



Review of Financial Administration and Governance at E-ACT: Final Report

March 2013

External Assurance team
Education Funding Agency
Department for Education

Executive summary

1. This report is our final report into the matters set out in [REDACTED]'s letter to [REDACTED] of 30 January 2013, as we have completed all of the work we are able to do with the information that has been supplied to us. It follows the Interim Report that was sent to [REDACTED] on 25 February 2013 which covered the first phase of this review, focusing on the arrangements at E-ACT's head office in London. The second phase involved interviews and testing at three E-ACT academies, which were completed by the end of February and evaluation of some documents and reports that E-ACT was given until the end of February to provide. All of that documentation has now been provided. This report updates the Interim Report as appropriate and is therefore a complete report of our work in relation to the complaint made about E-ACT.
2. Our field work prompted a number of unsolicited contacts from current and former E-ACT staff who made suggestions as to where our work on procurement should focus. These contacts also made a number of allegations relating to the management style of E-ACT's leadership which, while concerning, were beyond the scope of this review.
3. Our findings are summarised below. These have been discussed fully with E-ACT at a formal feedback meeting on 8 March 2013.
 - E-ACT has not acted swiftly to follow-up assurances in respect of corporate governance and senior staff expenses given to the Department in 2010;
 - Overall the complaint in relation to improper procurement in E-ACT is unproven, though E-ACT is not fully exonerated. E-ACT has broadly accepted that its procurement activity in relation to the engagement of a number of consultancy contracts did not comply with their own procurement processes. EU procurement rules may also have been breached. Board and Committee minutes indicated non-compliance purchases totalling £393k; our review of the [REDACTED]'s cost centre indicates that £361k has been spent on consultancy fees from 2008/09 with £237k of this not having an order. E-ACT has conducted an internal investigation into this matter. However, there is no written report or any other indication of proposed action.
 - The sample of academies visited did not provide any further evidence of incorrect procurement
 - E-ACT's approach to governance where a number of Board members receive payment is problematic in terms of the general requirements for charitable trusts and may constrain the ability of the Board to hold the senior executives' leadership to account;
 - KPMG's draft management letter in relation to the year ended 31 August 2012 has 30 recommendations; 19 classified as high risk and 11 classified as medium risk. It includes comments on the general capacity and skills level in financial reporting across the organisation. In KPMG's view the growth has meant that controls, processes and oversight at both a governance and management level have been, and still are, playing catch up;
 - E-ACT's systems of internal financial control are weak. Bank reconciliations

are not performed routinely. In 2011-12 these were not done until June 2012. In 2012-13 none had been completed at the time of our visit although officers have subsequently confirmed that the bank has been reconciled as at 18 February 2013. Administration of VAT is also a particular area of concern;

- The boundaries between E-ACT and its subsidiary, E-ACT Enterprises Ltd (EEL) are blurred. A number of activities undertaken by the subsidiary have been paid for with public funds and so appear irregular;
 - The controls around expenses for trustees are weak, there appears to be a culture of acceptance of non-compliance with E-ACT policy and a lack of rigour in the review and challenge applied by E-ACT finance;
 - Expenses claims and use of corporate credit cards indicate a culture involving prestige venues, large drinks bills, business lunches and first class travel, all funded from public monies. There is some evidence that alcohol purchased for business lunches is reimbursed but the audit trail is poor.
4. We have set out a number of steps that should be taken by EFA to progress matters. These include:
- Feedback to E-ACT and its external auditors;
 - A decision be made as to whether there should be a formal investigation in relation to procurement of professional services;
 - A decision made as to whether EFA should issue a Financial Notice to Improve;
 - A follow-up visit to E-ACT before the end of academic year 2012/13.

Background to the review

5. On 12 November 2012, [REDACTED] of E-ACT and [REDACTED] wrote to the EFA to advise that E-ACT's external auditors (KPMG) had concluded that they were unwilling to place reliance on E-ACT's internal control processes during their 2011-12 audit and that their 2011-12 financial statements would be submitted late.
6. In January 2013 [REDACTED] wrote to [REDACTED] setting out a number of complaints from a 'whistle blower' relating to E-ACT. [REDACTED], who has ministerial responsibility for academies, asked that EFA conduct a review to establish the substance of the complaints. The complaints covered a number of areas including:
- Failure to follow proper procurement procedures;
 - Financial concerns about travel and subsistence.
7. There were also complaints concerning E-ACT's culture, management practices and procedures. However, these did not fall within the EFA's remit. The EFA review is restricted to matters related to the proper and regular use of public monies and, in so far as it relates to that issue, the effectiveness of financial controls and governance within E-ACT.

