early change in funding policy.

¹ In evidence to the Education and Skills Select Committee (see list of references), the DfES permanent secretary described the gap in per pupil funding and the attempts being made to narrow it, and the secretary of state referred to the manifesto commitment to narrow the funding gap.

² The grant letter to the LSC from the secretary of state on 15th November 2004 sets out the terms for the review.

Section 6	<p>This is an analytical section that answers the three questions set out above and, in recommending ways forward, distinguishes between the most serious anomalies where early action is needed, and more complex cases where, for differing reasons, change may take longer to achieve.</p> <p>We estimate that early action would raise the cost to the LSC of educating 16-18 year-olds in colleges by 5-6%, or about £100m, and that a further 5% rise (making 10-11% or some £200m in all) would be needed in due course to eliminate the funding gap. This figure of 10-11% is smaller than our estimate of the funding gap, because behavioural changes induced by funding change might lessen the call on LSC funds.</p>
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2. Methods

This was a short project, conducted in December 2004 and January 2005, and the methods adopted were correspondingly simple:

- desk research, considering published guidance on the LSC funding approach, papers prepared by other commentators and information from the LSC website
- interviews with funding experts from colleges, schools, local education authorities and the Learning and Skills Council
- calculations undertaken at our request by the LSC that aimed to say how much more schools would have received than colleges for educating the cohort of full-time 16-18 year-olds that were actually educated by colleges – a task that was carried out in the best possible way and, albeit with some degree of approximation, in our view with sufficient accuracy for our purposes
- presentation of our findings to an expert group convened by the LSC on 19 January 2004 and to the Agenda for Change Funding Theme Task Group on 2 February 2004 – at each meeting our approach was broadly accepted, though refinements were proposed that have been reflected in this draft report
- analysis from first principles of the material that we assembled.

3. Principles

In carrying out our work, we have had in mind certain principles and other considerations that appear to be generally agreed, namely that:

- a funding gap is not simply a function of funding rates; indeed differences in funding rates are a small proportion of the funding gap
- the aim must be to level up to the position enjoyed by school sixth forms, not level down to current college arrangements
- learners in equivalent circumstances should receive equivalent treatment
- 16-18 year-olds are a minority of school and general FE students, and the costs, markets and objectives of these institutions differ, as do government policies towards them: 16-18 funding is influenced by all of these factors and so, while equity of treatment is the objective, perfect equality as an outcome is unattainable
- the size of the funding gap varies a little from year to year, as retention rates and other factors change; for this and other reasons, it is not possible to produce a precise and indisputable statement of the size of the funding gap; estimates will vary depending on the items it is agreed to include, the order of calculation and the pattern of student recruitment and retention in the year in which an estimate is made – nevertheless we believe that it is possible to produce a robust estimate of the broad size of the gap that is adequate to inform policy.

As a minor final point, we would note that, conventionally, learners aged 16-18 in schools are referred to as 'pupils' whereas those in colleges of the same age are referred to as 'students'. Where the context allows either, we have used 'student,' eg when referring to PLASC – the pupil level annual school census. (PLASC).

4. Overview of the funding system

The systems of allocating funding to school sixth forms (SSFs) and to colleges are similar in general terms, but differ substantially in detail. This introductory section describes the system in general. Section five reviews the individual elements of the system.

The starting point is that institutions are paid a flat *per capita* rate for each student ('entitlement'), plus a base rate for each eligible qualification pursued by their students, so, for example, a student studying four AS levels will generate funding for each of those AS levels. Base rates vary by qualification types. The base rate for AS levels, for instance, is higher than that for GCSEs.

Some programmes of study cost more to deliver than others. Base rates are multiplied by 'programme weightings' to reflect the differences. For instance, the programme weighting for English is 1.00, while that for chemistry is 1.12, so an A-level in English is funded at base rate, while an A-level in chemistry is funded at 112% of base rate. These weightings are based on FE practice, and are applied to schools.

There are limits to the number of qualifications for which an individual student may be funded. Although the precise mechanism differs significantly between schools and colleges, the limits are intended to avoid funding anomalously large volumes of study, such as a student taking 10 A-levels, as the costs do not rise in the same way.

It is more expensive to deliver learning programmes in London and certain other areas than in the country as a whole. Area cost factors allow for this. For instance, the funding levels as calculated above would be multiplied by 120% in inner London and by 107% in Oxfordshire, but would not be increased at all in most of England.

It is also said to be more expensive to deliver learning programmes in deprived areas than in more prosperous areas, and a disadvantage multiplier allows for this factor. In schools, the multiplier is based on the take up of free school meals. In colleges it is based on whether a student lives in an area described as deprived in the Index of Multiple Deprivation.

The funding system outlined above is modified by ministerial guarantees that protect schools funding, notably the Real Terms Guarantee (RTG). The RTG guarantees that no sixth form will suffer a fall in real funding per pupil, compared to its funding in 2000-01, as a result of the LSC funding formula. In 2004/05, the secretary of state agreed a 4% rise in base rates over 2003/04 (ie more than inflation) and this was applied to RTG baselines as well. So, for instance, a school with an RTG level of £4000 per student in 2003/04 would have had that level raised to £4160 in 2004/05, whatever the results of the LSC formula.

85% of schools receive more from the LSC funding formula than the guaranteed amounts under the RTG, but 15% of schools benefit from the RTG as they receive more funding per pupil than they would receive if only the LSC formula was used.

Non-retention arises where a student drops one or more subjects or leaves school or college entirely during a year before completion of the programme. The institution suffers a financial penalty for non-retention through the formula. The specific rationale for penalties is not clearly articulated, but there are two main arguments advanced: first, that non-retention is a form of failure; second, that non-retention reduces school or college costs, meaning that less funding is required. Both arguments have weaknesses. 'Failure' is already measured by the (non) achievement of the qualification aim, while total costs

may be little reduced by the departure of one or even several students from an established class. Be that as it may, both schools and colleges face significant penalties for non-retention as measured by censuses of students during the academic year. There is a key difference between the two, however, as the FE calculation is based on learning aims, whereas the school calculation is based on student numbers.

The case for penalising non-achievement is clearer than that for penalising non-retention. Indeed, it has been argued that all funding should be linked to achievement, rather than being determined through the formula system.³ In practice, however, non-achievement results in modest penalties for schools and colleges.

If schools or colleges recruit fewer learners than anticipated, this is reflected in reduced funding. If more learners are recruited than anticipated, however, the situation is treated differently in schools and colleges. SSFs are funded as of right for unanticipated growth, while colleges are funded only if LSC funds are available and if the college can show that the additional students have generated additional resource requirements.

³ The former Training and Enterprise Councils (TECs) funded some aspects of work-based learning in this way.

