

# DECISION PAPER

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**SUBJECT:** Proposals for Changes in Surplus & Deficit Policies in SCC Scheme for Financing Schools

**DATE:** 14<sup>th</sup> September 2016

**RECIPIENT:** Schools Forum

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## **SUMMARY:**

This paper seeks the agreement of members of the Forum on proposed changes to the Scheme for Financing schools from October 2016.

## **RECOMMENDATION:**

It is recommended that the Schools Forum agrees to changes proposed in this paper.

## **BACKGROUND**

1. There are a number of factors that will be affecting schools funding for example proposed changes to the schools' funding formula and the academisation agenda. This will change the role local authorities currently play in allocation of funds to schools and their ability to balance schools' accounts will be very limited, if not completely removed, going forward.
2. The School Forum agreed at the meeting in June that the procedures for the management of deficit and surplus budgets, as contained within the School Scheme of Financing, should be reviewed and a paper on proposed changes in future policies, be brought back to September meeting for further consideration and approval.

## **BRIEFING DETAILS:**

3. The Scheme for Financing Schools sets out the powers and responsibilities of governors and the local authority under delegated management and the financial controls within which a delegated budget can be operated.

The key changes are:

- Treatment of Surpluses and Deficits
- Loans from School Balances.

## Surplus Balance Policy

### New proposals for schools to carry forward balances above the permitted levels - The Balance Control Mechanism

4. As per SCC current Scheme for Financing Schools, Primary and Special Schools can carry forward up to 8% of the current years School Budget Share as general balances and Secondary Schools can carry forward up to 5%; anything above this is a surplus balance and the City Council has the authority to remove that excess from the school balance.
5. The City Council has not exercised this in practice to date. However, due to funding constraints school funding is subject to tighter scrutiny.
6. The new scheme has been designed to be:
  - forward looking
  - more specific with carry forwards only being allowed in limited circumstances
  - more accountable with the real likelihood of monies being removed from schools, who do not use them.
7. The revised principles of the scheme are as follows:
  - Primary and Special Schools can carry forward up to 8% of the current years School Budget Share as general balances. Secondary schools can carry forward up to 5%. Anything above this is a **surplus** balance
  - There are three allowable purposes for which excess surplus balances can be used:
    - as a revenue contribution to capital projects within a time limited maximum two year period
    - to maintain a reserve to fund staffing levels in the short / medium term due to a verified dip in pupil numbers
    - to provide reasonable and proportionate resources to fund the impact of major changes in Government policy on the curriculum for multiple subject areas. Any decisions to retain surplus balances for this reason will be subject to review by the Local Authority.
  - Schools will lose their surplus balances if:
    - they do not inform the LA of the governing body decision before 31 May that there are proposals to use any surplus balances and that those proposals have been approved and minuted by the appropriate Governing Body or Sub-Committee before 31 May
    - the proposals do not relate to one of the allowable purposes for the use of surplus balances
    - the Utilisation of Balances Pro-forma is incomplete
    - the intended use of the balance was on a capital project, which has not materialised at the end of the time limited two year period and detailed on the completed form
  - there will be no exceptions to the deadline date of 31 May so Governing Body meetings will need to be scheduled before the deadline to ensure the appropriate approvals are in place
  - surplus balances removed from schools will be added to the Schools in Financial Difficulty Fund for redistribution as per the criteria set for the fund.

## **Revised Procedure**

8. The revised procedure to obtain approval to carry forward surplus balances is as follows:
  - schools will complete a Balance Control Mechanism form known as the Utilisation of Balances form and return to the schools finance team by the 31 May. This form must be completed fully and the relevant minutes at the governing body or sub-committee meeting must be attached detailing the decisions agreeing to spend the surplus balances, or retain them for a period of two years. An example of the form is attached at Appendix 1.
  - the Schools Finance Team will monitor the balances and remove surplus balances as detailed above if the Utilisation of Balances form does not comply with the revised principles of the scheme. The Schools Finance Team will also ask for a breakdown and evidence of expenditure plans
  - it is the intention that surplus balances will be removed in the summer term of the following financial year if the spend does not materialise within the timescale detailed.
9. Any surplus balances removed from schools as above will be added to the School in Financial Difficulties Fund and will be available to all maintained schools as per the set criteria for the fund.

