



Education & Skills  
Funding Agency

# **College financial planning handbook 2017**

**Financial planning requirements for  
sixth-form and further education colleges**

**June 2017**

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## Introduction

1. The college financial planning handbook sets out the Education and Skills Funding Agency's (ESFA) financial planning requirements for sixth-form and further education colleges.
2. ESFA publishes the handbook on behalf of the Secretary of State for Education in their role as principal regulator, given colleges' status as [exempt charities](#).
3. This version applies to financial plans due by 31 July 2017.
4. This handbook is primarily for use by:
  - college principals, chief executives and finance directors
  - chairs of college governing bodies, finance and audit committees

## What has changed in this edition?

5. Changes in this version include:
  - addition of special arrangements for colleges planning to merge or to become an academy
  - addition of moderation criteria for colleges incurring significant costs ahead of plans to merge or to become an academy
  - revision to the implications of receiving an 'inadequate' financial health grade
  - additions to the financial planning checklist to improve the quality of the supporting commentary
  - addition of an explicit statement that the accounting officer has prepared the supporting commentary with due regard to the financial planning checklist
  - clarity on how we assess underlying financial health

## Specialist designated institutions

6. We use the term 'corporation' to refer to further education and sixth-form college corporations established under the Further and Higher Education Act 1992, where members of the corporation form the college's governing body.
7. For the avoidance of doubt, the requirements herein apply equally to institutions designated under s28 of the Further and Higher Education Act 1992, known as specialist designated institutions or Institutes for Adult Learning, which are independently constituted charities, to the extent permitted by their trust deeds and underlying legislation.

## Part 1: Submission requirements

8. Colleges must submit the following documents to ESFA by 31 July 2017:
  - 3-year financial plan (Excel version), including:
    - **estimated outturn** for the year ending 31 July 2017
    - **approved budget** for the year ending 31 July 2018
    - **forecast** for the year ending 31 July 2019
  - supporting commentary (Word version)
  - cover sheet signed by the accounting officer (scanned copy)
9. ESFA will confirm the submission route closer to the deadline. Colleges do not need to submit hard copies of documents.

## Special arrangements

### Transactions Unit's CFADS model

10. Where a college is completing the Transactions Unit's CFADS model in respect of a restructuring facility application, ESFA will issue further submission guidance in due course.

### Plans to merge or become an academy

11. ESFA has agreed [special arrangements for colleges](#) planning to merge with another college or to become an academy.
12. For such changes scheduled **between July and November 2017**:
  - dissolving corporations should submit a 1-year plan with estimated outturn for the current year
  - new corporations should submit a 2-year plan with budget and forecast only
  - merged corporations should submit a 3-year plan with estimated outturn of the continuing corporation and budget and forecast of the merged corporation
13. For such changes scheduled **between December 2017 and June 2018**, all corporations should submit a 2-year plan with estimated outturn for the current year and budget for the forthcoming year.

### Strategic recovery plan

14. Where a college is developing a strategic recovery plan and cannot provide a reliable 3-year plan, ESFA may give approval for the college to provide a 2-year plan with estimated outturn for the current year and budget for the forthcoming year.

## Part 2: Financial plan and supporting commentary

### Financial plan

15. The financial plan must give a **realistic** view of the college's financial performance and reflect the cost of implementing the college's strategy including income, expenditure and cash flows associated with projected levels of activity.

16. Colleges must:

- use the template published alongside this handbook
- complete all un-shaded fields in the template, entering a nil value where applicable
- enter balances in £'000s unless otherwise stated, for example £1,533,974.21 must be entered as 1,534
- enter the consolidated results for the college and any subsidiaries
- clear any error messages given, once all schedules are complete

17. Colleges may:

- 'unhide' columns to add data for subsequent years
- add comments to the narrative boxes on each schedule to detail significant variances, assumptions and/or risks

### Supporting commentary

18. Colleges must submit a supporting commentary with the financial plan, to include:

- summary of the college's strategic objectives
- description of how the plan is consistent with the college's strategic objectives
- explanations for significant year-on-year movements in the statement of comprehensive income and balance sheet
- explanations for significant variances between the estimated outturn for the current year and the original budget
- the contribution made by different areas of activity
- the college's self-assessment of its financial health and explanation for any change from the autograde

### Assumptions

19. The supporting commentary must include detailed assumptions underlying the financial plan and explanation for why the college has adopted these assumptions. The financial planning checklist (see **Annex A**) gives prompts as to the assumptions to be covered.