5. Findings

Introduction

This section presents the detail of our findings, covering in turn the following:

- The six elements of funding that constitute a clear funding gap as we see it, and which together represent a gap of about 13%, ie if colleges were to receive funding on the same basis as schools they would receive 13% more than at present. Anticipating our analysis in Section six, we would note that filling this gap is primarily a matter of according to colleges the more favourable treatment enjoyed in various respects by schools, rather than raising funding rates paid to colleges.
- The Real Terms Guarantee (RTG), which protects schools from reductions in their funding for sixth forms, resulting from use of LSC formula funding, rather than the LEA funding that they formerly received. We conclude that a temporary measure cushioning some institutions against too rapid a change should not be considered as part of the funding gap, but that indefinite protection at a higher level of resource could be. The RTG is still a relatively new mechanism, and it is unclear at the moment whether it is a temporary 'cushioning' measure, or a permanent feature of the system.
- Three elements of funding that might, conceivably, have contributed to the funding gap, but appear not to.
- Non-formula funding available to schools and colleges, which may contribute to a funding gap, but which is provided for a range of purposes for which calculation is difficult.
- We look at costs as distinct from funding. Costs influence funding and *vice versa*, and there are differences between college and school cost structures. As a matter of principle, and because of the great difficulties of making cost comparisons, we conclude that cost factors should not be regarded as contributing to the funding gap.

Elements of funding that constitute the 'funding gap'

Introduction and summary

FE colleges receive less funding than school sixth forms for educating 16-18 year olds as a result of the operation of the funding formula. In this section we quantify the size of this gap.

FE colleges collect more data on students than school sixth forms. This is most apparent in the censuses conducted during the academic year (Oct, Feb and May). Colleges collect data on each course being done by each student at three census points during the year. Schools use two census points (Sept and Jan) and, in practice, the second is a straightforward count of students rather than a count of the subjects still being studied by each student.⁴

⁴ The second ('PLASC') count does actually collect some limited data on subjects being studied by each student, but this data cannot easily be used by LSC.

Both schools (in the January PLASC) and Colleges also collect data on disadvantage; only colleges use student postcodes and the corresponding official Index of Multiple Deprivation to assess disadvantage, while disadvantage in schools is assessed simply by reference to the proportion of students in the whole school in receipt of free school meals.

Because of the differences in data collection the LSC are able to say how much schools would have received if FE students had studied in school, but cannot say how much colleges would have received if school students had studied in college. The figures that we present in this section have been prepared by the LSC, from its management information records. The figures generally show how much more (it is in every case more) schools would have received if they, rather than FE colleges, had educated the 16-18 year-olds who actually studied in the FE system, though this calculation principle has been modified in unimportant respects, in the light of the precise data available.⁵

There are six factors in the funding formula that work to the advantage of schools. They are listed in the table below, together with the percentage amount by which schools funding is greater than college funding. We then explain the differences in turn.

All of the figures, including the total figure, have been supplied to us by the LSC. We are confident that the individual figures for each factor are correct, as they are derived from the LSC management information system for all students.⁶ The total figure is, however, simply the arithmetic total of the individual figures. This seems unlikely to reflect the real position exactly. Take, for instance, the first two factors. They reveal that schools would have received 2.09% more than colleges because of higher funding rates and 2.78% more because of the special payments to schools in respect of staff pensions, an arithmetic sum of 4.87%. But if the pension contributions are calculated on the raised basis yielded by the funding rates (ie by multiplication, geometrically), the gap resulting from the two factors would be slightly higher – 4.93%. We have not been able to identify in detail whether the factors should be combined arithmetically or geometrically, and suspect that it is a complex combination of the two. The arithmetic total of 13.32% supplied by the LSC may be taken as the minimum figure, and the geometric total of 14.05% may be taken as the maximum, with the actual figure being somewhere between the two.⁶

Elements of funding that are calculable and clearly part of the funding gap, 2003/04	
Factor	Premium enjoyed by school sixth forms %
Funding rates	2.09
Special pension contributions	2.78
Pupil adjustment	2.98
Retention	3.60
The cap and taper	0.80
Disadvantage	1.07
Total	13.32*
Source: LSC calculations	
Note* 13.32% is the arithmetic sum provided by LSC. The geometric sum is 14.05% and, in our judgment, the overall sum of the six factors is somewhere between these two figures (see text).	

⁵ The principle occasionally had to be modified. For instance, the pensions differential (2.78%) is simply the percentage addition to school sixth form funding represented by the £38.5m of additional pension funding received by school sixth forms.

⁶ It is also the case that the figures derived will differ from year to year, depending on differences in the cohorts of learners recruited. If, for example, in one year the retention rates of FE students are significantly worse than average, the calculation for that year will show a wider funding gap. Nevertheless, there is sufficient stability in the factors identified year-on-year for this detail to be ignored when determining policy.

The calculations summarised above mean that, had the FE sector been funded on the same basis as school sixth forms, it would have received 13-14% more funding for 16-18 year-olds than it actually did.

The calculations do not, however, imply that FE funding rates should be raised by 13-14% – the difference in funding rates is only 2.09% and correcting the whole gap through changes to funding rates would have inequitable effects from one college to another and would create new inequities between colleges and schools in particular areas.

Nor should FE colleges necessarily be treated in the same way as schools are currently treated:

- On the face of it, the FE system may be thought a better system in several respects, for instance in its treatment of retention and disadvantage (see below), though moving to the FE system might conflict with the principle of ‘levelling up’ to the schools position, rather than ‘levelling down’ to the FE position.
- FE may need less funding in certain respects, for instance, schools may conceivably need a greater funding adjustment for pensions than colleges (this is a special case of the relationships between costs and funding that we discuss later in this report).

Funding rates (contribution of 2.09% to the funding gap)

FE colleges are paid on average lower rates for qualification aims than school sixth forms. This difference originated when the funding for school sixth forms was transferred to the LSC, and has been perpetuated through ongoing inflation increases and guaranteed minimum uplifts for schools. While there is a clear historical explanation for how this came about, there would seem to be no logical justification for having different schedules of rates for equivalent work.

Special pension contributions (contribution of 2.78% to the funding gap)

The recent difficulties with funding pension contributions for teachers and lecturers – both groups are, in the main, in the Teachers’ Pension Scheme (TPS) – have led government to provide additional funding for schools, which raised their LSC funding by 2.78%. A similar adjustment was made to the overall funding for colleges, though the sum is included in the published funding rates. These two factors should therefore be treated as one.

As with the funding rates argument, the basic position is that colleges should receive the same as schools, though with an adjustment to reflect differences in the pension contributions position. The colleges may be in a marginally more favourable position than schools because of their greater use of staff such as hourly paid lecturers who, even if eligible, may choose not to join TPS, and because they have some lecturing staff who are in non-TPS schemes.

