# CLIVE OWEN LLP ACADEMY NEWSLETTER

## OCTOBER 2019

CLIVE OWEN LLP
CHARTERED ACCOUNTANTS & BUSINESS ADVISERS

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# 1. Introduction

Clive Owen LLP are one of the country's leading advisers to academy trusts on accounting, audit and taxation matters. We have been advising academies for over 12 years and currently audit 45 academy trusts across the North East and Yorkshire. Whilst Clive Owen is an independent practice we are part of the Kreston network that advises over 10% of all academy trusts in England. Each year the Kreston firms collate the information they hold on academies to enable a detailed benchmarking report to be produced. We are pleased to say that Chris Beaumont, one of our partners, is one of the lead authors of this report.

**If you would like a copy please contact marketing@cliveowen.com**

**The last few months have seen a number of announcements that will impact on the financial position of academy trusts.**

Early in the year we had the substantial increase in the employers teachers' pension contribution from 16.48% to 23.6%, eventually followed by the announcement that there was to be some time limited funding now replaced with a £1.5bn/year funding for this expense.  In August the government announced an additional £14bn of funding for the sector (2020/21:£2.6bn, 2021/22:£4.8bn, 2022/23: £7.1bn) leading to a minimum funding by 2021/22 of £5,000 per secondary school pupil and £4,000 per primary school pupil. A move towards a national funding formula?

In early September in a bid to address teacher shortages, the government also announced plans to substantially increase primary and secondary teachers' starting salaries by circ £6,000 to £30,000 by 2022-23. The funding for this being included in that announced in August. Whilst this additional income is welcome at a time when trusts have told us that they are having problems balancing the books, given the likely implications on all pay bands of the planned increase in starting salaries, it must be hoped that the additional £14bn announced is sufficient to cover this. In addition, the recent McCloud judgement may mean that employers LGPS rates increase in due course, yet again increasing the costs. Given that we are living in uncertain times and we don't know the detail of these planned changes, it is important that academies ensure they have appropriate management information and controls in place. This is something Lord Agnew is putting specific emphasis on with this years' changes in the Academies Financial Handbook (AFH) and the Academies Accounts Direction (AAD).

## 2. Changes in the AFH 2019

Whilst the audit for the year ended 31 August 2019 will focus on compliance with the AFH 2018, the AFH 2019 which was released in June is effective from 1st September 2019 and will therefore be the focus of next year's audit.

There are a number of significant changes in the new AFH 2019 and it is important that trusts review and implement any changes they need to make as soon as possible.

**The main changes are as follows:**

### Management accounts (2.18 – 2.23)

Last Year the AFH introduced the requirement that the trust prepare management accounts on a monthly basis that MUST be shared with the Chair of the trust, each month and with the other trustees at least six times a year, including when it meets. Section 2.21 of the new AFH specifies that these management accounts MUST include:

- **Income and expenditure account;**
- **Variance to budget report;**
- **Cashflow; and**
- **Balance sheet.**

The Management accounts MUST now also include key financial performance indicators and measure the trusts performance against them (2.22).

The AFH also states that 'managers MUST take appropriate action to ensure ongoing viability' (2.18) and states 'where the board has concerns about financial performance, it should act quickly ensuring the trust has adequate financial skills in place' (2.23).

### Internal Scrutiny (3.1 – 3.22)

The Internal Scrutiny rules have been significantly enhanced. What was nine bullet points has become twenty. This expanded section now sets out what the committee responsible for this function MUST have in place – written terms of reference, annual programme of work that provides coverage across the year, review of risk register and review the relevant reports amongst other things (3.12). It is very important that trustees review this section as it is important that the trust ensures it has the proper structure in place to ensure it minimises the risks it has. Not unsurprisingly, given some of the issues that the ESFA have found at a number of trusts, Lord Agnew is increasing the departments focus on how trusts undertake this important function.

Previously the AFH specified that a trust SHOULD have a risk register, it now states that they MUST have a risk register (2.36).

There is now more of a focus between the items on the risk register and testing to ensure that the controls in place, which supposedly minimise these risks, work as expected.

