3. Capital Funding, Budgeting and Accounting Guidance

1. Introduction

In line with the Government's Consistent Financial Reporting Framework (CFR) schools are required to account for capital income and expenditure separately from revenue income and expenditure. This separation acknowledges certain differences between revenue and capital expenditure such as the nature, time-scale and funding of the activities involved.

Revenue expenditure enables the school to continue its on-going operational functions and is of little or no value beyond the financial year in which it is incurred (e.g. salaries, energy, rates, water etc). All revenue work to school premises is LA liability, but funding for this is delegated to schools through the LA.

Capital expenditure conversely provides value and benefit to the school over a longer period of time.

Capital Funding and accounting is governed by three main sources –
The Scheme for Financing Schools especially section 13 – Responsibility for repairs and Maintenance and Capital
DfE requirements in respect of Consistent Financial Reporting

2. Definition of Capital

Capital expenditure, for schools purposes, comprises:

- The cost of acquiring land and buildings
- Cost of new construction
- Cost of conversions forming a new structure
- Cost of extensions to existing buildings
- The *enhancement** of land, road or buildings
- Acquisition of vehicles, plant, equipment or machinery (if over £5k)
- The *enhancement** of vehicles, plant, equipment or machinery
- Purchase of computer, cabling, hardware & software if over £2k (software can only be funded this way if purchased with new hardware).

*Enhancement** is where money is spent on **an existing asset** which substantially increases its value or lengthens its useful life. It excludes routine repairs and maintenance. For example, re-roofing a building would normally count as capital expenditure where as replacing missing tiles would not.

3. Classification of Work

All work to the school premises is classified as being either:

Repair and Maintenance - the cost of which should be met from the School Budget Share, or
Capital - the cost of which will normally be met from either Devolved Formula Capital funding, central LA resources or from the Governing Body of a VA

School. However if the cost of these works is below £5,000 it will be deemed as repair and maintenance and will be required to be met from the School Budget Share.

Annex D of The Scheme for Financing Schools lists the nature of works that are classified as either Repair and Maintenance or Capital

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For some projects schools may feel they have a choice as to where to charge the expenditure – capital or revenue. Generally speaking significant purchases of items of a durable nature should wherever possible be charged as capital as this:

- Ensures full use of grant
- Reduces pressure on the revenue budget
- A revenue contribution can always be made to capital but not vice versa

Any acquisition or work on the above areas costing **below £5,000** are not classified as capital and therefore must be treated as revenue expenditure. However where a capital project includes building work and furnishings and equipment which are an integral part of the project, e.g. carpets and shelving in a new library, then such items can be treated as capital expenditure as setting up costs. The cost of professional fees associated with specific building work (e.g. architects) can also be treated as capital expenditure.

Schools are provided with devolved capital funds that they must use to implement capital priority works as identified in their Asset Management Plan.

THE TREATMENT OF CAPITAL INCOME & EXPENDITURE IN THE ACCOUNTS DEPENDS OF THE LEGAL STATUS OF THE SCHOOL, AS DESCRIBED BELOW

4. Different Types of Capital Funding Available to Schools

Devolved Formula Capital (DFC)

DFC is paid quarterly via a BACS payment into the schools budget share account. It is to be used to address building improvements identified in the Asset Management Plan if over £5k. Where large schemes are being proposed and funded by the LA schools should be prepared to contribute funds from their DFC allocation.

The DfE Technical Note on Devolved Formula Capital states amongst other matters –

“It is a general principle that schools should make best use of DFC as soon as it is received. However, given the nature and size of capital projects, schools may set aside their annual allocations up to three years to fund medium sized projects.

Where, exceptionally, a school wishes to accumulate DFC for more than three years to finance a specific large project, it may do so. This applies both to unspent funds from previous periods, and to future allocations. In these circumstances, we expect the school to advance the excess funding temporarily

available to its local authority to be spent on capital projects, with the right to reclaim the amount when the school needs the money.
Any DFC unspent at the end of this period, either the three year period or the longer period regarding a specific large project, must be returned to the Department.”

