

**MAYOR OF LONDON**

# **GLA Adult Education Budget 2019-23**

Annex 6 – Financial Health Requirements and Guidance



**European Union**

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Social Fund

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## Definition and Purpose

### *Definition*

1. The term organisation is used within this guidance to refer to colleges, higher education institutions, training organisations, local authorities and employers who are applying to be awarded contracts for education and training services as part of the GLA's Adult Education Budget (AEB) 2019-23.

### *Purpose*

2. This document sets out the GLA's approach to financial due diligence in respect of organisations who have been recommended to be awarded a contract for education and training services.
3. This approach is taken to understand an organisation's financial health and the degree of risk to the GLA in contracting with them.
4. We use financial health as a measure of an organisation's financial status, in terms of its financial performance and its ability to meet ongoing financial commitments.

## Overview and Due Diligence Assessment

### *Overview*

5. The GLA will only award contracts to Bidders that successfully pass the GLA’s financial due diligence process. Bidders will have to submit their financial due diligence information as part of the tender process and the GLA will undertake the financial due diligence checks on Bidders that have been recommended for a contract award following the ITT evaluation process.

### *Due Diligence Assessment*

6. The GLA will assess the financial health of Bidders in accordance with the process set out below. This follows a similar approach to that taken by the Education and Skills Funding Agency (ESFA) in previous years of awarding a financial health rating based on three key financial indicators: performance, solvency and borrowing.
7. Once the key financial ratios have been calculated, Bidders will be assigned a financial health rating of Outstanding, Good, Satisfactory or Inadequate and such rating may be subject to a moderation process, as detailed within this guidance. The GLA will determine whether to award contracts based upon the designated financial health rating as outlined in the table below:

<b>Financial health rating</b>	<b>Recommended action</b>
Outstanding	Award of contract
Good	Award of contract
Satisfactory	Award of contract conditional on agreement to contract management mitigation strategies
Inadequate	No contract awarded

## Financial Information and Data Source

8. Financial health for organisations is graded, based on the following three elements:

- Performance (performance ratio / Earnings before interest, tax, depreciation and amortisation (EBITDA))
- Solvency (current ratio)
- Borrowing (debt ratio)

9. To facilitate the financial health assessment, organisations must supply the following documentation as part of the bid (wherever applicable):

Audited accounts for the past 2 years, or accounts for the past 2 years signed by an independent qualified accountant, if your organisation is exempt from audit.

- Accounts that are exempt from audit must include all of the following information:
- a full set of notes
- a Director's report
- a balance sheet
- a statement of organisation turnover
- a profit and loss account / income & expenditure statement
- a cash flow for the most recent full year of trading/operations, where this information is not available in audited form

10. If your organisation, due to its legal form, is not required to produce statutory financial statements, you must submit accounts in the format used for producing annual accounts. These must include the same minimum elements noted within paragraph 9.

11. If your organisation is unable to supply statutory financial statements because it has not traded for a sufficient period, you must supply management accounts to date, showing actual activity, along with forecast figures for a remaining period. The combined information must cover a period no less than one year, with the management accounts comprising at least three months of actual trading activity. As a minimum, these must consist of:

- a profit and loss account covering a 12-month period
- an end of period forecast balance sheet

- a 12 month rolling cash flow statement
  - detailed narrative supporting assumptions made for both management accounts and forecast information
12. For an organisation to be awarded a contract, it must have been actively trading for a minimum period of three months. If the financial information demonstrates that an organisation has not been actively trading for this minimum period, then it is not eligible to be awarded a contract and its bid will be rejected. “Actively trading” is determined here as including income and expenditure arising from a result of trade and does not include the incurrence of set up or start-up costs.
  13. We will assess management accounts and financial forecasts submitted pursuant to paragraph 12 on an individual basis and the financial scored in line with the criteria set out in Appendices A and B.
  14. If any of the required financial information is missing, we will grade financial health as “Inadequate”, due to insufficient information available for assessment.

## Parent Companies

15. In accordance with the principle in Regulation 63 of the Public Contracts Regulations 2015, an organisation or a group of organisations bidding for a contract may rely on the capacities of a third party to demonstrate financial health (e.g. a parent or group company) of the bidder or bidding group. In such circumstances, the third party being relied upon must provide the financial information and satisfy the requirements set out in this guidance and provide a guarantee or otherwise confirm it will be jointly liable for the execution of the contract if the bidder is successful. The financial health assessment will be undertaken upon the third party being relied upon.