Pupil adjustment (contribution of 2.98% to the funding gap)

If a school recruits more students than planned it automatically receives proportionately more funding.⁷ School funding for sixth form students was 2.98% higher on this account.

When colleges recruit more students than planned, there is no automatic entitlement to increased funding. The college must negotiate any increase with its local LSC, and any increase is contingent on the college displaying a need – ie demonstrating that it is unable to find the extra resources required from other areas of its budget – and on the local LSC having funding available. There are no statistics available on the extent of any extra funding received by colleges on this account, but such funding is believed to be small.

There would not appear to be any justification for the difference in treatment. Given the government's view that education is the best option for the great majority of 16-18 year-olds, there is a strong *prima facie* justification for encouraging the maximum possible level of recruitment, whether by schools or colleges, and automatic funding of increased numbers is the natural way to do this.⁸

Although the LSC has quantified the extent of the gap as 2.98%, this is reduced to an unknown though probably minor extent by local funding of unplanned growth in colleges.

We would note further that this factor is fundamentally different from the others, in the type of behavioural response that it is likely to elicit. At present colleges have a strong disincentive to recruit beyond plan, whereas schools have an incentive to maximise recruitment. If colleges are funded on the same basis as schools, there will be a one-off increase as the stock of unfunded students in colleges attracts funding at the average rate. Thereafter, the LSC funding to schools and colleges taken together will rise only if there is a resulting increase in cohort participation (rather than a redistribution of learners between institutions). Closing this sizable element of the funding gap might have a relatively smaller impact on the funding requirement from the LSC.

Retention (contribution of 3.60% to the funding gap)

Retention is one of the most contentious areas of the funding system. In essence, the system aims to ensure that schools and colleges receive reduced (or even zero) funding when students fail to remain in class for the whole academic year, or until the completion of their programme.

The specific rationale for penalising non-retention is unclear, though the possible justifications are well rehearsed. One argument is that if a student leaves there is a failure to achieve, but this is, in a sense, covered by the (separate) achievement factor in the funding formula. A second argument is that if a student leaves there is less work to be done by the school or college and therefore less cost; but it is questionable whether departures of individual students from classes lead to cost savings as, once running, the cost of a class is largely fixed.⁹

The schools system is to fund all students in respect of their qualification aims as recorded in September, unless they are recorded as having left in the January PLASC

⁷ The method of operation of the secretary of state's guarantee may mean that, for some schools, the increase in funding is slightly less than proportionate to the increase in numbers.

⁸ Logic suggests that this principle should also be extended to young people participating in work-based learning.

⁹ Though large colleges in particular are sometimes able to effect cost savings by merging classes.

return, in which case only half a year's funding is paid. A school sixth form with 100 students each starting four qualifications in September, but which was down to 90 students in January, would receive funding in respect of 380 qualifications: 90 students X four qualifications for whole year (=360), plus 10 students X four qualifications for a half year (=20), ie a loss of 5% of funding compared with 100% retention.

It should be carefully noted that even if by January the 90 continuing students have, on average, dropped one subject and are by then doing three subjects rather than four, there is no reduction in funding on this account.

Some of our consultees argued forcefully that some schools exploit the subject position by encouraging students to start many subjects in September in the knowledge that this will determine total funding for the whole year, even if some subjects are quickly dropped. We have seen no evidence of this, but it seems undesirable that the incentive for such behaviour exists. It is also argued by schools that the FE system encourages colleges to maintain the size of students' programmes, even when it might be in their best interests to drop a subject. Equally we have no evidence of this, but were it to happen it would be undesirable.¹⁰

The college system is more precise. There are three census points and at each point the number of subjects being studied by each student is recorded. Suppose a college starts with 100 students each doing four subjects, but is down to 90 doing 3.5 subjects by February, and to 80 students doing 3 subjects by Easter. The college would receive 100% funding in respect of the 240 qualifications pursued throughout the year, two-thirds funding in respect of the 85 further qualifications pursued until Easter, and one-third funding in respect of the 85 further qualifications pursued until February. In total this would mean a loss of 18.75% of the funding that would have been received if all students had continued to pursue all of their (original) subjects throughout the year.

The examples above have been contrived so that the real pattern of retention might be approximately the same in the school as in the college, but the school loses 5% of funding while the college loses 18.75%. Some of our college consultees did indeed indicate to us that a gap of this order of magnitude (ie 13.75% in this example) actually exists.

Despite the plausibility of the above example, the LSC's calculations indicate that schools (on their methodology) would have received just 3.6% more than colleges for educating the college FE group.

It is apparent that colleges differ widely in their patterns of retention. Some sixth form colleges in particular appear to have very high retention and would benefit hardly at all from adoption of the schools system, while some general FE colleges would benefit substantially.

The cap and taper (contribution of 0.80% to the funding gap)

Some students pursue an unusually large number of qualifications. Without a mechanism for preventing this, such students would generate substantially more funding for their school or college than a normal full-time student.

¹⁰ The data does not allow us to assess this claim – we don't have individual learning aim data for schools and it seems we can't actually check how much drop-out there is – so success rates can't be calculated as in FE.

Where a student pursues more qualifications than five AS levels (or equivalent), funding for additional qualifications is first reduced (by the taper) and ultimately capped.

The system applies in the same way to schools and to colleges with the crucial difference that it is applied to individual students in colleges, but to an average across all students in schools.

It is quite common to find individual students taking sufficient qualifications to be affected by the taper and the cap, and the LSC estimates that college funding for 16-18 year-olds is reduced by 0.9% by the taper and cap. It is, however, unusual for an institution to find that its students are, on average, taking sufficient qualifications to be affected. As a result, the LSC estimates that the cap and taper reduce school funding by just 0.1%.

Disadvantage (contribution of 1.07% to the funding gap)

Students from disadvantaged areas are generally viewed as being more costly to teach than students from other areas.

Student disadvantage is assessed for purposes of college funding by reference to the government's Index of Multiple Deprivation (IMD) for the area of residence of the individual student. It is assessed for purposes of school funding by reference to the proportion of students in the whole school entitled to free school meals.

Deprivation is difficult to assess. In our judgment, the IMD is the better method; a finding that is reinforced by the fact that entitlement to free school meals across an 11-18 school may not be at all closely related to deprivation among that school's 16-18 year-old students.¹¹

Whatever the merits of our tentative conclusion that the IMD is the better measure of deprivation, we suggest that a single system is employed across both sectors, so as to eliminate the funding differential that currently arises from this factor.

