3: Financial Planning Assumptions 2008/09 to 2010/11

Introduction

3.1 The Learning and Skills Council (LSC) publishes national guidance on many aspects of further education (FE) funding. Furthermore, it is important for local and regional priorities to be met. It is the LSC's intention for greater emphasis to be placed on area and regional, rather than national planning. Therefore, colleges are requested to agree planning assumptions with the LSC area offices.

3.2 **The following guidance on financial planning assumptions should be taken as being advisory rather than specific instructions.**

3.3 With the change to demand-led funding from 2008/09, it is important this year that planning assumptions are clearly set out in the commentary to the financial plan and that colleges' sensitivity analyses and risk management plans identify contingency actions where it is felt that the assumptions adopted may not be secure.

The implementation of demand led funding, within a context of greater contestability and minimum levels of performance, will result in less certainty of funding for many colleges. Some colleges will receive considerably more funding than previously, but others may receive less. The need for robust risk management regimes is therefore even more important than for previous years, and it is strongly suggested that colleges:

- carry out sensitivity analyses for individual funding streams;
- identify detailed and robust contingency plans for the loss of specific funding streams and/or funding agreements; and
- identify opportunities for securing additional funding agreements.

Colleges will want to reflect the outcome of this work in "what if scenarios", possibly preparing alternative financial plans for different situations which can be considered by their senior management teams and governors.

LSC Allocations

3.4 Guidance on the LSC's funding methodology is given in the LSC's publication, *LSC Funding Guidance 2008/09*. This consists of a number of separate documents under the overall title. The LSC seeks to establish realistic allocations in order to ensure that institutions deliver their funding agreements and that resources are made available to fund deliverable growth in priority areas.

3.5 The above publication should be read in conjunction with the following LSC documents:

- *Better skills Better jobs Better lives – Our Statement of Priorities December 2007*
- *LSC Grant Letter 2008/09 published by the DIUS November 2007*
- *Planning for Success – a framework for planning and quality*, December 2007
- *Addendum to the Statement of Priorities: Aligning Public Funding with Priority Vocational Qualifications in England December 2007*
- *Framework for managing the balance and mix of provision 2007/08, March 2007*

3.6 These documents are available on the LSC's website (www.lsc.gov.uk).

Base level of funding

3.7 The national funding rate for young people aged between 16 and 18 has been increased by 2.1 per cent for the academic year 2008/09 apart from apprenticeship learners where the increase is 1.6%. This is in line with the minimum funding guarantee for school sixth forms. Funding rates of learning aims studied by adults aged 19 and over have been increased by 1.5 per cent.

3.8 **It is important to note that these increases apply to individual learner funding rates and not to the totality of providers' funding allocations and actual increases will depend on the provider's baseline SLN rate.**

Assumed fee income

3.9 In response to the consultation on fees resulting from the Skills Strategy, the LSC is increasing the fee assumption from **37.5 per cent** of the base unit of funding to **42.5 per cent in 2008/09.** Colleges should assume that there will be a subsequent increase in the fee assumptions to **47.5 per cent for 2009/10** and to **50 per cent for 2010/11.**

3.10 The increased fee assumption means in practice that the LSC expects the overall volumes of adult learning activity to remain substantially the same, but with a shift in contributions; a reduction in public subsidy balanced by an increase in individual and/or employer contributions.

3.11 The LSC will discuss a fee income measure within the planning process for each LSC provider.

Subsequent funding increases

3.12 For financial planning purposes, all colleges should assume that, o*n average* funding rate increases for inflation continue at **2.0 per cent** a year beyond 2008/09.

3.13 **It should be noted again that rate increases should not be assumed to apply to the total value of colleges' allocations.**

3.14 Colleges should consider *Our Statement of Priorities* and the national and regional statement of priorities in determining the extent of any overall changes in the learning delivery and its impact on funding allocations. However, colleges should continue to identify, in their risk management plans, the opportunity or risk that funding may be higher or lower than their plan assumptions.

Growth funding

3.15 It is recommended that colleges discuss with their LSC area office whether or not future growth will be funded by the LSC. If colleges include any growth in their financial plan then they must identify in their risk management plans the risk that this growth is not funded by the LSC.

Standard Learner Number (SLN) definition

3.16 A learner studying a programme of 450 or more planned guided learning hours (glh) in a funding year will count as one full-time SLN. A learner studying a programme of fewer than 450 glh in a funding year will be converted to a fraction of one SLN by dividing the planned glh of the learner's programme by 450. The maximum SLN value for individual learners will be 1.75.

European Funding

3.17 The LSC is a Co-financing Organisation and uses the European Social Fund to fully fund activities based on contract costs. The funding approach is described in the current funding guidance document, *LSC Funding Guidance 2008/09,* in greater detail. If you hold an ESF co-financed contract the funding arrangements will be specified within the specific agreement.

3.18 Colleges planning to receive ESF should be aware that all ESF provision will be sought by Open and Competitive Tender and therefore will be contracted with the successful applicant.

Adjustments to Funding Allocations

3.19 The rules for funding reconciliation for 2008/09 are set out in *LSC Funding Guidance 2008/09* and particularly in document *ILR Funding Claims and Audit Return 2008/09* (to be issued in due course).

