

Halton Borough Council

**Licensed Deficit Procedure
for
Schools**

March 2017

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Revenue Loans Procedure for Schools

Section 1 – Identification of Schools in Financial Difficulty

What does “financial difficulty” mean?

1. A school is defined as being in “financial difficulty” when either or both the following circumstances occur
 - If the school plans to be in cumulative deficit in the current financial year.
 - If the school forecasts that it will be in cumulative deficit in the current or any subsequent financial year unless remedial action is undertaken.

Why is it important?

2. The Schools Financial Regulations require that Schools maintain a balanced budget¹. However, regulations also recognise that circumstances may mean that this is not always possible, so provision is made for the Authority to agree a “**Licensed Deficit**”² with the school.
3. A Licensed Deficit is an agreement between the school and the Authority. The school specifies the actions it proposes to take to return its budget to balance, and the timetable for their implementation. This is known as the **Recovery Plan**.
4. A deficit means that the school may not have the cash available in its bank account to meet its commitments. Bank overdrafts are a form of borrowing, and since schools are not allowed to borrow money except by written permission of the Secretary of State³, this puts a school in deficit in a difficult position. As its part of the ‘Licensed Deficit’ agreement, the Local Authority may finance the deficit for the duration of the recovery plan by the granting of a **Loan** (known as a **Deficit Financing Agreement**). Such a loan does not need to be approved by the Secretary of State.
5. Loans arranged in support of a Licensed Deficit will not attract any interest.

¹ See Regulation 3.13 in Schools Financial Regulations.

² See Regulations 3.19 and 3.20 in Schools Financial Regulations

³ See Regulations 8.18 and 8.19 in Schools Financial Regulations

The Process of Identification

6. Ideally the process should start by the School formally notifying the Authority that, as a result of internal budget setting or monitoring, it is planning or forecasting a cumulative deficit position. This notification should be addressed to the Strategic Director – People and should acknowledge the situation and seek an early meeting to discuss the formulation of a Recovery Plan.
7. The Authority has its own arrangements to monitor schools budgets based on the reporting requirements in Schools Financial Regulations⁴. On the basis of these arrangements, the Authority may detect that a School is in financial difficulty, and has neither notified the Authority, nor has an existing Licensed Deficit in place. In this case, the Authority will write to the school .
8. The key to successfully ‘Recovering Your Balance’ is early identification of potential financial difficulties, followed promptly by consideration of what the school needs to do to return its budget to long-term financial balance.

Section 2 – Working with schools in financial difficulty

9. **The ultimate responsibility for formulating a recovery plan proposal lies with the Headteacher and the Governing Body of the school.** Each school has its own arrangement for financial support. When formulating a recovery plan, it is vital that the school engages with its financial support at an early stage in the process.
10. It is also recommended that the school consider involvement from other contacts in the formulation of the recovery plan, their Link Officer for example, so that educational standards are not compromised. Also, if employment issues are involved, advice must be taken from the appropriate HR advisor.
11. Every school will have its own unique circumstances and problems, but in working through the process of formulating a recovery plan, the school and its advisers should cover the range of issues listed below. It is worth noting that the list below broadly corresponds to the issues to be included in the ultimate application to the Authority for a Licensed Deficit and Deficit Financing Agreement, and the criteria the Authority will use to consider the application.

⁴ See Regulations 4.8 to 4.14 in Schools Financial Regulations

- 11.1. A clear understanding of why the budget problem has arisen.
- 11.2. Are the forecasts of income and expenditure underlying the identified deficit robust?
- 11.3. Does the school's expenditure pattern differ significantly from others of similar size and profile? This may inform the areas where cost savings may be sought. This should include an analysis of use of staffing and consideration of alternative ways of organising the school. Does the school maximise income from lettings and other local sources?
- 11.4. Has the school identified a series of proposed actions that will return the budget to balance? Are these specific, measureable, realistic, achievable and time bound?
- 11.5. Has the school robustly projected income and expenditure, incorporating the proposed actions, for each year until the budget returns to balance? In particular are any pupil number forecasts robust?
- 11.6. Will the value of the Loan, taken together with the projected annual cash flows (including repayment of the Loan), prevent the school from overdrawing their bank account?
- 11.7. Has the school identified the risks inherent in their proposed actions, and what steps have been put into place to minimise the impact of these risks?
- 11.8. Have all issues been considered e.g.:
 - Use of devolved capital to fund certain one-off items of expenditure where so allowable
 - Use of staff to support statemented pupils and dates these pupils are leaving school
- 11.9. What specific monitoring arrangements have been put into place so that the Governing Body can monitor the successful fulfilment of the recovery plan?
12. The Governing Body should formally consider and endorse the recovery plan prior to submission to the Authority.
13. The over-riding consideration is to formulate a plan that:
 - Returns the school to a sustainable position of cumulative surplus as soon as possible