20. ESFA does not provide guidance on which assumptions to use, however colleges may find the published [financial benchmarking tool](#) useful to inform their decisions.

## Sensitivity analysis

21. As part of their risk management process, colleges should assess their resilience to adverse events that pose a risk to successful delivery of strategic objectives.

22. Colleges can use the sensitivity analysis schedule to model various scenarios, flexing a small number of assumptions underlying the financial plan. Colleges should use their own judgement to consider what level of flex is appropriate.

23. Colleges may undertake further sensitivity analysis, to consider the impact of specific adverse events. This may include preparing alternative versions of the financial plan based on revised assumptions. Where a college identifies a material risk to financial viability and solvency, they must share these alternative plans with ESFA.

24. The supporting commentary must include detail of:

- sensitivity analysis undertaken
- level of flex applied and/or specific revisions to assumptions
- college's assessment of the risk to financial viability and solvency
- plans to mitigate risks should they arise

25. Mitigating actions may include:

- additional in-year financial monitoring, with a clear process of escalating concerns
- ensuring a flexible cost base
- negotiating further cost savings
- ceasing any loss-making activities
- making better use of assets to generate income and/or savings

26. Colleges should discuss with ESFA where these actions include a rationalisation of provision in any programme area or locality.

## Approval of documents

27. The governing body is responsible for ensuring the financial viability of the college. They should regularly assess financial health, considering all relevant information.

28. In signing the cover sheet, the Principal confirms that the governing body has approved the financial plan and that it supports the college's strategic objectives. The Principal also confirms that the supporting commentary has been prepared with due regard to the financial planning checklist (see **Annex A**).

## Part 3: Assessing financial health

### Financial indicators

29. ESFA assesses the financial health of colleges at two main points in the year – on receipt of the financial plan (due 31 July) and finance record (due 31 December) – based on 3 financial indicators:

### Solvency

30. ESFA assesses solvency using an **adjusted current ratio**, being the ratio between current assets and current liabilities. The ratio excludes:

- proceeds from the sale of fixed assets held for reinvestment
- fixed assets held for sale
- deferred capital grants held as liabilities
- holiday pay accrual

### Performance

31. ESFA assesses performance using **sector-specific earnings before interest, tax, depreciation and amortisation (EBITDA)** as a percentage of adjusted income.

32. Sector-specific EBITDA excludes:

- exceptional financial support/restructuring facility transition support grants
- income from the release of deferred capital grants
- net return on LGPS pension scheme
- LGPS service costs, curtailments and settlements, which are replaced by employer contributions
- other comprehensive income not included in surplus/deficit for the year

33. Adjusted income excludes:

- income from the release of deferred capital grants
- net return on LGPS pension scheme

### Borrowing

34. ESFA assesses borrowing as a percentage of adjusted income. Borrowing includes:

- repayable exceptional financial support / restructuring facility transition support
- bank and other commercial loans
- finance lease obligations
- overdraft liability

## Scoring and grading

35. Each indicator is given a score out of 100:

Score	Solvency	Performance	Borrowing
100	$\geq 2.0$	$\geq 10\%$	$= 0$
90	$\geq 1.8$	$\geq 9\%$	$< 10\%$
80	$\geq 1.6$	$\geq 8\%$	$< 20\%$
70	$\geq 1.4$	$\geq 7\%$	$< 30\%$
60	$\geq 1.2$	$\geq 6\%$	$< 35\%$
50	$\geq 1.0$	$\geq 5\%$	$< 40\%$
40	$\geq 0.8$	$\geq 4\%$	$< 45\%$
30	$\geq 0.7$	$\geq 3\%$	$< 50\%$
20	$\geq 0.6$	$\geq 2\%$	$< 55\%$
10	$\geq 0.5$	$\geq 1\%$	$< 60\%$
0	$< 0.5$	$< 1\%$	$\geq 60\%$

36. The total score is translated to a financial health grade:

Score	Grade	Definition	Indicators
240 – 300	Outstanding	Very robust finances to meet obligations and respond successfully to opportunities or adverse circumstances	Outstanding/ good for all indicators
180 – 230	Good	Sufficiently robust finances to meet obligations and respond successfully to most opportunities or adverse circumstances	At least 2 good indicators
120 – 170	Satisfactory	Sufficient resources to meet obligations but limited capacity to respond successfully to opportunities or adverse circumstances	At least 2 satisfactory indicators
$\leq 110$	Inadequate	Financial difficulty and likely to be dependent on the goodwill of others, with a significant risk of not being able to meet obligations	At least 2 inadequate indicators



37. Where a college's financial health is assessed as 'inadequate' in any year, ESFA will look to intervene in line with the published approach and may issue a Financial Notice if considered appropriate.