Full details are given in:

http://www.education.gov.uk/schools/adminandfinance/schoolscapital/funding/a00202906/devolved-capital12-13

The authority’s measures to implement this will be to monitor schools use of DFC and require schools to complete a return at the Year end as to the school’s use of its capital funding sources. **Schools wishing to retain DFC for more than the permitted three year period must submit an application to the Schools Finance Services Manager** before the end of the financial year, stating the reason for the accumulation of DFC funding and details of the proposed project with its timescale. Subject to this being acceptable to the authority, arrangements will be made for the DFC to be repaid to the authority for use on alternative school capital projects and repaid to the school when required.

Schools should also be aware that the Schools Forum approved a proposal in July 2007 that with effect from April 2008 all schools would be expected to contribute up to 50% of the school’s annual DFC for each LA funded (non emergency) repair and enhancement project. Also for large projects a contribution from the DFC of future years would also be expected.

5. Revenue Financing of Capital

All schools, including the Governing Bodies of Voluntary Aided Schools are allowed to use their formula allocation budget share as a contribution towards the cost of any capital expenditure. Section 2.19 of The Scheme for Financing Schools states:

“2.19 Capital Spending from Budget Shares on Premises

Governing Bodies are allowed to use their budget shares to meet the cost of capital expenditure on the school premises. This includes expenditure by the Governing Body of a voluntary aided school on work, which is their responsibility under paragraph 3 of Schedule 3 of the School Standards and Framework Act 1998.

However if the expected capital expenditure from the budget share and/or balance brought forward, in any one year exceeds £50,000 the Governing Body must notify the LA and take into account any advice from the Chief Education Officer as to the merits of the proposed expenditure. If the premises are owned by the LA, then the Governing Body must seek the consent of the LA to any proposed capital works, but consent can be withheld only on health and safety grounds.”

This typically takes place where the school has an in year surplus of revenue resources over planned revenue expenditure and wishes to bring forward capital expenditure that would otherwise not take place until future years.

Capital expenditure for Direct Revenue Financing purposes includes the acquisition of land or buildings; capital works to premises, capital ICT projects including cabling etc and the purchase of equipment or machinery.

Schools that chose to use revenue resources for capital expenditure anticipate this by having income and expenditure budgets on CFR codes E30 and CI04 (Revenue Financing of Capital). Before the end of the financial year these schools need to complete an adjustment to transfer actual resources from revenue to capital consistent with the budgets set against codes E30 and CI01. **This adjustment should only take place once the work has been completed or if the work is imminent and the school is under a contractual obligation in the new financial year.**

6. Loans

Schools can apply for an advance of future year's budget share for a specific project. Full details are set out in Section 4.10 of the Scheme for Financing Schools (Loan Scheme) but it should be noted that the loan advanced to the school is repayable from future year's budget share or devolved capital allocation and is subject to interest.

7. Private Capital Income

Private or school generated income used solely for capital projects e.g. where a school's PTA makes a contribution to a capital project.

8. Budgeting for Capital

VA Schools

The land & buildings are owned by the Governors who, in the form of Devolved Formula Capital, receive funding direct from the DfE for premises and ICT capital expenditure. Therefore, for VA schools: -

DFC **must not** be paid into the school's budget share account, but into a bank account in the name of the Governors (or diocese)
VA schools **cannot** contract or pay directly for any capital work to the schools premises

Therefore VA schools are not normally expected to show capital income and expenditure budgets on their annual budget plan. However section 2.19 of The Scheme for Financing Schools states:

"2.19 Capital Spending from Budget Shares on Premises
Governing Bodies are allowed to use their budget shares to meet the cost of capital expenditure on the school premises. This includes expenditure by the Governing Body of a voluntary aided school on work, which is their responsibility under paragraph 3 of Schedule 3 of the School Standards and Framework Act 1998. "

Therefore:
VA schools are able to use any surplus revenue resources as a contribution towards a capital project that has been contracted for by the Governors or Diocese. In this event Direct Revenue Financing budgets should be shown on codes E30 & CI04 together with a capital expenditure budget on CE01 – CE04. On receipt of an invoice or letter of request from Governors / Diocese the contribution from the budget share can then be paid from CE01-CE04. (VAT may not be claimed on capital expenditure in VA schools)

Community & Foundation Schools

Community & Foundation schools receive their Devolved Formula Capital allocation direct into their Budget Share Account from the LA and must use it to implement priority capital works identified in their Asset Management Plan. The DFC should be shown under CI01 and it can also be used to purchase ICT equipment costing over £2,000 providing it conforms to the DfE publication "Transforming Teaching and Learning through ICT in Schools".