- Does not compromise educational standards
 - Generates sufficient cash to repay any loan advanced by the Authority to finance the deficit
14. Guidance on how to process transactions related to loans is attached as Appendix 6.

Section 3 – Applying for a Licensed Deficit

15. To apply for a Licensed Deficit, a school must write formally to the Strategic Director - People. The letter must include an attachment detailing the following information:
- 15.1. A full description of the circumstances leading to the forecast or planned cumulative deficit.
 - 15.2. A description of the steps the school intends to take to reduce expenditure and / or increase income so as to return their budget to balance. This should include costings and other relevant calculations. Also, the planned timing of implementation should be made explicit.
 - 15.3. An assessment of the risks associated with these planned actions, and the steps taken by the school to mitigate these risks.
 - 15.4. The amount of cash required to finance the recovery plan, the repayment schedule (i.e. the number of years over which the cash loan will be repaid, and the start date for repayments)
 - 15.5. The standard repayment schedule is:
 - Repayments commence on the first of April in the financial year following the date of the loan.
 - Repayments are made in equal instalments every month over the number of financial years specified in the recovery plan.

For example:

A loan of £180,000 was agreed and paid in August 2015, supporting a recovery plan over 3 financial years.

Thus the first repayment of £5,000 (i.e. $£180,000 \div 3 \div 12$) would be due on April 1st 2016, and the last on 1st March 2019.

15.6. If appropriate, a non-standard repayment profile tailored to the specific circumstances may be agreed with the school. Such a profile may vary:

- The start date of repayments – and/or
- The amount payable in any year of the recovery plan

15.7. A financial schedule will be provided by Finance which will show, in full CFR format, the forecast income, expenditure and cash flow for

- a) The previous financial year actual
- b) The current financial year
- c) Future financial years up to the end of the loan repayment period.

Thus, if the loan cash advance is sought in 2016/17, and repayments commence in April 2017 and continue until March 2020, then figures are required up to that date. These forecasts should clearly reflect the savings arising from the proposed actions referred to in paragraph 15.2.

15.8. Details of any existing loan agreement in force between the school and the Authority.

15.9. A statement confirming that the Governing Body has considered and approved the recovery plan.

15.10. Details of how the Governing Body intends to monitor the progress of the recovery plan

Section 4 – Processing the application for a Licensed Deficit

16. The Authority has implemented procedures to manage the processing of each Application for a Licensed Deficit. These procedures have been designed to ensure that:

- Applications are reviewed, and amendments agreed with schools, to ensure that only robust achievable recovery plans are approved.
- The decision to approve an application is taken without undue delay.
- The process is managed and transparent.

17. Following the submission of a 'Governor Approved Budget Plan' and recovery plan a number of validation checks will be completed by the Local Authority to ensure that the plans are reasonable. This will be done by: -
- Comparing the current year's income and expenditure budgets with previous years' trends to identify any significant differences.
 - Checking that the correct balances have been brought forward into the current year and all funding delegated by the LA have Been taken in to account.
 - Actions included in the recovery plan are realistic and that by implementing them the required level of savings can be achieved.
 - Any areas that are unclear or simply not achievable will be queried with the school and clarification sought.
18. The review process will usually involve a visit to the school by a member of the Local Authority Finance Team.
19. The next step in the process is that the school will receive a Deficit Financing Agreement form from the Authority. An example is attached as Appendix 1. The Agreement Form will be signed on behalf of the Operational Director Finance. The Deficit License will only be activated (and any loan cash advanced) when the Headteacher and the Chair of Governors sign the form on behalf of the School; and then return the original agreement form and a completed bank mandate to the Authority. A standing order mandate form will also need to be completed.
20. When the Authority receives the final signed agreement and the standing order mandate, it will promptly transfer the loan cash to the school's bank account. Repayments will commence on the agreed date and at the agreed amount.
21. It is possible that a School is in deficit yet does not require cash due to payment timelags. This means that the authority may merely license a deficit within the need for repayments or interest. In all other aspects the procedure is the same as that of deficits arranged with a cash advance.