An element of funding that is calculable, but is not as clearly part of the funding gap: the Real Terms Guarantee (RTG)

The Real Terms Guarantee was introduced when funding for school sixth forms switched from LEAs to the LSC. The LSC funding formula raised the prospect that some schools would receive less funding for their sixth forms than under the previous arrangements. To obviate this possibility, the government guaranteed that no school that maintained its student numbers would receive less, in real terms, than under the LEA arrangements.

Every school sixth form has a base level of funding, represented by its LEA funding prior to the LSC's assumption of responsibility, which is raised annually in line with inflation. The school receives whichever is the higher of its funding entitlement, the LSC formula, or its RTG figure.

The RTG was also affected by the (separate) secretary of state's 4% guarantee, ie a guaranteed 4% rise in funding for every school in 2004/05 over 2003/04 funding.

¹¹ Although this argument has support in schools, the LSC modelling suggests that the change in calculation would cause turbulence at individual school level.

Schools on the RTG receive more funding than if only the LSC Formula was used. They receive the equivalent funding they received in 2000-01, uprated for inflation and adjusted for pupil numbers.

The effect of the RTG is to raise funding for school sixth forms by 1.20% compared with the funding they would receive in respect of the formula alone.

It is understandable that colleges, which do not benefit from the RTG, should regard RTG funding as part of the funding gap. Were it to be abolished, the schools quantum and learner numbers would remain the same and it is probable that it would simply be translated into an increase in schools rates.

It is possible to argue that the RTG is required because schools and colleges differ in certain relevant respects. School sixth forms are much smaller than college 16-18 provision - on average school sixth forms have about one-eighth as many 16-18 year-olds as colleges.¹² Schools have far less funding flexibility than do colleges. There was therefore a justification for offering schools a degree of protection from the full operation of the formula, at least for the first few years of the formula's operation. It should also be noted that any gap on account of the RTG arises not between the two sectors (schools and FE), but between RTG schools on the one hand, and colleges and all other schools on the other hand.

It is also the case that as formula funding per student slowly rises in real terms, the number of schools benefiting from the RTG will slowly fall, and in that sense the RTG can be seen as a transitional arrangement, though this argument is seriously weakened by the lack of an explicit end date and the application to the RTG of the secretary of state's 4% guarantee. In 2005/06, 85% of schools will be on the LSC formula and only 15% on RTG, a figure that has been reduced from 37% in 2002/03.

In conclusion, we do not view the temporary benefit that some schools have received from the RTG as part of the funding gap, but the aggregate resources added to schools funding in order to finance it should be. It may well prove necessary to introduce a new guarantee to schools and colleges to mitigate the consequences of moves to eliminate the gap.

Elements of funding that are calculable and clearly not part of the funding gap

Introduction

In this section we cover three factors that, it has been suggested, might contribute to the funding gap:

- .
- achievement funding
- area cost adjustment
- non-Age Weighted Pupil Unit (AWPU) deductions.

It is easy to demonstrate that the first two do not contribute to the funding gap. It has been suggested that the third (non-AWPU deductions) might work to the disadvantage of schools and thus reduce the funding gap between schools and colleges arising from the

¹² The argument is much more straightforward for sixth form colleges, which may have up to 2000 pupils on A-level programmes, far more than the largest school. Many general FE colleges offer such a wide range of programmes that they might be better considered as a collection of small units.

sources already discussed in this report. In fact, however, we do not consider there to be any such effect.

Achievement funding

A comparatively small amount of funding is contingent on learner achievement of the qualifications for which they have studied. The system works rather differently for schools and colleges, but the LSC's calculations reveal that, on aggregate, schools would receive no more funding than colleges do presently for the level of achievement attained by college students – in other words, no funding gap arises on this account. Some misunderstanding may arise from the fact that there is a difference in the way that success rates are calculated for schools and colleges. The college success rate is calculated on the basis of the number of qualifications for which a student enrolls, whereas the schools calculation takes into account only those qualifications for which the student is entered (ie it ignores subjects dropped in-year and is therefore more favourable). While there is certainly an issue here that needs to be addressed, it does not affect the funding calculation.

It is worth noting that some colleges and schools refer to the concept of 'attrition' - that is the combined effect of non-retention and non-achievement. Suppose 100 students start a course and some drop out and some others, though remaining to the end of the course, fail to achieve their qualification. Funding will be reduced on account both of non-retention and of non-achievement. The total loss, compared with the funding that would have resulted from all 100 students staying the course and achieving their qualification, is referred to as 'attrition'. The funding gap arises, however, from the differing treatment of retention only, and not from differing treatment of achievement.

Area cost adjustment

The area cost adjustment factors are multipliers applied to funding to reflect the higher cost of delivering education in London and nearby areas. Schools and colleges use the same multipliers and area definitions, so no funding gap arises from this factor.

Non-AWPU deductions

Most LEA funding for schools (for students aged under 16) is determined by AWPU. The most obvious system would be to allocate the available funding on the basis of school pupil head-counts, but age-weighting is used to reflect more accurately the differing costs of educating students of different ages.

LEAs have discretion to fund some costs on a non-AWPU basis, because they are not closely related to pupil numbers. For instance, an LEA may have some small schools with unusually extensive grounds, or listed buildings that are expensive to maintain, and larger schools that are more economical in that respect; they may decide to meet actual maintenance costs rather than paying on an AWPU basis. Most schools therefore receive non-AWPU funding as well as a much larger element of AWPU funding, though some LEAs choose not to use the non-AWPU system at all, and the LEAs that do use it vary greatly in the share of expenditure that is counted as non-AWPU.

The LSC (like some LEAs) does not operate a non-AWPU system. LSC payments are intended to cover the whole cost of educating 16-18 year-olds. Where an LEA meets (say) maintenance costs for an 11-18 school, the share of those costs attributable to 16-18 year-olds risks being double funded, once by the LEA and once by the LSC. To avoid this risk, LEAs are permitted to make non-AWPU deductions from school funding. In a 1000 pupil school with 150 (15%) 16-18 year-olds, the LEA could make a *pro rata* deduction of

£15,000 from non-AWPU funding of £100,000 to allow for the share of cost that, notionally at least, is included in the LSC funding for the school's 16-18 year-olds. Non-AWPU deductions can be significant - hundreds of thousands of pounds in a large school in an LEA with substantial non-AWPU funding. It is understandable that the head teachers most affected compare their non-AWPU deductions with discretionary expenditures, such as those on teaching materials, and conclude that non-AWPU is a major source of disadvantage.

The practice of making non-AWPU deductions varies, with little apparent justification, from one LEA to another.

Nonetheless, the principle of non-AWPU deductions is fair. Indeed it is unfair not to make such deductions, since where an LEA double funds part of a school's costs by failing to make non-AWPU deductions, the burden is borne by the LEA's other schools (11-16 and junior schools) whose total funding is correspondingly reduced.