8. On 30 January 2013, ██████████ of EFA wrote to ██████████ explaining that the EFA would carry out a fact-finding review. A copy of the letter is attached.

E-ACT's history

9. E-ACT was founded in 2009 to establish and operate academies following the break-up of a predecessor organisation, Edutrust Academies Charitable Trust, which had been sponsored by the British Edutrust Foundation (Edutrust), chaired by ██████████. Ties with Edutrust were severed in 2009 and E-ACT became a sponsor-less Multi-Academy Trust, chaired by ██████████, who remained as chair until 2012 when he was replaced by ██████████. At 1 September 2011 E-ACT was operating 14 academies and free schools and has grown further to 32 institutions currently. E-ACT remains committed to a growth strategy. Throughout, E-ACT's ██████████ has been ██████████; to whom the board have delegated operational management. The D-G is also E-ACT's accounting officer.

Previous concerns

10. This review covers some of the same ground as previous complaints and concerns raised with the DfE about E-ACT and its predecessor organisation, Edutrust Academies Charitable Trust.
11. In late 2008 DfE Internal Audit conducted a review into Edutrust Academies Charitable Trust's proper use of grant funding which found that there had been a number of instances of irregular expenditure and others where review work was inconclusive. Findings included instances of payments to related parties, conflicts of interest, profligacy and overall poor financial control. Following this review the Chair stepped down and the link to the sponsor, Edutrust, was removed.
12. In April 2010 both the DfE and the NAO received a letter of complaint setting out concerns about E-ACT's approach to governance and propriety. The matter was also raised with the Charity Commission. Issues raised included inappropriate use of external consultancy, conflicts of interest relating to payments to a supplier who was also a chair of two E-ACT academies and inappropriate recruitment. The original complainant made further complaints in relation to allegations of profligacy which had appeared in the national press. DfE officials met with E-ACT and found that: the matter was inconclusive; or that E-ACT was able to prove satisfactory assurances; or that the issue was not for DfE. The single outstanding issue related to E-ACT's practice of remunerating chairs of governing bodies in some academies which was contrary to Charity Commission rules and which was also held to be contrary to E-ACT's own Memorandum and Articles. In June 2011 NAO wrote to DfE to state that they considered that this matter was not fully resolved.

Fact-finding review approach

13. This review has involved:-

Consideration of matters raised in the draft management letter by E-ACT's external auditors KPMG in relation to the 2011-12 financial statements (though not a re-performance of this work).

Consideration of aspects of the operation of corporate governance within E-ACT.

On site work at E-ACT head office to examine some:

- Travel and subsistence claims by E-ACT Directors and Senior Leadership Team members;
- Use of corporate credit/charge cards by E-ACT Directors and Senior Leadership Team (SLT);
- Some procurement activity by E-ACT.

The review involved interviews with:

- [REDACTED] (Director-General);
- [REDACTED] (Chair of the Board);
- [REDACTED] (Chair of the Audit and Risk Committee)
- [REDACTED] (Director of Finance)
- E-ACT staff at head office and academies.

Visits have also been conducted at the following E-ACT academies:

- Dartmouth: 13 February 2013;
- Heartlands: 21 February 2013;
- Shenley: 25 February 2013.

14. While the review team was at E-ACT, it received a small number of unsolicited contacts from current and former E-ACT staff who wished to speak to us on conditions of anonymity. A substantial portion of what these contacts said was connected with the management style at E-ACT and so was not within the scope of this review. However, they also indicated that certain procurements by E-ACT had been irregular further supporting the complaint initiating this review.

Findings

We found concerns in the following areas:

Governance

15. The composition of E-ACT's board is unusual and gives rise to concern that the ability of the Board to effectively hold the SLT to account is constrained.
16. It is E-ACT practice for some chairs of governors at individual academies to also serve on the E-ACT Board. There are currently four academy chairs on the Board. It is also E-ACT practice to remunerate some academy chairs. Three of the four Board members who are academy chairs, are paid as academy chairs. Three Board members including the Chair also hold current or past consultancy contracts with E-ACT. Although the Chair has a contract we understand that no payments have been made to date. Together with [REDACTED], this means that around half of the 13 current Board members have or have in the past had contracts for service or services provided.
17. Payment to trustees is unusual in the charities sector, where the basic position is that trustees should not benefit personally from their position as trustees so that they can exercise independent scrutiny over the charity's operations. This point is set out clearly in Charity Commission publication "Trustee expenses and payments (CC11)":

"The concept of unpaid trusteeship has been one of the defining characteristics of the charitable sector, contributing greatly to public confidence in charities. The basic principle is that trustees must not put themselves in a position where their personal interests conflict with their duty to act in the interests of the charity unless authorised to do so".