Section 5 - Monitoring and Reviewing Recovery Plans

22. Schools are expected to honour any commitments regarding internal monitoring procedures given in their application for a Licensed Deficit.
23. In addition to this, the Authority will monitor the progress of all live recovery plans.
24. Depending on the perceived level of risk inherent in the recovery plan, and any special reporting conditions imposed when the deficit was licensed, the school will supply the Authority with monitoring information, on a monthly basis, to allow them to assess how closely current year forecasts and / or actual outturns compare with the predictions for the corresponding year in the approved recovery plan.
25. If this monitoring suggests that a significant deviation is becoming apparent between the recovery plan and what is actually happening, then the Head of Schools Finance and the School will review the plan and:
 - 25.1. Where the school is ahead of its plan, determine whether the repayment schedule could be accelerated to so that the license may be declared expired sooner than originally planned.
 - 25.2. Where the school is drifting behind its plan, determine agreed action to get the plan back onto track, within the scope of the existing loan agreement.
 - 25.3. Where it is apparent that the original plan cannot now be achieved, reach an agreement to expire the existing License, and construct a new recovery plan appropriate to the circumstances. In this case, any existing outstanding loan balance will be carried forward to the new Agreement.
26. If this routine monitoring suggests that the recovery plan has achieved its objective, that is, the school is in sustainable cumulative surplus, and the loan has been repaid, then the License will be formally declared expired, and the Authority will notify the school accordingly in writing.
27. Monitoring will continue throughout the life of a Licensed Deficit, until it can be declared to have expired.

GENERAL

Section 6 – Making Payments

Deficit Financing Agreements

28. The standard repayment profile normally commences at the beginning of the Financial Year following the year in which the loan was advanced, unless an alternative arrangement is agreed between the Authority and the school.
29. Repayments (by standing order) will be taken from the school's bank account on the first of each month throughout the agreed repayment period
30. Monthly repayments will normally be equal throughout the repayment period, unless an alternative arrangement is agreed between the Authority and the school.
31. The agreed repayments will continue until the loan is re-paid in full. The agreed re-payments will continue notwithstanding any changes to the School management structure or governing body after the commencement of the loan agreement.

Halton Borough Council

Deficit Financing Agreement Form

Reference Number	
School Name	
Date of Application	
Amount of loan requested	£
Period of loan repayment	
First Repayment instalment due	
Last Repayment instalment due	
Instalment amount	£
Non-standard Repayment Profile requested? <i>(if yes, attach details)</i>	Yes / No
Existing Loan ? <i>(if yes, quote reference number)</i>	Yes / No

The following terms and conditions apply to this Financing Agreement

Standard Conditions

- The School will not vary the terms of the Standing Order mandate supporting the repayment plan without prior agreement with the Authority.
- The School will implement the actions detailed in the recovery plan supplied with the Application for a Licensed Deficit.
- The School will monitor the progress of the recovery plan in accordance with the arrangements detailed in its Application for a Licensed Deficit.
- The School will conform to the routine monitoring and reporting requirements set down in Schools Financial Regulations.
- The School will notify the Local Authority of any material error within their Application for a Licensed Deficit, including all related documentation, as soon as they become apparent
- The School will participate in regular reviews of the progress of the recovery plan as required by the Authority.
- Should the School transfer to academy status, the loan balance will be transferred to the Academy.

Special Conditions (at the discretion of the Authority)

- (to be added as required)

Review by the Head of Schools Finance

Comments:

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Signature: _____ Date: _____

Agreement approved on behalf of the Operational Director Finance:

Name:	
Position:	
Signature:	
Date:	

Comments:

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Acceptance of this Agreement (including all terms and conditions) by the School

Headteacher's signature	
Date:	

Chair of Governor's signature	
Date:	

Please return the completed School Loan Agreement to:-

Operational Director – Finance
Municipal Building
Kingsway
Widnes
WA8 7QF