3.20 Arrangements for the submission of individualised learner record (ILR) funding claims and adjustments to allocations for underachievement in 2007/08 are set out in the booklet *FE Individualised Learner Record Funding Estimate/Claim 2007/08.*

3.21 There will be no unplanned or responsive growth payments for colleges that over-deliver in 2007/08 or 2008/09.

Other Funding and Grants Guidance

3.22 The LSC has published guidance in respect of other funding and grant programmes as follows:

- *LSC Capital Handbook, issued November 2006 due to be updated May/June 2008*
- Circular 03/03: *Development of a Common Funding Approach for Additional Learning Support*.

3.23 These documents, and any subsequent updates, are available on the LSC's website (www.lsc.gov.uk).

Staffing Costs

3.24 Colleges should continue to make their own decisions on pay awards based on the institution's individual circumstances.

3.25 The Office of National Statistics has published data showing that average earnings in the public sector have risen by between 4 and 5 per cent in each of the past four years. Colleges should therefore consider how to ensure their overall staff costs remain affordable within the resources available.

Non-pay Inflation

3.26 HM Treasury has estimated that the gross domestic product (GDP) deflator – a measure of inflation – for the year 2008/09 will be 2.7 per cent and over the years 2009 to 2011 will be 2.7 per cent each year. Colleges should use these estimates in calculating movements in the cost of non-pay items, unless they have better information about the specific price changes that will affect them.

FRS 17 Assumptions

3.27 Unless colleges know with some certainty that the balance on the pension reserve as at 31 July 2007 will improve or worsen in subsequent years, they should assume that the balance as at 31 July 2007 will remain the same over the life of the plan.

Capital Projects

3.28 The financial plan should reflect the key factors in the college's strategic plans and property strategies. Therefore, if the college is planning to conduct a capital project then this should be considered for inclusion in the financial plan. The question of inclusion revolves around the degree of certainty associated with the project.

3.29 If the college has received approval for a project at the 'Application in Principle' (AiP) stage then the project should be included in the financial plan.

3.30 If a college is likely to submit an AiP project in the budget year (year 1) then the matter *should be discussed and agreed with their regional PFM team*. The appropriateness of including planned capital projects in financial plans will only be considered by the LSC if ***ALL*** the following conditions apply:

- the education case has been endorsed by the local LSC;
- the estimated costs of the project have, for all intents and purposes, been determined [in discussion with the regional property adviser];
- the approximate timing of the project is known; and
- the financing of the project, including the LSC grant and level of borrowings has been assessed in conjunction with regional PFM teams.

If a college anticipates submitting a project in years 2 or 3 it should not be included in the plan, as it is unlikely that the conditions mentioned above for including projects in plans will have been agreed.

3.31 The college should ensure that the risks associated with major capital projects are properly reflected in its risk management and associated contingency plans.

College Mergers

3.32 Where colleges are planning to merge after the deadline for the receipt of the financial plans by the regional office, then all parties must still submit a copy of their three-year financial plan. If the merger is occurring before or on 31 July 2008 then the LSC should only receive a copy of the merged college's financial plan by the required deadline of 31 July 2008.

College Recovery Plans

3.33 Where a college is developing a strategic recovery plan and cannot provide a reliable three-year financial plan at 31 July, then it must seek consent from the regional LSC office to provide a financial plan for only the first two years (the first year will show the expected out-turn and the second year will be the budget which must be in place prior to the start of the financial year). This shortened financial plan must be submitted to the LSC by the required deadline of 31 July.

Enhanced Pension Provisions

3.34 The actual cost of any enhanced ongoing pension to a former member of staff is paid by a college annually. However, it is a requirement of FRS 17 that an estimate of the expected future cost of any enhancement to the ongoing pension of a former member of staff will need to be made and charged in full to the college's income and expenditure account in the year that the member of staff retires (this follows the principle that the future costs to a college of an individual's pension enhancement should be fully accounted for during the period that the college benefits from the employee's services). In subsequent years, a provision needs to be made in the balance sheet.

3.35 Colleges must use the tables provided in Supplement A of Circular 05/02 *Enhanced Pensions Tables* in calculating any provision for enhanced pension.

3.36 In calculating the level of the enhanced pension provision in colleges' financial statements it is necessary to look up the rate of the yield indices for UK bonds – FTSE Actuarial Government Securities, index-linked over five years (5 per cent inflation real yield). From this a net interest rate (NIR) figure is calculated, which is basically the figure for the yield indices plus one, rounded up to the nearest 0.5.

3.37 At 20 May 2008, the fixed interest 10 year yield was 4.84 (31 July 2007: 5.22) and the 5% inflation real yield was 0.96 (31 July 2007: 1.48). The NIR based on the figures at 20 May 2008 would therefore be 2.00, compared to 2.50 at 31 July 2007.

3.38 For future years, colleges should assume that the level of the NIR will remain constant at 2.00.

Other Pension Provisions

3.39 Where the college originally made a SSAP 24 pension provision for "strain on fund", the college should continue to make a provision under the auspices of FRS 17, as it relates to past contributions payable that have yet to be settled. For example, a specific amount has been calculated by the college using the pension scheme official spreadsheet and paid by the college to the scheme for early retirements of named employees.