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Our summary of the Academies Financial Handbook 2018

Our summary of the key changes trustees and finance staff need to be aware of.

The Education and Skills Funding Agency (ESFA) have published the new Academies Financial Handbook (AFH) 2018, which is effective from 1 September 2018.

The AFH sets out the financial management, control and reporting requirements that apply to all academy trusts. It describes a financial framework for trusts that focuses on principles rather than detailed guidance and reflects their accountability to parliament and to the public.

Compliance with the Handbook is a condition of each trust's funding agreement. It is therefore vital that your academy trustees, finance staff and your Accounting Officer are all aware of the forthcoming changes so that they can ensure the trust is fully compliant from the effective date.

The new AFH has been published a month earlier this year, giving trusts plenty of time to prepare before the summer holiday period and the effective date. In his opening Executive Summary Lord Agnew highlights boards' responsibilities for effective oversight and robust challenge.

There are a number of key changes in the new Handbook, some of which may be challenging for smaller trusts. These changes appear to be designed to reinforce some of the areas the ESFA have focused on recently as they seek to improve governance, financial management and transparency in the sector.

The AFH itself contains a summary of the main changes, but we have outlined these here with our own insight and commentary on what these changes may mean in practice, along with the action we recommend that you take to prepare.

Three key changes:

Delegated authorities for related party transactions

- [3.10.4, 3.10.6 and 3.10.7] The new Handbook introduces some key changes in respect of related party transactions (which is now the conventional term adopted rather than 'connected parties').

UHY commentary

From 1 April 2019 trusts will be required to report all transactions with related parties in advance of the transaction taking place, via the ESFA's online form. Since this is a 'must' requirement any failure to notify the ESFA in advance will be a breach of the Handbook, and would need to be reported in the Accounting

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Officer's regularity and propriety statement in the annual financial statements. The Handbook does not distinguish between income and expenditure transactions here, and so the expectation is that the ESFA should be notified even before a related party makes a donation to the trust!

For higher value transactions above £20,000 it will be necessary to obtain approval from the ESFA in advance. The £20,000 threshold can be breached by an individual contract, or a number of contracts with the related party in the same financial year.

The only exemption in respect of notifying or obtaining approval from the ESFA are salaries and other payments made to an individual under a contract of employment through the trust's payroll.

These changes are, in our view, welcome, and should do a lot to stop some of the situations that have occurred, resulting in bad press for the sector. The great majority of trusts abide by the related party transaction rules, and many err on the side of caution and avoid transactions altogether. One can assume that some of the specific situations that have made headlines in the media in recent years, and which were blatant flouting of the rules, would not have been allowed to happen under these new rules. The repercussions will be serious for any trust and its trustees found to be not complying with the new rules.

Clause 3.10.20 of the new Handbook clarifies one specific case where trusts make contributions to its diocese for services it receives that only the diocese can provide. These will now be regarded as meeting the 'at cost' requirement.

Management accounts

- [2.3.3] The new Handbook introduces some specific detail and frequency in respect of the preparation of management information and how often this is shared with trustees.

UHY commentary

The rules were relaxed slightly in the 2015 Handbook in recognition of the difficulties some small trusts had preparing monthly management accounts. The relaxed rules then allowed a 'monthly budget monitoring report' rather than full accruals basis management accounts. Now, presumably in an attempt to bring an increased level of rigour to internal financial reporting in view of the pressure on budgets, the rules have been tightened back up. Now all trusts must:

- Prepare management accounts every month which set out financial performance (a Statement of Financial Activities (SOFA) or Income & Expenditure Account), position (a Balance Sheet), budget variance reports and cash flow forecasts.
- Share the management accounts with the Chair of Trustees every month irrespective of the size of the trust, and with the other trustees six times a year.
- Select and use key financial performance indicators and measure performance against them regularly.

Monthly management accounts may be a challenge for some small trusts, particularly single primary academies.

The requirement to share the management accounts with other trustees at least six times a year suggests that the management accounts should be shared, at least half termly, with all trustees and not just the Finance Committee. Trusts may need to assess their approach to how they prepare financial information and report this internally to ensure they can deal with these new requirements from 1 September.

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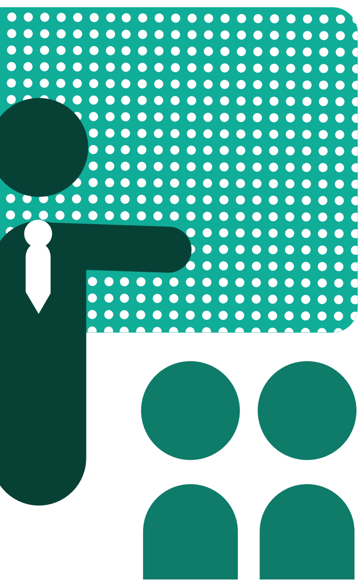

Frequency of full board meetings

- The Handbook explains the reporting requirements if the board meets less than six times a year [2.1.2].