## Consortium

16. If you are bidding as a Consortium, all the relevant documents above (wherever applicable) must be submitted for all Consortium members. In the event one or more of the members is rated 'inadequate', a contract will not be awarded.

## Sole Lead Bidders

17. If you are bidding as a Sole Lead Bidder with subcontractors, it will be your responsibility to check the financial health of your subcontractors. The financial health assessment will apply only to your organisation, as the Sole Lead Bidder with whom the GLA will have the contractual relationship.

## Exemptions

18. Local authorities are not subject to the standard GLA financial due diligence checks as they are well established public bodies, backed by Government funding and supported by local government legislation, whose Section 151 Officers (Chief Financial Officers) are in a position to guarantee their financial standing and honour their financial commitments.

## Moderation Criteria



19. We reserve the right to moderate any initial grade. Moderation criteria include, but are not limited to the following:
- a. We will not grade higher than 'Satisfactory' if an organisation scores 0 points for any one of the three ratios, meaning if you score high enough in two of the three ratios to get a Good rating but score 0 in the other ratio, the highest grade you will be awarded is 'Satisfactory'.
  - b. Where auditors have given the financial statements a qualified or adverse opinion, they will be classified as 'Inadequate' and will not be awarded a contract.
  - c. We will grade financial health as 'Inadequate' if your organisation is in liquidation, insolvency, a Company Voluntary Arrangement, or has become dormant.
  - d. We will grade financial health as 'Inadequate' if financial statements are overdue for filing at Companies House or the Charities Commission (or equivalent statutory registers)

## Increase in Contract Value

20. The financial due diligence checks that are undertaken during this procurement exercise may be repeated prior to an award of an increase in contract value to confirm that the financial health of the organisation has not fallen below what was originally tested during this procurement exercise. Should the organisations financial health fall below that was originally tested, an increase in contract award may not be offered (depending on the revised grading – See Appendices A and B).

## Appendix A – Financial Health Elements

### (ratios)

All organisations (except local authorities) will be assessed on three key financial health elements: performance, solvency and borrowing, with the following elements (ratios) computed for each.

Element	Definition
Performance	<p>EBITDA – Earnings before interest, tax, depreciation and amortisation is defined as</p> $\frac{\text{EBDITA}}{\text{*Income}} \times 100$ <p>*Income</p> <p>*For this purpose, income will be adjusted to exclude capital grant</p>
Solvency	<p>Current ration defined as:</p> $\frac{\text{Current Assets}}{\text{Current Liabilities}}$
Borrowing	<p>Borrowing as a % of income</p> <p>Borrowing is defined as Overdrafts + Short-term Loans + Long-term Loans + Total Capital Finance Leases</p> <p><b>Divided by: Income</b></p>

## Appendix B – Financial Health Scoring and Grading

For each of the three elements a score will be awarded as shown below:

Score	Performance	Solvency	Borrowing
0	< 1%	< 0.5	>= 60%
10	>= 1%	>= 0.6	< 60%
20	>= 2%	>= 0.7	< 55%
30	>= 3%	>= 0.8	< 50%
40	>= 4%	>= 0.9	< 45%
50	>= 5%	>= 1.0	< 40%
60	>= 6%	>= 1.2	< 35%
70	>= 7%	>= 1.4	< 30%
80	>= 8%	>= 1.6	< 20%
90	>= 9%	>= 1.8	< 10%
100	>= 10%	>= 2.0	= 0

We will make a grade assessment by comparing the aggregated points score with the assessment criteria shown below.

Grade	Grade Assessment	Description
Outstanding	240 to 300 points	An organisation that has very robust resources to fulfil its contractual obligations comfortably (as indicated by at the aggregated points score).
Good	180 to 230 points	An organisation that appears to have sufficiently robust resources to fulfil its contractual obligations (as indicated by at the aggregated points score).
Satisfactory	120 to 170 points	An organisation that appears to have sufficient resources to fulfil contractual obligations (as indicated by at the aggregated points score).
Inadequate	<= 110 points	An organisation that appears to be in financial difficulty (as indicated by at the aggregated points score). There is a significant risk that organisations in this group not being able to fulfil contractual obligations because of weak financial health.

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