Any advance of future years DFC that the school anticipates to receive under the Council's Loan Scheme should also be shown under CI01.

Schools are also allowed to use their revenue resources towards the cost of capital expenditure. Any contribution from revenue resources should be shown on the Schools budget plan under code E30 with the same amount shown on CI04.

See section 2.19 of The Scheme for Financing Schools;

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Any private or voluntary income that has been collected for a specific capital project should be shown against CI03.

Schools should plan capital programmes over a longer period than the annual budget and three or five years is suggested. The budget should relate to that part of the School Improvement Plan relating to Asset Management or Premises Plan.

Taking into account any b/fwd capital balance, the total capital resources available as shown under CI01, CI03 and CI04 must equal budgeted capital expenditure that is planned for that financial year and future years. Note that any sum planned to be spent in a future financial year should be shown on the Budget Plan under the heading 'Capital Resources for Future Years'.

9. Accounting for Capital Expenditure - Community & Foundation Schools

Payment of Devolved Formula Capital to the school is made into the schools Budget Share Account. All associated expenditure that is incurred in connection with this funding should be paid out of the schools Budget Share Account.

Although schools do not keep separate bank accounts to distinguish between capital and revenue activity – the coding of such income and expenditure must be accounted for separately in the schools ledger / local accounting system according to the Council's coding list for schools that is based on the government's CFR framework.

Where capital funding is delegated / devolved, the school is responsible for placing orders for works and appointing contractors and demonstrating best value. In doing so the school must take proper advice from the LA to ensure it complies with Contract Standing Orders, the Construction Industry Scheme, planning and building control restrictions.

10. Accounting for Loans for Capital Purposes - VA Schools

The loan advance of revenue funds will be transferred into the school's Budget Share Account and should be recorded as capital income to CFR code CI01. On receipt of an invoice or letter of request from Governors / Diocese the contribution from the budget share can then be paid from CE01-CE04. (VAT may not be claimed on capital expenditure in VA schools)

For each of the repayment years the school will receive the amount of its annual budget share less the annual repayment of loan principal. The school should not account for this as expenditure, but as reduced funds delegated by the LA on CFR code I01.

The school will receive invoices annually for the interest payable on the loan. This cost should be coded to CFR code E29.

11. Accounting for Capital Loans - Community & Foundation Schools

Community and Foundation schools can repay the loan advance from their future years Budget Share or their future years Devolved Capital Allocation. If the loan is deemed an advance of the school's Budget Share, the repayments are financed from revenue resources and the accounting treatment is the same as shown above for VA Schools. If the loan is deemed an advance of the school's Devolved Formula Capital allocation, the repayments are financed from capital resources and the accounting treatment is as set out in the following example:-

The school applies for a loan of £80k over 4 years. The school requires the loan to be advanced in April 20xx to enable it to undertake a capital project earlier than would otherwise be possible. The school will finance the annual repayments of loan principal from its future years Devolved Formula Capital allocations.

The loan advance will be transferred into the school's Budget Share Account and should be recorded as capital income to code CI01. The full cost of works for which the loan was obtained should be charged to the relevant capital expenditure code at the time of incurring the expenditure, CFR codes CE01-CE04.

For each of the repayment years the school will receive the amount of its Devolved Formula Capital allocation less the agreed annual principal repayment. The school does not account for this as expenditure, but as reduced Capital Income on code CI01.

For each of the repayment years the school will also receive an invoice for interest accrued which it should pay by drawing a cheque from its Budget Share Account for the required amount, charging CFR revenue code E29.

12. Monitoring

Schools are recommended to monitor actual capital expenditure against budgeted on a monthly basis to ensure the following:

- Medium and short term plans, goals and objectives are being achieved
- That the priorities of the schools AMP and SIP can be re-assessed
- Expenditure incurred is within budget
- To identify any errors (for example incorrect coding of expenditure)
- To identify at an early stage any additional resource requirements or surplus funds available

13. Contact Points

Any queries relating to budgeting and accounting for capital works should be made to;

Schools Accountancy Section on 020 8359 7228 / 7223 / 7227 or schools.accountancy@barnet.gov.uk

Any queries relating to the Council's Capital Programme should be made to;

Children's Service Finance Team on 020 8359 7147