UHY commentary

Boards must meet at least three times per annum, but the new requirement to explain how the board maintains effective oversight if there are less than six meetings is a clear indication that the ESFA would expect, in most cases, for there to be a meeting every half term. Single academy trusts and very small MATs may find this is too often, but if they do not hold six full board meetings they will need to disclose in the governance statement within the annual accounts how the board maintained effective oversight with fewer meetings. We would recommend that you consider the number of meetings very carefully because the ESFA are likely to look unfavourably on any trusts holding less than six meetings that find themselves in financial difficulty.

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Other changes:

Roles and responsibilities

- Highlighting directions the Secretary of State may make in relation to members, trustees and other individuals [1.2.7 and 1.2.8].

UHY commentary

The new AFH merely clarifies the Secretary of State's powers, subject to the relevant provisions in the trust's funding agreement, to require a trust to remove a member or trustee. The Secretary of State can also prohibit individuals – for example someone subject to a caution or conviction – from becoming a member or trustee.

- Referring to the Charity Commission's role in addressing non-compliance [1.2.9].

UHY commentary

Whilst the ESFA act as the regulator for academy trusts it should be remembered that trusts are exempt charities and have to comply with general charity legislation. The Charity Commission do not directly govern exempt charities, but they do retain an interest, and the new AFH makes it clear that the ESFA may refer trusts to the Charity Commission where there is a concern. In reality this is unlikely to be something the ESFA do often.

- Referring to the Charity Commission's role in addressing non-compliance [1.2.9].
- Updating the description of the role of members to align with the Governance Handbook [1.4.1 to 1.4.5].

UHY commentary

Taking these two points together, the terms 'trustee' and 'member' often cause confusion in the academy sector, and also how these interact with 'director'. Trustees and directors are one and the same; the former is a charity term and director is a term from company law. The ESFA have always preferred to use the term trustee since trusts are exempt charities. The new AFH acknowledges that in some trusts, commonly where there are church academies, the term 'trustee' is also used for those on the board of the separate trust that often owns the land, and this can therefore cause confusion.

Members – akin to shareholders in a commercial company – are again defined in 1.4. The role of the member is explained clearly and that it should be an "eyes on hands off" approach. The AFH makes it clear that employees of the trust must not be members unless permitted by the articles, and that the current model articles do not allow this. The Department for Education's strong preference for there to be at least five members, more than the basic minimum of three, is also reiterated. The strong preference

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for a majority of members to be independent from the board of trustees is also stated. This remains a difficult area for trusts since it is hard to attract trustees; it is arguably harder still to attract members who will have no tangible decision making power. As we have commented previously, in the general charity sector it is common for the members and trustees to be the same people.

- Removing the term 'ex-officio' to avoid suggesting an academy trust's senior executive leader would automatically act as a trustee [1.5.1].

UHY commentary

Previous AFH's have used the term 'ex-officio' since for early academy trusts it was usual for the Accounting Officer ("AO") to be a trustee automatically by virtue of his or her role. Whilst it is probably still more common for the AO to be a trustee, the AFH now acknowledges that this only may be the case, giving trusts some flexibility here.

Financial and governance requirements

- Confirming that trusts must apply robust cash management [2.2.1, 2.3.3 and 2.3.5].

UHY commentary

Cash management speaks for itself and is not a new requirement. However the Handbook reiterates how this can be achieved through the use of a robust control framework and a strong, accurate budgeting process. Previously the Handbook said that the trust "should manage its cash position, avoid going overdrawn, and reconcile bank and control accounts regularly." Now cash management must be "robust" and a stronger statement that the trust must avoid becoming overdrawn is included.

- Setting clearer requirements for budgeting [2.3.2 and 2.3.3].

UHY commentary

These sections make it clear how rigorous the budgeting processes should be. Both the Budget Forecast Return Outturn in May and the new 3-year Budget Forecast Return in July must be approved by trustees before submission. Budgets need to be compiled accurately, using realistic assumptions, and reflect lessons learned from previous years. Pupil numbers, so important as they underpin the revenue forecasts, should be challenged.

We are hearing a lot about Integrated Curriculum Financial Planning ("ICFP") at the moment, and boards are encouraged to consider this.

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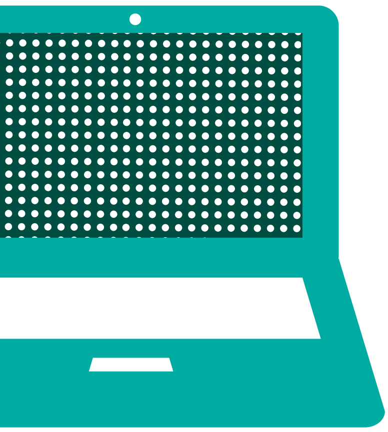
- Recommending the national deals for schools [2.4.2].