**The process is summarised in a flow chart format at Appendix 2.**

## **Deficit Budget Policy**

### **10. Planning for deficit budgets**

Schools cannot plan for a year end deficit budget when submitting budget plans at the start of the year i.e. expenditure exceeding funding and income for the year plus the accumulated surplus brought forward. Schools that submit deficit plans will be required to resubmit their budget with plans to bring the budget back into balance. The authority will intervene if a school refuses to set a balanced budget by identifying the action a school could take and ultimately by suspending delegation.

11. Any unplanned deficit incurred during the year would be a first call on the following year's budget; the school would need to include the deficit in its balanced budget plan for the following year. Schools that incur unplanned deficits in successive years would be treated the same as schools submitting deficit plans and the authority would need to intervene.
12. School bank accounts are not permitted to go overdrawn. If a school gets into financial difficulty and is facing a potential unplanned deficit they will need to apply to the local authority for a revenue budget deficit loan in order to be able to continue meeting their liabilities.

## **Proposal for Changes in Policy & Procedure**

13. If a school submits a Three Year Plan to the LA that contains a deficit in the second or third year of the plan, then it will be returned. The school will be required to undertake Step 1; Preparation prior to Notification as detailed below. It will be necessary to identify management action and resubmit a plan which does not show a deficit in any of the three years. If this is not possible or the plan shows a deficit in the first year then the school should proceed to Step 2 – Step 6. The assigned School Improvement Officer will inform the school if a resolution can be achieved before there is a need for a Deficit Recovery Plan.
  
14. **Steps in the process**
  1. Preparation prior to Notification of Financial Difficulty
  2. Notification and Supporting Documentation
  3. Initial Meeting
  4. Submitting a Deficit Recovery Plan
  5. LA Approval
  6. Monitoring a Deficit Budget
  
15. **Step 1 – Preparation prior to Notification of Financial Difficulty**

When first aware of a potential deficit the school should:

  - check all the figures and the assumptions that have been made
  - identify the cause of the forecasted deficit, for example, a falling roll
  - undertake a benchmarking exercise
  - discuss and draw up a range of Management Actions.

This action should be incorporated with a view to being able to amend the figures so that the Three Year Plan does not result in a deficit in any of the three years.
  
16. Only after undertaking this work, which must be documented within the Governor minutes, is it acceptable to approach the LA to discuss the possibility of having a Deficit Recovery Plan approved. The School Improvement Officer will expect sound arguments to be offered as to why early remedial action cannot be taken or why it was not taken in the past. Without SCC's approval to a planned deficit, the school would be acting illegally in setting a deficit budget.
  
17. Following this course of action represents sound financial management practice and schools that contact the LA having completed the preparatory work will be viewed as following the correct procedures; schools that fail to follow these steps and go into deficit or produce a deficit budget without this analysis could result in further action being taken by the LA.

18. **Step 2 – Notification and Supporting Documentation**

Once the preparatory work has been completed and the Governing Body is satisfied that a potential deficit is unavoidable without a significant impact on the provision of education, then Schools Improvement should be contacted. This must be done immediately, by e-mail, outlining the deficit position. The Chair of Governors must be made aware that the LA has been contacted regarding the budget situation.

19. On receipt of the notification the school will be asked to submit supporting documentation for analysis. This will include details of the actions that would be required to avoid a deficit and why those actions are not possible or acceptable. In the extreme case of a current year deficit that was not previously anticipated, a full explanation will be required as to how this has arisen, together with evidence of internal monitoring and reports to Governors.

20. **Step 3 – Initial Meeting**

Schools Improvement Team will contact the school to arrange a meeting with the Head teacher and School Finance Team to go through the process and to discuss the documentation previously provided by the school. Any observations that Schools Finance have made relating to the data will be reviewed and potential savings will be discussed with the school.

21. The school may wish to have the Chair of Governors or the Governor responsible for finance present at the meeting. In certain circumstances the LA may require attendance of the Chair of Governors/Finance. Notes of the meeting will be circulated to the Head teacher, Chair of Governors and the School Finance Team.

22. The school will then be required to make any agreed adjustment to the Three Year Plan and/or salary calculations and resubmitted to Schools Finance within five working days of the initial meeting.

23. School Finance will undertake further checks in order to reach a decision on whether a Deficit Recovery Plan is appropriate. The school will be notified by email recording any decisions made at the meeting and confirming if an approved deficit should be sought.