Since the AFH was released, the ESFA have issued a bulletin, which sets out that for 2018/2019 each trust must submit a copy of their latest internal audit/assurance report to the ESFA with their 31st August 2019 financial statements.

For 2019/20 the ESFA require that each trust prepare a summary of the work undertaken during the financial year which will need to be submitted to them with the 31st August 2020 financial statements.

**Executive Pay (2.30 - 2.31)**

The AFH 2018 introduced rules regarding the setting of executive pay. These have been enhanced with words like 'robust', 'decision making' and 'pay and benefits represent good value for money'. There is also a new section on commercial interest, 'ensuring the board is sighted on broader business interest held by the senior executives'. This appears to be an attempt to ensure that all earnings directly or indirectly paid by the trust to the executive team are disclosed.

**Whistleblowing (2.41 - 2.46)**

The rules about whistleblowing have been expanded. In particular the trust SHOULD appoint at least one trustee and one member of staff who other staff can contact to report concerns.

**Gender pay gap (2.32)**

A reminder that all trusts with more than 250 employees must publish information on their website and on the government reporting website about the gender pay gap in their organisation.

**Notifications to the ESFA (2.51 – 2.55)**

This section reminds trusts that they MUST notify the ESFA, within 14 days, via the Get Information About Schools (GIAS) platform of changes to the following:

- **Members**
- **Chair of trustees**
- **All other trustees**
- **Accounting Officer**
- **Chief Financial Officer**

**(including direct contact details for all)**

The GIAS should also be updated for all academies within a multi-academy trust when any of the following change:

- **Head Teacher (including direct contact details)**
- **Chair of LGB (where adopted), including direct contact details**
- **Members of the LGB (where adopted)**

**Others**

A requirement for trusts with an active Financial Notice to Improve (FNtI) to publish it on their website (6.15).

Clarification regarding related party transactions (5.1 and 5.40 – 5.43) – see later section for further information on the significant changes introduced in April.

Emphasising that the audited financial statement MUST be provided to members (4.4)

Guidance about the work of a clerk to the board (1.38)

Guidance about good estates management and the ESFA tools available (2.14)

Ensuring senior employees are on the payroll (2.33)

List the authorities that are revoked when a FNtI is issued (6.15)

Sets out how the Secretary of State may intervene if they become concerned about an academy (6.19 – 6.23)

## 3. Changes in the AAD 2019

The ESFA released the 2018 to 2019 Academies Accounts Direction (AAD) in May for those trusts that were incorporated before 31st December 2018 (There are some additional changes for those who incorporated after the 1st January 2019 due to changes in accounting standards). The model financial statements are now contained in annex A, rather than in the main body of the document.

It's probably not surprising given Lord Agnew's focus on governance that the ESFA have now produced a list of regularity tests that they 'suggest' external auditors undertake to 'support the conclusion on regularity'. These tests are detailed in annex B of the AAD.

The document also mentions that where consolidated financial statements are prepared, the regularity work also applies to all other entities within the group.

Whilst the document lists at the front the main changes, having reviewed the whole document there are some other points which we feel are worth noting which we have included below.

### Transfers where fixed assets are bought from unrestricted funds (5.1.11)

The AAD highlights that where assets are bought from GAG there should be a transfer from GAG to Restricted Fixed Assets. This is consistent with how trust's have historically dealt with these transactions.

Where, however the assets are bought from unrestricted funds the AAD state that this does not require a transfer. This may lead to a different approach to that commonly adopted by trusts.

### Related party transactions (6.6.4)

The AAD defines related parties as including:

- Parties with control over, or controlled by, the entity eg parent and subsidiary companies
- Parties having significant influence over the entity
- Key management personnel of the entity, including any director, whether executive or otherwise
- Close family members of any of the above; and/or
- Others subject to control or significant influence by any individual referred to above

When determining whether someone is deemed to be a related party, the issue of significant influence has always had to be considered.

The definition set out above would seem to include relationships where we do not believe there would be any significant influence. It therefore seems to us that the definition is wider than most readers may expect.