UHY commentary

The DfE have introduced various procurement tools to help all schools achieve value for money. The Handbook contains links to their guidance explaining how to plan and run an efficient procurement process and the national deals available which can bring savings on energy and water, through interest free loans for energy saving schemes, printing and photocopying costs, Microsoft software licensing and ICT purchases. Most academies seem to be aware of these deals and the benefits they can bring, and with potential savings of, for example, 40% on photocopier and printer costs, it would be foolish not to look at them.

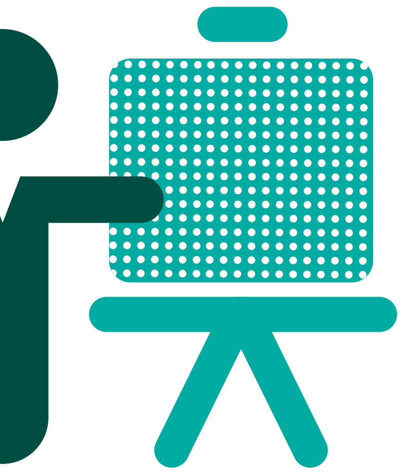


- Strengthening expectations about the process for setting executive pay and highlighting gender pay gap reporting [2.4.4 and 2.4.5].

UHY commentary

There has been a large focus on executive pay recently, and the ESFA have written to trusts paying over £150,000 to their CEO

It is clear that trusts need to be able to justify higher levels of remuneration, and boards should maintain strong written records that document how their decisions were reached. We recommend that boards benchmark their executive pay levels against other local trusts of a similar size.



and/or over £100,000 to two or more staff. It is clear that trusts need to be able to justify higher levels of remuneration, and boards should maintain strong written records that document their decisions and how these were reached. The media have picked up on some of the high levels of pay at some trusts, and in particular amounts paid to non-teaching staff. The Handbook comments that there should be a basic presumption that non-teaching pay should not increase at a faster rate than that of teachers. We recommend that boards benchmark their executive pay levels, particularly for the CEO/Accounting Officer, against other local trusts of a similar size.

- Clarifying the section on the risk protection arrangement ("RPA") [2.6.2 and 2.6.3].

UHY commentary

This section clarifies that the RPA does not cover all possible risks. Areas not covered by the RPA are not mentioned specifically, but include motor insurance and foreign travel.

- Emphasising the proper handling of whistleblowers [2.7.1].

UHY commentary

The previous Handbook only required trusts to maintain appropriate procedures for whistleblowing. The new edition comments that "the trust must ensure that all concerns raised with them by whistleblowers are responded to properly and fairly." It may be helpful to refer to ESFA's guidance on procedures for dealing with complaints.

- Confirming reporting requirements in relation to internal challenge (internal audit) [2.9.7 to 2.9.9].

UHY commentary

The requirement to manage risk by developing a programme of risk review and checking of controls remains. Trusts remain free to approach this in a way appropriate to their circumstances,

Findings from internal audit and similar reports would normally be reported to the Audit or Finance Committee. The new Handbook suggests that the findings reports should be circulated to the full board even when a separate sub-committee has already reviewed them.

and it would be reasonable to expect sizeable MATs to have a detailed internal audit service. In our experience most trusts will buy this in from a firm of auditors; some will use their external auditors, others prefer to use a different firm. The use of a non-employed trustee with appropriate skills, or a peer review from another trust, remain options but both of these are quite rare. Our approach to a full internal audit service can be tailored to a trust's individual requirements, but often follows a programme of themed visits, each focusing on specific areas of risk. The new Handbook makes it clear that the findings of the work, whichever form it takes, must be made available to all trustees promptly.

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Audit requirements

- Focussing on the importance of acting on audit advice [4.3.1].

UHY commentary

There must be an appropriate, reasonable and timely response to any findings by auditors. Year end management letters that have to be submitted to the ESFA with the financial statements require a management response, but it is easy for a comment to be added and then not actioned. It is important that any control issues and weaknesses identified are rectified soon after the audit since, by then, several months of the new financial year will have passed.

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- Highlighting how the ESFA may take action where trusts do not comply with requirements for submitting financial information [4.8.4].

UHY commentary

Last year the ESFA announced that it would 'name and shame' any trusts that were late in submitting two or more required returns during the 2017–18 reporting year. Now the Handbook clarifies that the ESFA may conduct investigations if information is delivered late or is submitted but is not of acceptable quality. The Handbook moves on to say that the ESFA may deduct the cost of any resulting investigations from the trust's recurrent funding.

- Annex C now identifies some 'musts' that are particularly relevant to boards.

UHY commentary

Annex C to the Handbook is a very useful list of all the 'must' requirements, and we recommend that this is circulated to all trustees and key finance staff as a reminder of the Handbook requirements.

The new edition introduced an opening section of "top 10 musts for chairs and other trustees" which are particularly pertinent.

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THE NEXT STEP

You can read the full AFH 2017-2018 **here**.

If you have any questions or concerns over our summary, or indeed in respect of reporting requirements for academies more generally, please contact your usual UHY adviser or find your local academy expert on our website at **www.uhy-uk.com/academy-schools**.

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