24. **Step 4 – Submitting a Deficit Recovery Plan**

The school will need to work with SCC's School Finance Team (if they have purchased SCC Finance Services via an SLA) or their own finance support (if they have not bought back SCC Finance Services), together with SCC School Improvement Teams to produce a robust Deficit Recovery Plan (DRP), ensuring the spend is brought back in line with their allocated funds.

25. The purpose of a Deficit Recovery Plan is to identify the actions that can be taken to bring the school budget back to a balanced position within an agreed period of time (maximum of 3 years). The recovery plan can be a simple statement showing:
- what actions will be taken and who will be responsible
  - when these actions will happen
  - how much will be saved by taking the action i.e. part year / full year financial impact of proposed savings.
26. The Deficit Recovery Plan must be approved by the Governing Body and signed by the Chair of Governors prior to the final submission. This may require the school to call an extraordinary meeting of the Governing Body.
27. The signed Deficit Recovery Plan must be submitted to the Schools Improvement and Finance in line with the date stated in the written confirmation. The Deficit Recovery Plan will become the formal application for an approved deficit and must show that the school will return to a surplus position within a maximum of three years.

If the Deficit Recovery Plan does not meet the requirements of the LA and the DfE it will be rejected providing reasons as to why and the school will be required to resubmit.

## 28. **Step 5 – Local Authority Approval**

The Deficit Recovery Plan requires formal approval by Service Lead for Education and Early Help before a loan can be agreed. After the plan has been approved a confirmation letter will be sent to the school.

## **Loan Scheme**

29. Southampton City Council currently operates a loan scheme that allows schools to borrow amounts of up to £200,000 from the pool of school balances to fund certain types of project. Projects to be supported may include:
- major maintenance or improvements to school properties (deemed as necessary by Capital Assets)
  - investment projects which will produce a future revenue saving e.g. schemes to improve energy efficiency
  - projects to improve school security (deemed as necessary by Health & Safety)
  - major purchases of equipment (e.g. IT).
30. Due to the financial challenges that some schools are facing, it is important that the schools are supported with cash flow issues for schools in deficit; whilst at the same time seeking to protect the Schools Budget and LA from risk of the cost of deficits arising from schools in deficit converting to academy.

31. It is proposed to revise the current loan scheme available for above projects and introduce the revised loan scheme to formalise such support setting out clear agreements for repayment schedules. If it becomes clear that a school is to be closed or merged, the remaining balance of the loan would become payable immediately. Schools closing to become academy will have the loan transferred as part of their Commercial Transfer Agreement.

32. It is therefore proposed to add the following section to the Scheme.

#### **Proposed Changes to Loan Scheme**

- the Authority operates a loan scheme for schools that may require a revenue loan during a period of financial difficulty
- the length of the loan will not normally exceed 3 years. There is no minimum period. Approval will be given by the Service Lead for Education and Early Help and the Service Director Finance & Commercialisation, following a review of an application for financial support
- a loan will be the last resort after taking all necessary steps e.g. production of a robust Deficit Recovery Plan, exploring any available funding such as School in Financial Difficulties Fund
- each decision to grant a revenue loan will be based on the circumstances of the school and the financial ability of the school to repay. A viable repayment plan must accompany the Loan request
- the Governing Body will have to vote to enter into a loan and the GB will be required to sign a legally binding loan agreement signed by the Governors in accordance with their Constitution
- if a school refuses to repay the loan, the Authority reserves the right to charge the School Budget Share
- any default on a loan by the academy will be raised with the funding agency in the first instance, who may be required to sign as guarantor as part of the CTA, but if informal resolution cannot be agreed will be treated as a civil debt and recovered through the County Courts accordingly
- the Service Director Finance & Commercialisation reserves the right to refuse a loan for any reason
- interest will be charged on loans at an average previous year base rate plus 0.5%.

#### **33. School Converting to an Academy**

If the school converts to academy during the period of the loan, the academy or sponsor will be responsible for any outstanding loan. Any outstanding loan will be transferred into the name of the academy and will be detailed on the Commercial Transfer Agreement (CTA).

Any new loans taken out by a maintained school will need to be fully repaid should the school become a non-sponsored academy.