18. This matter was raised with E-ACT by DfE in 2010, and assurances were received that E-ACT's Memorandum and Articles did allow Directors, or firms associated with Directors, to be paid for services other than as Directors so long as certain specified procedures were followed (set out in CC11).
19. CC11 also establishes that:

"The statutory power (to pay trustees) can only be used if, at the time in question, the total number of trustees receiving payment from the charity's funds will be in a minority on the trustee board".

20. E-ACT has been seeking legal opinion to support its interpretation of CC11 guidance that past payment to a trustee is not an issue. We also received assurances from E-ACT's Board Manager that work was currently underway to amend E-ACT's Memorandum and Articles along the lines of a model set developed by DfE for Multi Academy Trusts. However, almost three years after this matter was first raised by DfE it has not been concluded.
21. The SLT headed by the D-G contains two former DfE employees, one of whom has joined this month. One of the allegations received during the review was that some or all of the appointments to E-ACT of former civil servants was contrary to the civil service business appointment rule. This is a DfE matter. Allegations in relation to the appointment of one SLT member were considered

by DfE in 2010 and there were not found to be any fundamental problems with his appointment to E-ACT. Likewise, it has been confirmed that there were no impediments to the February 2013 appointment either. These allegations therefore appear to be unfounded.

Financial Controls

22. There are issues around financial controls, particularly bank reconciliations and VAT and also concerns on the capacity and skills level in financial reporting.
23. Unlike the majority of academy trusts E-ACT financial statements were not submitted by the 31st December deadline. E-ACT informed us that this was due to the late implementation of the regularity assurance approach for academy trusts, together with the rigour with which the new external auditors KPMG were conducting their work. The financial statements have yet to be finalised and this is unlikely while this review is in progress.
24. KPMG's draft management letter in relation to the year ended 31 August 2012 has 30 recommendations; 19 classified as high risk "matters that are considered fundamental against which management should take action as soon as possible" and 11 classified as medium risk "matters that are considered significant that should be addressed within 3 to 6 months". It points to a number of areas of financial administration within E-ACT capable of improvement and includes the following comments:
 - General capacity and skills level in financial reporting across the organisation are not at the level they need to be in light of expansion and increasingly complex reporting;
 - The Trust "has grown rapidly within an environment of earned autonomy and in (the auditors') view this growth has meant that controls, processes and oversight at both a governance and management level have been, and still are, playing catch up".
25. At the time of our visit the dialogue between E-ACT and KPMG was drawing to a close and, although there were matters where E-ACT contested the significance of some of KPMG's observations in many areas E-ACT broadly accepted KPMG's criticisms. We note in particular that:
26. E-ACT has not demonstrated a consistent and disciplined approach to bank reconciliation: a usually routine monthly procedure in any business and, in an organisation with a turnover of many millions of pounds, an absolutely fundamental one. This was noted in the external auditors' management letter, and acknowledged by E-ACT. At the time of our visit no bank reconciliations had been completed for 2012-13. E-ACT's finance team have now carried out what appears to be a very rudimentary bank reconciliation as at 18th February 2013 and includes a number of aged items.
27. Another significant concern noted by KPMG is that, currently, E-ACT's current practice in relation to VAT attribution on purchases, and especially in relation to capital items, means that VAT may not be correctly recovered and even that

penalties and interest could be incurred. This has been borne out by our own testing in relation to expenses claims and charge cards.

28. The boundary between EACT and its subsidiary EEL is blurred. EEL has been established principally to “sell” E-ACT “know-how” in the UK and abroad. There is inconsistency in practice as to when E-ACT “charges back” costs it has borne on EEL’s behalf. This includes travel claims by [REDACTED] and payments to consultants. Such sums are immaterial in terms of E-ACT’s own accounts. But they are material to the accounts of EEL which in 2011-12 had a reported turnover of only £14k.