We recognise that the lack of uniformity in application of the non-AWPU deduction system is a significant problem, but it is not, we suggest, a problem that bears on the funding gap.

Elements of funding that are difficult to calculate and are not clearly part of the funding gap

Introduction

In this section we review four elements of funding that do not contribute, unambiguously, to the funding gap. In each case there is some element of doubt and a need for further research, which may in due course identify that there is indeed some inequity of treatment that requires an adjustment to the funding system. The four elements are:

- non-formula funding, such as the Standards Fund for schools
- capital expenditure
- additional learning support
- learner support.

Non-formula funding

Both schools and colleges receive funding outside the formula system for particular purposes. For instance, the Association of Colleges (AoC) estimates that secondary schools currently receive sums equivalent to £226 per student from the Schools Standards Funds, and the LSC website summary of college accounts reveals that colleges received £18.5m in 2002/03 from the European Social Fund and £11.6m for Centres of Vocational Excellence (CoVEs).

Such funding arrives under numerous budget heads and – sixth form colleges aside – it is frequently difficult to assess whether the funding is aimed at 16-18 year-olds, primarily, in part or not at all.

Some funding is simply to reimburse particular expenditures, and often not in full. The recipient institution may well find itself no better off, and sometimes even worse off, as a result of such funding.

We have not found it possible to assess whether non-formula funding is greater for 16-18 year olds in schools than in colleges, nor, even if it is greater, whether the additional funding for schools constitutes part of the funding gap or is simply a reimbursement of direct expenditure (as with additional learning support – see below). As a result, we see non-formula funding as a potential contributor to the funding gap, but it would take much more research to quantify any such contribution.

Capital expenditure

The arrangements for funding capital expenditure differ markedly between schools and colleges.

Funding for school capital projects is channelled through LEAs. There are three main routes. First, schools receive a relatively small sum allocated on a formula basis to cover minor capital works. Second, major projects are funded by the LEA using funds allocated to each LEA for that purpose. Third, the government's Building Schools for the Future programme operates in a growing number of LEAs as it is rolled out across England; its aim is the renewal of every school over a 10-year period. Expenditure through these routes is currently some £6bn a year.

It is not possible at national level to differentiate between school capital expenditure intended to support sixth form activities and expenditure intended to benefit younger students. Indeed, while some expenditure might be clearly attributable to one group or the other, much expenditure will benefit both groups.

Schools are not usually called upon to make major contributions to the cost of capital projects, though they may be asked for a modest contribution – typically less than 10% – to the cost of a major project, perhaps by using part of their formula-funded minor capital budget. There are examples of schools using other sources of funding, eg from foundation funds.

College capital expenditure is essentially the responsibility of each college. Colleges can seek grants from the LSC, and will normally receive up to 35% of the cost of projects meeting the LSC's criteria, and occasionally more. Colleges can also seek grants from other public bodies, such as Regional Development Agencies.

Colleges, unlike schools, are expected to make major contributions to capital expenditure from their own resources, from asset sales, from surpluses of revenue over expenditure and from taking out loans to be repaid from future operating surpluses. In 2002/03, colleges undertook capital expenditure of £575m¹³ and received £213m (37%) of capital grants, primarily from the LSC but also from other public bodies.¹⁴ They also received £94m from asset sales.

The LSC capital budget, the bulk of which is spent on colleges, is £400m in 2005/06, and this figure is set to expand to £596m in 2007/08.¹⁵

The same data on college and school capital expenditure can be presented in two different ways.

¹³ Summary accounts of colleges as published on the LSC website.

¹⁴ Including Higher Education Funding Council for England (HEFCE), to a very minor extent.

¹⁵ Grant letter of 15 November 2004 from secretary of state to LSC.

Colleges argue that schools receive virtually 100% of the cost of their capital expenditure programmes, while colleges receive only (say) 40%. The annuitised costs of the capital expenditure that colleges have to bear themselves is a charge on their revenues and constitutes a significant part of the funding gap, estimated by the AoC as being equal to about 5% of college revenues.

We would note, however, that the FE sector taken collectively makes more use of past accumulated surpluses than it does of loans. In 2002/03, FE colleges held between them cash and short term investments of £962m and had total loans of just £396m. Interest paid on loans was £30m and was outweighed by £37m of interest received.

The alternative argument is that schools receive £6000m a year from the government for capital, while colleges receive perhaps £400m a year via the LSC and other public bodies. Colleges, however, have far more flexible funding arrangements than schools, and are able to add funds to their (government) allocation by the use of past surpluses, asset sales and so on.

The fundamental question is whether the right amount is being spent on school and college capital expenditure. The right amount, in principle, is the amount that funds all projects offering social rates of return, in excess of the rates published in HM Treasury's Green Book. It may not be possible to undertake all such projects in the short run, given pressures on public finances, but this 'capital rationing' case is easily accommodated by the standard discounting tools.

It is not possible for us to judge, even approximately, whether the right amounts (in Green Book terms) are being spent. The schools sector is, of course, much larger than the FE sector and has a considerably larger capital expenditure programme, but whether the difference is of the right amount is unclear and would require further analysis, well beyond the scope of this project.

Additional Learning Support and statemented pupils

Additional learning support in colleges consists of extra support offered to learners, in respect of their learning needs, to enable them to access their main learning programme. For instance, a learner with a major disability may need to be accompanied by a dedicated support worker whenever in class. The requirement for support is professionally assessed and, above a minimum threshold, its cost is reimbursed to the college.¹⁶

Colleges argue that the system has no implications for their funding. Although the funding passes through the college accounts, it is 'in and out' and has no effect on their budgets. It is, in reality, as if an external agency (say the LEA or a charity) provided and paid for the support, without the college being directly involved.

The parallel system in schools is represented by funding provided for pupils with statements of special educational need, plus an additional sum for those with needs but without statements. For those who have them, statements set out the additional resources required to meet a pupil's extra needs, and additional funding is provided outside the formula to meet them. As with the argument above, the school generally derives no specific benefit from this funding.

¹⁶ In 2004/5, with the introduction of plan-led funding, the FE system for ALS changed from one based on the reimbursement of individual claims to one based on a block allocation, derived from the existing pattern of expenditure.

There are, however, several differences between the two systems. The major one is that additional learning support, which is equal to about 7% of college funding for full-time young learners, is larger as a percentage of college budgets than the funding associated with statements of special educational need for learners in maintained school sixth forms. The question for this research is whether this fact constitutes a funding gap.