34. Should a school become a sponsored academy, the academy will be required to repay the loan under the original terms, unless the loan can be fully repaid without incurring a deficit, in which case the loan must be fully repaid prior to conversion. For existing loans, taken out prior to July 2015, any converting school will be able to continue to Southampton City Council Scheme for Financing Schools repay the loan in accordance with the agreed repayment schedule. This requirement would be included in the CTA.

35. Section 8 'Schools with internal loans outstanding' under DfE guidance on the Treatment of surplus and deficit balances when maintained schools become academies is copied below for reference.

*"The Department for Education would expect that the liability to repay a loan made by the LA to a maintained school (which is technically an advance of funding from the LA) would normally transfer to the academy, which would continue repayments from its revenue budget on the previously agreed schedule, unless the LA and school agree to liquidate the loan and pay it off at the point of transfer. The transfer of responsibility for the loan should be reflected in a legal agreement between the LA and the AT, either by amending the Commercial Transfer Agreement (CTA) or in a separate agreement. Any current loan repayments a maintained school has to make will need to be checked for their affordability alongside the repayment of any deficit at the point of conversion. The Department will not recognise as a loan any arrangement that is agreed between the LA and a maintained school after the governing body or IEB has made an application to become a sponsored academy or after the school becomes eligible for intervention by the SoS, unless the AT sponsoring the academy has agreed to take on the liability".*

36. **Step 6 – Monitoring a Deficit Budget**

The confirmation letter will include details of the LA's deficit monitoring requirements, with which the school must comply. During the period covered by the Deficit Recovery Plan schools will not be permitted to make any staff changes that are above the agreed level of staffing within the plan, without prior agreement of the LA.

37. The schools' progress against the Deficit Recovery Plan will be reviewed regularly the School Improvement and School Finance Teams and further meetings may be required. Failure to keep within the terms of this guidance will put the school at risk of being issued with a formal Notice of Concern, while further failure to comply may lead to the withdrawal of financial delegation.

38. **Notice of Concern**

The LA may issue a notice of concern to the governing body of any school it maintains where, in the opinion of the Service Director, Children and Families Services and the Service Lead for Education and Early Help.

- the school has failed to comply with any provisions of the scheme, or
- where actions need to be taken to safeguard the financial position of the LA or the school.

39. A notice may be issued as a first step to signal the LA's serious concerns, and will hopefully be a precautionary measure. It should be seen by the Head Teacher and the Governing Body as signalling the need for major improvements in financial management.



40. A further notice will be issued if the LA exercises its right to withdraw financial delegation responsibility from the Governing Body. Withdrawal of delegation will not normally be initiated as we expect to work in partnership with Governors to address concerns before such a stage is considered necessary. The authority will not hesitate, however, to withdraw delegation if a school consistently fails to meet the LA's stated requirements, and/or continues to exceed agreed deficit recovery plan limits.
41. Such a notice will set out the reasons and evidence for it being made and may place on the governing body restrictions, limitations or prohibitions in relation to the management of funds delegated to it.
42. These may include:
- insisting that relevant staff undertake appropriate training to address any identified weaknesses in the financial management of the school
  - insisting that an appropriately trained / qualified person chairs the finance committee of the governing body
  - placing more stringent restrictions or conditions on the day to day financial management of a school than the scheme requires for all schools – such as the provision of monthly accounts to the City Council
  - insisting on regular financial monitoring meetings at the school attended by local authority officers
  - requiring a governing body to buy into the City Council's financial management systems; and imposing restrictions or limitations on the manner in which a school manages extended school activity funded from within its delegated budget share – for example by requiring a school to submit income projections and / or financial monitoring reports on such activities.
43. The notice will clearly state what these requirements are and the way in which and the time by which such requirements must be complied with in order for the notice to be withdrawn.
44. It will also state the actions that the City Council may take where the governing body does not comply with the notice.

#### **Appendices/Supporting Information:**

Appendix 1 – Link to Current Scheme for Financing Schools

<http://www.southampton.gov.uk/policies/Scheme-for-Financing-Schools.pdf>

Further Information Available From:

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## Template for Utilisation of Balances Pro-forma

## REVENUE SCHOOL BALANCE 20XX/XX

School:

Revenue Balance as at 31<sup>st</sup> March 20XX:

Brought Forward Balance	
Allowable Surplus	
Excess Surplus	

Of which the following is:

<b>Excess Surplus</b>	<b>£</b>
<b>Committed</b>	
<b>Uncommitted</b>	
<b>TOTAL</b>	