Supplier/professional services

29. It was not practicable for the review to look at the entirety of procurement practice across E-ACT. The review work focussed on areas raised through anonymous contact or identified in E-ACT’s own Board or Committee minutes as problematic.
30. E-ACT board minutes from 2012 indicated that there had been procedural irregularities in respect of certain contract lets and that the extent of irregularity was £393k. The E-ACT Chair of Audit and Risk Committee (CARC) led the review into the “procedural discrepancies” (i.e. payment processed with no purchase order present) around these lets. The CARC confirmed to us that he had conducted a review into these lets. Although the Finance Director was able to provide us with EACT’s own underpinning numerical analysis which supported the CARC’s review, the “report” (to E-ACT’s Board on 26 April 2012) was merely verbal. Consequently, we are unable to conclude that the review was rigorous or that all of the matters in question were addressed or resolved. It is both surprising and disappointing that no Board paper was tabled in connection with the CARC’s investigation into this very serious matter, especially in the context of significant changes in E-ACT’s Board at the time. The Board minutes of 26 April also record the wish of the new Chair to “draw a line” under these matters and to “move on” and so it seems reasonable to conclude that this must have been the directors’ central concern at the time. The CARC advised us orally that he considered the figure of £393k to be overstated in terms of non-compliance as it contains a number of payments to suppliers where, in any event, it would not be usual for there to be a purchase order in place (e.g. rail bookings). Our review of [REDACTED] cost centre indicates that £361k had been spent on consultancy fees from 2008/09 with £237k of this not supported by an order. Both the board minutes and the CARC personally indicated that the following lets were problematic:

31. [REDACTED]
[REDACTED] is a consultant in education in the UK and overseas, with specialist knowledge in e-learning and strategy development. [REDACTED] is an associate of WSP Ltd/Edunova which conducts education work in the Middle East as well as the UK. E-ACT Board Minutes from 2012 indicated that a contract let by E-ACT to [REDACTED] had not been properly procured, though this is disputed by [REDACTED].

32. It appears that a portion of the work undertaken by [REDACTED] was overseas and so likely to be for the benefit of EEL as opposed to EACT and it is not clear that all of these costs have been fully charged out to EEL.
33. [REDACTED]
[REDACTED] are a consultancy firm specialising in strategy development and working in the field of education. E-ACT engaged [REDACTED] to provide support and guidance on a number of projects. E-ACT board minutes from 2012 state that the contract with [REDACTED] had not been properly procured and that, in relation to 29 invoices submitted, only two had purchase orders that could be associated with them.
34. The extent of irregularity in respect of the above lets needs to be carefully considered. There is no suggestion that services were not rendered, but there is that the contractors were previously known to E-ACT. The issue is about E-ACT failing to follow its own procurement procedures and demonstrate appropriate value for money. It was also a matter of concern that E-ACT finance would process invoices without associated purchase orders.
35. The CARC's view was that the quality and capacity of procurement and finance functions within E-ACT is not all that it should have been but they had learned the appropriate lessons following the 2012 allegations and improving (e.g. a procurement manager was appointed in 2012) and would continue to improve. In the absence of any written report we cannot confirm this conclusion.
36. The CARC indicated that there had also been problems associated with lets to [REDACTED] and [REDACTED]. It was not possible to look at these in detail during our site visit. However, it appears that two suppliers may have been paid sums, for contractual work, that were in excess of the EU procurement thresholds and therefore required an EU tender advert and procurement process and as a minimum should have been subject to market testing.
37. The above indicates that E-ACT has almost certainly not followed its own due and proper process in relation to the procurement of professional services. However our interviews with Principals at three E-ACT academies provided no complaints or other evidence to support any claim that inappropriate professional services had been "hard sold" to the academies by E-ACT head office.
38. The focus of our work has been on professional services procured via the D-G's personal cost centre and so we are unable to form any conclusions as to the extent of compliance or non-compliance with proper procurement practice throughout E-ACT as a whole. It is therefore disappointing that we have not been able to place any reliance upon the internal review commissioned by the CARC which may have gone some way to provide some additional comfort in relation to procurement generally.

Directors' expenses

39. We looked at expenses reimbursed to E-ACT directors for 2010-11, 2011-12 and 2012/-3 (to date)

40. General observations

We found a tolerance of a degree of low-level non-compliance with the approved policy and/or a lack of capacity by the finance team to apply consistent standards of scrutiny. We noted that some expenses incurred in relation to EEL, the subsidiary company, have been charged to E-ACT and subsequently included in the expenses declarations/disclosures for Trustees' in connection with E-ACT business. The amounts involved are relatively small and would not have impacted the material accuracy of E-ACT's own financial statements. But it does mean that these payments have been charged against public funds and that the expenses for ██████████ in E-ACT's draft 2011-12 financial statements and in previous years' financial statements have been misstated. It also indicates a blurring of the demarcation lines between E-ACT and EEL but more testing in this area would be needed to establish the full extent to which EEL is receiving public subsidy via E-ACT.