The provision of ALS has been thoroughly researched recently by LSDA on behalf of the LSC.¹⁷ The conclusion of the research is that colleges are able to support a greater number of learners through ALS than schools are through statements and 'school action'.¹⁸ This partly reflects the fact that colleges are likely to attract a greater number of learners who need additional support (selective school sixth forms are less likely, for example, to have many learners with basic skills needs). It is partly a reflection of the perception in schools that they have no funding to meet lower level needs, which in turn leads some potential learners to transfer to colleges. While the official LSC stance is that appropriate funding for the additional needs of non-statemented pupils is included in the schools rates, the LSDA research concludes that a more explicit identification of the availability of such resources would lead to an increase in appropriate provision.

In relation to the funding gap, however, our view is that this difference should count as part of the funding gap calculations if it derives from the application of different policies to the same or similar populations. It should not count if it derives from the application of the same or similar policies to different populations. This logic is consistent with how we have treated any differences arising from the application of programme area weights, or the fact that pupils in some institutions follow larger programmes than in others.

The two populations are clearly different. While provision in school sixth forms is predominantly at Level 3, colleges teach a much higher proportion of learners at Levels 1 and 2.¹⁹ The groups also differ in terms of prior attainment, with colleges attracting a higher proportion of low attainment students, and a higher proportion from disadvantaged areas. These differences appear to be significant for the provision of ALS; for example, in general FE colleges, around 7% of pupils studying at Level 3 receive some form of additional support, whereas at Level 1 and Entry level the proportion is almost a quarter. The amount spent per learner at Level 1 and Entry level is around four times the expenditure per head at Level 3.

Some of the learners funded through ALS are taught in discrete courses for learners with learning difficulties. Although funded through ALS this is, in effect, programme funding that reflects the lower group sizes needed by such students. The proper comparison for this group is with similar learners in special schools where a higher rate of funding than normal school rates would apply.²⁰ The 15% of ALS attributable to this element should not be counted as additional to main funding, so the extra resourcing from ALS is around 6%.

Although it can clearly be demonstrated that the college and school post-16 populations are different, it is more difficult to assess whether the treatment of learners in similar circumstances is equivalent. This is because the application of both Special Educational

¹⁷ Fletcher, Faraday et al (2004) *Improving arrangements for Additional Learning Support*. London: Learning and Skills Development Agency.

¹⁸ 'School action' refers to help provided by a school for pupils who have special educational needs.

¹⁹ In the 16-18 age group 33% of those studying A/AS levels are in colleges compared with 90% of those whose highest qualification aim is at Level 1 or 2 - SFR03/2005.

²⁰ For a summary of funding arrangements in special school 6th forms see: Fletcher M, and Kirk G (2004). *Funding Special School 6th Forms*. London: Learning and Skills Development Agency.

Needs (SEN) resources in schools, and ALS resources in colleges, is non-formulaic. There is no school sixth form calculation that can be applied to FE numbers. It is, however, possible to form a reasonable assessment of the level of SEN resources that the LEA schools approach would deliver to the 16-18 FE population, by looking at the resources delivered to the maintained school secondary sector as a whole.²¹

For 2004/5 local authorities delegated £618m to secondary schools (excluding special schools) for SEN. In addition, they allocated £250m for central SEN services (such as educational psychologists), of which the *pro rata* share of secondary education would be £55m. They also allocated £203m for non-delegated SEN provision, covering items such as provision for pupils with statements, provision for pupils without statements and placements at independent secondary schools (other than special schools). If half of this latter figure is included as analogous to ALS, the total provision is around £775m or 6% of the £13bn budget for secondary education.²²

The clear implication of this is that if the population of 16-18 year olds in the FE sector (or in school sixth forms) were representative of the secondary school population as a whole, the schools funding model would provide additional resources totalling around 6% of the overall budget. We know, however, that the populations of school sixth forms and FE colleges differ from the secondary population as a whole. The former in a way which makes them less likely to need additional resourcing and the latter in a way which makes them more likely to do so. It is logical to infer that observed differences between the resources allocated for SEN/ALS in the 16-18 phase derive from such compositional effects, rather than the application of different principles. We can therefore conclude that this should not be considered as part of any funding gap.

Learner Support

Learner support is intended to help learners participate in learning (as distinct from helping the actual process of learning), for instance by contributing to the costs of childcare and transport for disadvantaged learners. By far the largest element of public expenditure under this heading consists of Education Maintenance Allowances (EMAs), the application of which is formally neutral between schools and colleges. It is probable that the number of learners receiving EMAs is greater in the college sector than in schools, because of the social class composition of their respective intakes, but since this money is paid directly to the learner it is not relevant to the funding gap.

In addition to EMAs, the LSC distributes learner support funds and manages arrangements to support learners at residential colleges. In broad terms, funding per 16-18 year-old learner under this head appears to be about 20% higher in colleges than in schools, though some of this difference is accounted for by colleges having a higher proportion of disadvantaged students than schools. Some is also accounted for by the fact that college students are more likely to incur high indirect costs – travel to a specialist centre, or the high equipment costs associated with, for example, craft catering courses.

The amount of spending on learner support is small in comparison with total funding and the resources are directed to the learner not the institution. Any benefit to colleges as a

²¹ The level and distribution of SEN resources in school sixth forms is essentially a reflection of LEA practice, rather than a result of LSC policies.

²² Section 52 : The Education (Budget Statements) (England) Regulations 2004-05. Total planned expenditure on special needs education in England in 2004-05. As reported by LEAs as at 10th March 2005.

result of this support mechanism has, at most, a very small offsetting effect on the funding gap.

Costs

Costs and funding are inter-linked. Over the years, a view has developed about how 16-18 year-olds, other than those in work-based learning, should be educated. They study in groups led by suitably-qualified teachers or lecturers paid, for the most part, in accordance with national scales, in buildings that meet basic standards of comfort, and using suitable support materials (including the traditional books and paper, and ICT). Provision requires support services, ranging from headteachers, college principals and other senior managers, to administrative staff and manual staff. In practice, government has to meet the costs of this system.

There is continuous upward pressure on real costs, as workers in education pursue higher standards of living, as educationalists seek to raise the quantity of inputs per student (eg through smaller class sizes), and as new methods of teaching and learning develop (eg through ICT). Properly managed, increases in costs can yield substantial benefits in terms of improved learning and achievement by students.

The extent to which government meets the upward pressure on costs is a political choice, based on the state of government finances, government attitudes to education and to taxation, competing claims on tax revenues and many other factors. Once the political decision is made, there is general agreement that the funding mechanism should allocate the available resources as equitably as possible, though that mechanism is itself the subject of political decision-making, given the vagueness attached to the idea of equitable funding.

In the past two to three years, the government's policy response to cost pressures in schools has been made somewhat more explicit. The government now calculates and publishes its own estimates of the cost pressures on schools, expressed as percentage rises in costs each year, and indicates what its response will be.