As noted in section 5, from 1 April 2019, all new transactions with related parties need to be notified to the ESFA, and approval obtained for those transactions which are cumulatively over £20,000. Confirmation of compliance with this will now be required in the related party note to the accounts (6.6)

### Changes to disclosures in the financial statements

- Removing the requirement to include the dates of any payments made regarding non statutory/non-contractual staff severance payments. (Note 10b)
- Removing the table within the funds note which showed the current and prior 12 months movements combined. (Note 19)

- There are more fixed asset categories in the notes to the financial statements. Where fixed assets have two or more components trusts need to consider if there are different economic lives e.g. the boilers or windows in a building compared to the structure. This potentially adds further complexity to valuations of buildings at conversion (Note 14)

- Prior year comparatives will be required for agency arrangements, events after the reporting period, contingent liabilities and guarantees, letters of comfort and indemnities (note 27)

- Clarification that the guarantee from Parliament in respect of the LGPS liability relates to academy trusts not individual academies (note 30)

- The pension note has been updated, but it does not give the new rate, stating instead 'the employer contribution rate is expected to be reassessed and will be payable from 1st September 2019'. Given we are signing the financial statements after this date, and we know the rate is 23.6% this note will need updating (note 30)

### Clarification – who should receive accounts, capital grants and the purchase of alcohol

- Including the requirement that a copy of the annual report and financial statements be sent to every member of the company and to every person who is entitled to receive notice of general meetings (1.6.3. This is repeated in the 2019 AFH)

- Specifies that grants received for capital purposes must be spent on capital projects in line with the terms and conditions of the grant (7.4.3).

- Clarification that irregular expenditure includes all alcohol and any excessive gifts including those purchased through unrestricted funds. We have confirmed with the ESFA that this includes the buying of alcohol even when used/resold at a fundraising event. The only exception that has been agreed to date is the purchase of communion wine for faith trusts. As a result we expect PTA's to become more active in fundraising where the purchase and possible sale of alcohol is involved (1.22)

### When a donation can be recognised from a trading subsidiary

- SORP update bulletin 2 section 3 which includes rules about when to recognise a donation from trading subsidiaries has been updated. Now donations can only be accrued where there is a legal obligation on the subsidiary to make the payment. We are recommending that trusts take advice on the implementation of a covenant (5.1.9)

### Including of a rent cost when no rent is paid

- Those schools that use premises rent free, there is the option of including a donation and related expenditure. The problem for most schools will be obtaining a relevant rental valuation that the trustees consider reliable (7.7)

## 4. Risk protection arrangements (RPA) changes

From 1st September 2019 the RPA deduction from the general annual grant (GAG) reduced from £20 per pupil to £18 per pupil for the 2019/20 academic year. The cover offered will remain the same.

The ESFA have also guaranteed that the GAG deduction will not exceed £20 per pupil for the academic years 2020/21 and 2021/22.

## 5. Related parties transactions

There are new requirements in respect of related party transactions which were implemented 1 April 2019.

**For all new transactions, irrespective of value, the ESFA must be advised in advance via their online portal.**

Where the value of the transaction(s) exceeds the following, the ESFA must give their approval before the transaction is undertaken:

1. Contract exceeds £20,000; or
2. Contracts that take the value of contracts with the related party above £20,000 in the same financial year; or
3. Any additional contracts issued after either 1 or 2 above have occurred.

Note – Pension benefits and related employment costs are exempt from the above.

## 6. Update about ESFA approval for related party transactions at a faith based school

The guidance concerning related party transactions between a faith based trust and the diocese was updated on the 2nd of October. If you now set up a supplier on the ESFA's portal and confirm the transaction is with the diocese, the form no longer requires you to input further information about the supplier or the relationship. You will however need to confirm the transactions are:

- Solely provided as part of your voluntary contribution or levy to the diocese for the purpose of maintaining the religious ethos or character of the academy trust or character of the academy trust; and
- Do not include traded services

If you then select 'yes' the trust is confirming that the services can only be provided by the diocese and that they are essential functions that are fundamental to the religious character and ethos of the school. If the transactions exceed £20,000 evidence will need to be uploaded. The transaction are deemed to be at cost.

If 'no' is selected the form continues as before.

# 7. Education contacts

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