## Moderation criteria

38. Where a college scores zero points for one of the three ratios, its financial health can be graded no better than 'satisfactory'. The financial plan automatically applies this moderation.

39. The autograde can only be moderated in accordance with the criteria below.

## Capital projects

40. The financial health grade may be uplifted to 'satisfactory' where a college is undertaking a significant capital project (defined as more than the lower of £5 million or 25% of total income) provided that:

- the project has started its capital life cycle (being the date approved by the governing body)
- the college's financial health is graded 'outstanding', 'good', or 'satisfactory' at the time of the detailed project approval
- the college will return to a financial health grade of at least 'satisfactory' by the year following project completion
- the college performs at least as well (in the opinion of ESFA) as forecast during the intervening years; if a college performs less well than it forecast at the start of the year then ESFA will reflect this in its assessment

## Professional fees associated with capital projects

41. Where a college incurs significant professional fees (defined as more than £250,000) in relation to a capital project that cannot be capitalised, it may make a case for moderation to one grade higher.

## Restructuring costs

42. Where a college incurs significant restructuring costs (defined as more than 5% of staff costs) in a single year, the financial health grade may be uplifted to 'satisfactory'.

43. This may include restructuring funded from the government's restructuring facility following the area review process.

## Exceptional financial support

44. ESFA may provide [exceptional financial support](#) to further education colleges to protect the continuity of provision for learners in cases of college financial distress. Where support is given, financial health may be moderated to 'inadequate' and may trigger a referral to the FE Commissioner in line with the published policy.
45. Where a college is in receipt of long-term exceptional financial support and is on track with its repayment schedule, the financial health grade will not be automatically moderated to 'inadequate' if the autograde is 'satisfactory' or above.
46. However, if a college fails to meet its repayment obligations or performs less well (in the opinion of ESFA) than forecast at the time the exceptional financial support was agreed then ESFA will reflect this in its assessment. This could result in the financial health grade being moderated to 'inadequate'.

## Cash generation

47. Where the cash being generated year-on-year is more than sufficient to enable a college to meet net current liabilities, the financial health grade may be uplifted to 'satisfactory'.
48. Where the cash generated year-on-year is insufficient to meet debt service obligations (repayment of capital plus interest and similar charges), this may lead to a financial health grade of 'inadequate'.

## Other

49. Other information may be available and evidenced that indicates financial health is significantly different from the autoscore. Examples include:
- a court ruling which has financial consequences
  - the loss or significant reduction of a material contract or area of provision
  - a significant recovery of funds following a funding audit or investigation
  - a contingent liability crystallising
  - one or more bank loan covenants being breached for the year with long-term loan obligations reclassified to current liabilities
  - a delay in the sale of fixed assets and/or receipt of proceeds
  - evidence that the assumptions adopted are unrealistic

## Self-assessment

50. Colleges must self-assess their financial health for each year of the plan with reference to the moderation criteria above. The governing body must approve this self-assessment.

51. Where the self-assessed financial health grade differs from the autograde in any year, the college must explain why and which moderation criteria they consider applicable.

## **Significant deteriorations**

52. Colleges must notify ESFA if, at any time, they become aware of a significant deterioration in their current or forecast financial health.

## **Underlying financial health**

53. ESFA also assesses the underlying financial health for each college, taking into account both the estimated outturn for the current year and budget for the subsequent year, along with other relevant information. This assessment accommodates any significant year-on-year swing in financial health.

## Annex A: Financial planning checklist

Colleges should share the completed checklist with their governing body to provide assurance that they have considered relevant matters. It does not need to be submitted to ESFA, however Principals are asked to confirm that the supporting commentary has been prepared with due regard to the checklist.