To the extent described above, aggregate costs determine aggregate funding, and funding determines how far costs can rise.

There is a consensus that the funding of 16-18 year-olds should be equitable between schools and colleges (though a recognition that equity may take some time to achieve). There is, however, doubt about whether equity means equality of funding. Abstracting from definitional difficulties, does equity mean that a full-time A-level student should be funded at the same rate, whether studying in school or in college?²³

If equity does indeed mean equality, then under the current system colleges would receive funding equal to that in schools and determined for the future (pragmatically if not logically) by cost pressures faced by schools. The logic of such a system might be flawed, though doubtless many colleges would regard that as a price worth paying for closure of the current funding gap.

The alternative to the argument that equity means equality is to look at the differing cost circumstances of the two sectors, and to take that into account in setting funding rates. The AoC have argued, for instance, that colleges face a range of costs, associated with

²³ The question might be posed rather more starkly in relation to apprenticeship training where the cost profile faced, for example, by a trainee employed in the retail sector may be substantially different to class-based instruction in a school or college. Should a 17 year-old on a Level 3 programme receive the same resources irrespective of sector?

governance and other matters, that schools face to a lesser degree, if at all. As a result, they argue, equity in funding requires that colleges should receive greater funding per student or per qualification aim than schools, to reflect their higher costs.

The AoC quantifies two specific cost pressures on colleges that they see as major: capital expenditure and irrecoverable VAT. Together, these two factors make up to approaching half of the funding gap, as estimated by the AoC. We have covered capital expenditure earlier in this report.

The VAT issue may be simply described. Most expenditure by schools and colleges is on staff, where no VAT issues arise. Moreover, some of the supplies they buy, such as books, are not subject to VAT. Nonetheless, there is substantial expenditure on goods and services that are subject to VAT. Schools are allowed to reclaim the VAT that they have paid, while colleges are not. The AoC quantify the burden on colleges in respect of their 16-18 work as £75m a year. There would be serious administrative difficulties in allowing colleges to reclaim VAT. First, the EU would oppose any extension of exemptions; second, it would almost certainly prove impractical to confine an exemption to colleges' 16-18 work – it would need to apply to all work done by colleges; third, private colleges and providers would doubtless claim that they should be entitled to exemption as well, on competition policy grounds. Notwithstanding these difficulties, if the funding system were to take differing cost structures into account, the current differing VAT position across the sectors would be an anomaly to be corrected, whether by additional funding to compensate colleges, or by exemption.

Other commentators, including several of the individuals consulted for this study, have pointed out, however, that colleges enjoy a range of cost advantages compared with schools. The most commonly cited are:

- economies of scale in provision
- lower average salaries
- a smaller average input of teaching hours.

Economies of scale in provision

Colleges have on average about eight times more 16-18 year-olds than school sixth forms, and there are clear opportunities for economies of scale. Sixth form colleges in particular can offer a reasonable range of A-level and other provision without risking the diseconomies resulting from small class sizes.

It has been suggested that some colleges, for good educational reasons, more or less consciously re-invest the savings from these economies of scale in improving the range and quality of their offer. Plainly, with any given cohort size, the probability of diseconomies arising from small classes depends on the number of subjects offered. A college with 1000 16-18 year-olds on A-level programmes can expand the number of subjects that it offers, so that it enjoys no more economies of scale than a school with 200 such students.

Despite this effect, it appears certain that one way in which colleges have coped with the funding gap is through economies of scale.

Lower average salaries

Colleges are free to set their own staff salaries, while schools adhere to national pay scales. It is difficult to compare the position in the two sectors, but it is widely accepted that average salary cost per hour taught is higher in schools than in colleges, partly as a result of the average salary of full-time classroom teachers now exceeding that of college lecturers, and partly as a result of colleges' greater use of inexpensive hourly-paid staff. Evidence, admittedly on very small samples, from the LSDA studies on understanding costs confirms this picture but suggests that the average cost of a lecturer in the sixth form college sector is close to that in schools, and over 10% higher than in FE. A broad generalisation might be that while sixth form colleges cope with the funding gap through economies of scale, FE colleges do so through lower salaries.

A smaller average input of teaching hours

It has been suggested by some in the schools sector that full-time 16-18 year-old students in colleges receive fewer hours of tuition per year than their counterparts in schools. College representatives say this is not the case. Again, we are not in a position to say whether or not this is true.

The overall cost position

We have not investigated the various cost factors in detail, and it would be exceedingly complex to do so. There is, however, general agreement that, for a combination of the reasons reviewed above, costs in colleges are lower than in schools. The existence of a funding gap, in conjunction with the observed fact that both schools and colleges achieve broad financial balance between income and expenditure, demonstrates that college costs are lower. Colleges receive less funding, but they are not in deficit, so their costs must be lower.²⁴

Colleges respond that their costs are lower than those of schools because they have had to adapt their operations to the reality of lower funding. On one specific point, they argue that lecturers' salaries have fallen behind those in schools because lower funding has meant that colleges cannot afford to pay as much as schools. We do not doubt that this is correct, though it is worth saying that the position could not easily be reversed: there is, for instance, no mechanism for ensuring that lecturers' salaries would catch up with schoolteachers' salaries if the funding gap were removed.

Our general conclusion is that cost differentials between the two sectors should be ignored in reaching funding decisions, for the following reasons:

- There is a commonsense logic in government paying the same price for the same service - regardless of costs.
- Repeated experience of attempts to assess and compare costs for purposes such as the construction of programme weights has shown that the discussions are exceedingly complex – it would take years to compare school and college costs effectively and fairly, if the task could be accomplished at all.
- The correction of some clearly identifiable cost differentials – such as the VAT position – without taking a comprehensive view of costs would in itself be unfair.

²⁴ It is logically possible that colleges could achieve financial balance through cross-subsidy from other activities. While this may be true in individual cases, it is unlikely that either adult FE, or other sources of college funding overall, have sufficient scope to cancel out a shortfall of the scale we have identified.

- More work needs to be undertaken to understand the potential for economies of scale in some contexts.

6. Analysis

This section aims to reach conclusions on each of the specific aims of this project, namely to:

- assess claims about the existence and scale of a funding gap between schools and colleges
- produce a best estimate of the size of any gap
- recommend ways forward.

The government is committed to closing the funding gap between schools and colleges, in respect of their 16-18 year-old students, by raising college funding, rather than by reducing school funding, and this principle has widespread support.²⁵

The government is not, as we understand it, committed to any specific definition of the funding gap, nor to a specific timetable for closing the gap, however defined.

Our best estimate, presented above, is that the funding gap is about 13%, ie FE funding would need to rise by 13% to match the funding that schools would receive for educating the same students that FE educates at present.