Summary of Spending Plans:

Committed

Uncommitted

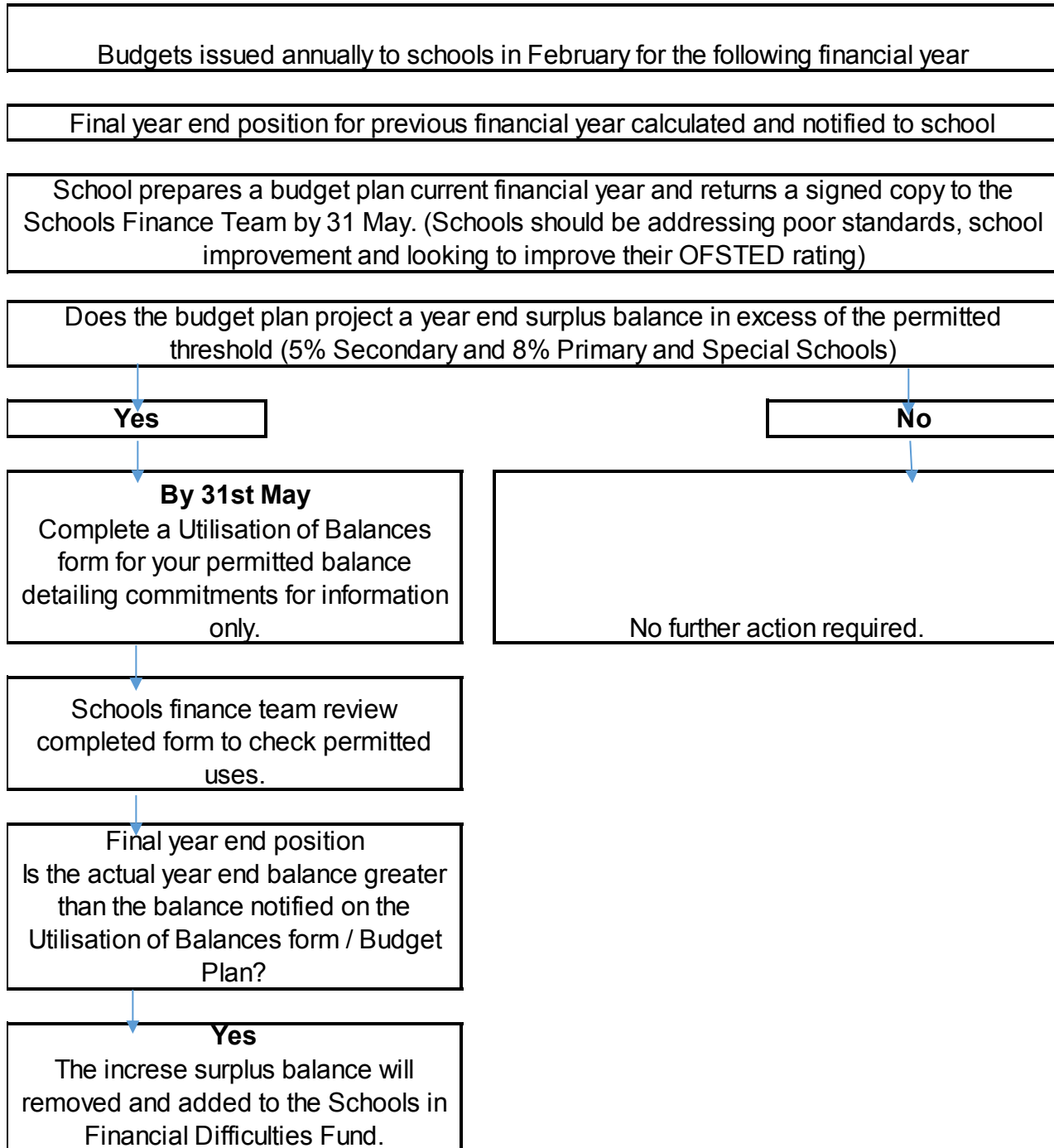
Signed \_\_\_\_\_  
Chair of Governors:

Date \_\_\_\_\_

Please return the completed form by 31 May 20XX to  
[school.finance@southampton.gov.uk](mailto:school.finance@southampton.gov.uk).

## Appendix 2

### SCHOOL BALANCE CONTROL MECHANISM 20XX/XX



# DECISION PAPER

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