Does the supporting commentary include:		Yes / No / N/A
<b>1. Strategic and financial objectives</b>		
	Detailed financial objectives (see <b>Annex B</b> )	
	College's assessment of performance against financial objectives, and any actions taken and/or planned	
	Strengths and weaknesses of the college's financial position and the extent to which the college may be vulnerable to adverse variances	
	Risks arising from overseas ventures	
<b>2. Detailed assumptions</b>		
	Movements in funding, including student numbers and funding per student	
	Apprenticeship forecasts	
	Adult Education Budget performance and recovery	
	16 to 19 growth	
	Income from ESFA other than the main funding streams, including formula protection funding and high needs funding	
	Income from other sources, including education contracts, tuition fees, European funds and commercial activities	
	Impact of estates strategy, including capital investment, sale of assets, long-term maintenance and routine maintenance costs	
	The level of pay awards and the impact on staffing costs	
	Future staffing plans and the impact on staffing costs	
	National insurance contributions	
	Pension fund contributions, including LGPS and TPS	
	Incremental drift, including any gain resulting from staff losses at the high end of the scale being replaced by staff at the lower end	

<b>Does the supporting commentary include:</b>		<b>Yes / No / N/A</b>
	General inflation rate, plus any variation from the general inflation rate for specific items of income or expenditure	
	Interest rates	
	Sub-contractor costs and/or any franchising arrangements	
	Transfers to and from restricted reserves	
<b>3. Financial health self-assessment</b>		
	Rationale behind the self-assessment of financial health, with reasons for any moderation from the autograde with reference to the moderation criteria	
<b>4. Primary financial statements</b>		
	Explanation for significant year-on-year movements	
	Explanation for significant variances between the estimated outturn for the current year and the original budget	
<b>5. Income, expenditure, assets and liabilities</b>		
	Detail on the sources of grant income and the underlying assumptions of learner numbers, including any forecast growth	
	The nature of any repayment of European Social Funding	
	Sources of income from franchising provision	
	Detail of all income-generating activities and the contribution made net of expenditure	
	Provisions included in expenditure	
	Detail of significant asset purchases and disposals	
	Details of loans, including consents and background	
	Assessment of ability to repay borrowings as they fall due	
<b>6. Sensitivity analysis</b>		
	Detail of the sensitivity analysis undertaken and outcomes	
	Detail of plans to mitigate risks should they arise	

## Annex B: Example financial objectives

- Maintain a sound financial base (solvency and liquidity) as measured by:
  - a) general reserve of XX% of income by 31 July 20XX and YY% by 31 July 20XX
  - b) cash days of XX or more at all times
  - c) break-even position by 31 July 20XX and operating surplus by 31 July 20XX
  - d) cash inflow from operating activities by 31 July 20XX
  - e) borrowing reduced to XX% of general reserves by 31 July 20XX and YY% by 31 July 20XX
  - f) current ratio of more than XX by 31 July 20XX
  
- Improve financial management by producing management accounts each month, incorporating an income and expenditure account, balance sheet, 12-month rolling cash-flow forecast, capital expenditure, financial performance indicators, staffing information and funding information (including plans)
  
- Strengthen procedures for testing the desirability and affordability of proposals which have a financial implication by 31 July 20XX
  
- Introduce post-implementation review to assess the success or otherwise of major investments (building, IT, staffing, marketing etc.) exceeding £XX by 31 July 20XX
  
- Maintain the confidence of ESFA, suppliers and professional advisers by:
  - a) providing financial and non-financial returns on time and in the agreed format
  - b) ensuring all returns requiring certification are unqualified and submitted on time
  - c) adhering to the college policy to pay suppliers within XX days of receipt of invoice
  
- Raise awareness of financial issues by:
  - a) providing advice, guidance and training to staff, management and governors on funding, funding methodologies, budgeting and the college's financial procedures
  - b) providing adequate information to ensure that staff, management and governors are kept up-to-date with the financial position of the college
  
- Improve the college estate and equipment by:
  - a) generating sufficient funds to ensure that the college can undertake its specified programme of planned maintenance
  - b) generating sufficient funds to ensure that the college can invest in the new technology and equipment required to support learning and college administration
  - c) ensuring adequate procedures are in place to protect assets from loss, theft and neglect



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