The LSC accounts for 2002/03 show that the cost of 16-18 provision in further education was £1881.6m. The amount will have risen since then, but a small part of the expenditure will have been on part-time 16-18 year-old students, who are outside the scope of this report. To provide a rough indication of the overall cost of the changes we propose, we have used £1881.6m as a basis. Using that basis, the 13% funding gap amounts to £245m. We explain below, however, our reasons for believing that closing the funding gap would result in an increase in LSC expenditure smaller than £245m.

A large, general increase in funding rates payable to FE colleges would not be the right way to close the funding gap. In our judgment, the right way is to increase FE funding rates so as to close the (small) gap in national funding rates, and to make a series of policy changes aimed at putting FE and schools sixth forms on an equal footing. The policy changes will tend to raise FE funding, but the extent of the rise will depend on the behavioural response of colleges and schools to the changes. Some of the changes require detailed investigation before implementation.

In our view, fairness requires that the changes be implemented as quickly as possible, but we accept that budgetary restrictions may moderate the pace of change. We suggest a distinction between glaring anomalies that should be removed as soon as practicable, and other anomalies where the extent of the discrepancy is less clear or where, for some other reason, such as the need for research, immediate implementation is unlikely to be possible, and where, as a result, the timing of change might be phased.

We are aware, of course, that plan-led funding for colleges is being progressively implemented across the FE system and that the funding system itself is currently under review by an LSC task group. Our recommendations may need to be adapted to reflect those changes. In particular, if schools and colleges were funded on the basis of FTEs

²⁵ See, for instance, the FE Focus section of the Times Educational Supplement of 11 February 2005, where Sir Mike Tomlinson, the Association of Colleges, the Secondary Heads Association and DfES are reported as supporting this principle.

rather than qualification aims, it would have a significant effect on how the gap might be addressed.

The table below indicates the changes and research programmes needed to address the most serious anomalies. The impact of these changes would be to raise the cost of educating 16-18 year-olds in colleges by perhaps 7-9%, or in absolute terms by about £150m. There is some uncertainty about this figure, because we do not know how much is currently spent by local LSCs to fund unplanned expansion by colleges and what the behavioural response would be to the funding of unplanned expansion in colleges.²⁶ There is also uncertainty due to the estimate that half of the 'retention' contribution to the funding gap might be removed pending research into an effective method of treating non-retention common to both schools and colleges.

Immediate action			
	Action recommended	Comment	Impact*
1	Establish a single set of base rates for school sixth forms and FE colleges.	The rates must be the same across sectors after allowing for the secretary of state's 4% guarantee (including any similar future guarantees) which is the main source of the current difference.	2.09%
2	Consolidate the adjustment for pensions increases into the base rates.	The logic of our argument on costs suggests that the precise calculation of the cost of pension contributions is less important than setting an equal quantum/FTE.	2.78%
3	Apply to colleges the schools pupil adjustment system, under which recruitment beyond plan of 16-18 year-olds is funded in full.	The application of this principle under plan-led funding will require careful thought.	<<2.98%
4	Reduce significantly, and indicatively by one-half, the penalties for non-retention suffered by colleges.	The ideal is to have the same system for schools and colleges. The college system is more precise, but seems excessively burdensome in relation to the purposes of penalising non-retention. A more precise system for schools would run counter to the principle of reducing bureaucratic burdens on schools. A reduction in penalties for colleges would be a move towards fairness. without removing the incentive to retain students. A possible method would be reducing funding penalties for students leaving early.	1.80%
5	Undertake research aimed at identifying the same optimal system of penalties for non-retention, applicable to both schools and colleges.	If funding were on the basis of FTEs some of the detail of the FE retention calculation would become redundant.	

²⁶ In areas with both colleges and school sixth forms, it is possible that unanticipated demand from 16-18 year-olds flows to schools rather than colleges, because the former have access to the funding. Offering equal access to the funding may, in those circumstances, not raise the total budget at all.

Immediate action			
	Action recommended	Comment	Impact*
6	Apply the cap and taper system to colleges in the same ways as it is currently applied in schools, ie on average across a cohort, rather than to pupils individually.	If funding moves to an FTE basis the taper and cap become redundant.	0.80%
7	Undertake research aimed at identifying a practicable method, common to schools and colleges, of reflecting the additional costs of delivering learning for disadvantaged students.		
8	Approximate early impact on the FE budget for 16-18 year-olds.	See text for reasons why this total is less than the sum of the individual components.	7-9%
*ie impact on the LSC budget for 16-18 year-olds in colleges			

The research proposed above (items 2, 5 and 7) is likely to yield recommendations that, on the assumption that schools funding should not be adversely affected, will raise FE funding by a further 2-3% or so, or an absolute amount of about £50m, representing the balance of the retention funding gap not covered by recommendation 4, and the move to a uniform system of measuring disadvantage.

In summary, the best estimate that we can make at present is that the funding gap is about 13%, but that complete closure of the gap requires an increase in the FE budget of about 10-11% (£200m), given likely behavioural changes in response to changes in the pupil adjustment system.

In addition to the conclusions above, there is a need for further investigation of the system of support for capital expenditure and of non-formula funding, to assess whether either area adds to the funding gap identified above.

We also feel that there is a need for further research on additional learning support and on the system of non-AWPU deductions by LEAs. Such research would, however, be for purposes other than assessment of the funding gap.

As a more general point, the relationship between funding for and the costs of educating 16-18 year-olds is opaque and merits further investigation.

As a final point, we have encountered evidence during the course of this work that there is another funding gap; not between schools and colleges but between able and well-prepared pupils who are capable of undertaking substantial programmes at Level 3, and those who, for a variety of reasons, are only capable of more modest aspirations. The logic of the current funding formula, based on funding qualifications, not learners, delivers almost twice the level of resources to support a learner who can undertake a programme of five AS Levels with ease, compared with one who struggles to achieve two. There may be a logic in this approach if teaching is based on allocating learners, say, four

hours per subject per week of traditional class-based instruction, irrespective of need. It does not sit well with moves towards the personalisation of learning.

Further evidence for the existence of this other gap comes from an analysis of the individual learning record (ILR) carried out by LSDA, to inform its comments on the Tomlinson interim report. If one examines the median planned guided learning hours (GLH) for learners following programmes at various levels, it is found that the most teaching is given to Level 3 learners and the least to those studying at Level 1. More teaching at each level is given to learners in sixth form colleges than learners in FE and, against all logic, those colleges in areas of the greatest disadvantage offer less teaching at each level than those in the areas of least deprivation. The gap between Level 3 learners in sixth form colleges and Level 1 learners in FE is over 20%. More work needs to be done to understand what is happening here, but initial research suggests that this other gap is equally worthy of investigation.

List of references

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