41. Specific Observations

Our observations in relation to a selection of specific expenses claims are:

- There is a potential significant risk to the organisation in the event of a VAT inspection, due to the incorrect treatment of VAT;
- There is a lack of rigor to ensure that costs are coded to correct cost centre/subsidiary organisation;
- There is a lack of management control over the safekeeping of original documentation with several invoices and claim forms in our sample being 'lost';
- We identified breaches of E-ACT expenses policies indicating an apparent lack of verifying of expenses claims at the point of authorisation;
- There is no specific expenses policy for Board members who instead use the staff policy;
- When expenditure limits specified within the expenses policy are exceeded approval should be sought in advance. However, in practice this is only done retrospectively;
- Overpayments have been identified through error and incorrect processing of VAT;
- E-ACT does not have a comprehensive Scheme of Delegation;
- Failure to recover season tickets loans for rail-fares within a 12 month period;
- Extravagant use of public funds for an annual strategy conference held at Ashridge Business Centre in April 2012 at a total costs of £15,990 which included a pre-event meal, and hire of a room specifically for pre-meal drinks. The room and drinks bill totalled approximately £1,000.

42. A claim involving ██████████ in business travel to Dubai in February 2011 was examined. This may have been legitimate in terms of his support for EEL and was authorised by ██████████ but the costs do not appear to have been charged out to EEL and so have been met from public funds.

Credit/charge card payments

43. We looked at a number of transactions on E-ACT's corporate credit cards in relation to the current academic year to date.

44. General observations

Similar to our observations regarding expenses we found issues of non-compliance with the policy in relation to items purchased and the level of supporting documentation supplied.

Discussions indicate that claims submitted by ██████████ may not be subjected to appropriate scrutiny. The control is that the Chair authorises his claims but we understand that she expects the claim to have been compiled correctly using the guidance and that finance will carry out their checks only after she has authorised these. The check from finance is mainly that the Chair has authorised the claim and payment is then made. The process can therefore be circular and is consequently diluted.

45. Specific observations

Our specific observations in relation to a number of transactions effected via E-ACT's credit card are as follows:

- Visa receipts are often provided as supporting evidence for meals so there is no record of purchases or names of recipients. This practice results in an inability to be able to recover VAT. This contravenes the expenses policy which requires names of all persons and who they are representing to be included in the claim;
- Meals claimed are generally lunch and include alcohol; both appear to contravene E-ACT policy although some alcohol is permitted if entertaining. At least one of these events was a meeting between E-ACT Board members only. Evidence was provided of reimbursement by ██████████ of alcohol via credits on bank statements on occasions but this was not linked back to purchases resulting in an incomplete audit trail. The ██████████ has acknowledged the inadequacy of practice to date and has set out his expectations for better record keeping from now on;
- ██████████ has travelled a mix of first class and standard class and an SLT colleague has travelled first class when accompanying him. This contravenes the policy which states that all employees should travel standard class (the Director of Finance has stated that the D-G's employment contract does permit first class travel, but the contract has not been provided);

- ██████ claims for a monthly lunch at the Reform Club with no details of who attends. He has confirmed that these visits are on special occasions where it is necessary to impress a potential benefactor;
 - Some element of challenge was evident as the Director of Finance queried ██████ claim containing £213.00 of alcohol. A business case was completed retrospectively and authorised by ██████, but should have been approved in advance;
 - Some minor items of expenditure which appear to contravene the policy were identified e.g. flowers.
46. The Bloomsbury Hotel was used for a governance workshop and Board meeting at the suggestion of consultants. Ten people attended an evening dinner, seven stayed overnight with more attending the day itself. Total cost was £5,406.00 (£2,200 charged to credit card and £3,206 settled by bank transfer). It was noted that ██████'s credit card had limits set at £5000 as total card limit and £3000 per transaction. This means that it would not have been possible to process this booking wholly through the credit card. The splitting of payments in the way could be seen as a means to circumvent these embedded controls. We spoke to ██████ about this event and he advised that it was booked at short notice and on the advice of a consultant who suggested that the E-ACT boardroom was not appropriate; further that, because of the short notice, it was not possible to secure a sponsor to foot the drinks bill as would usually be the case.
47. The Director of Finance broadly accepted the control weaknesses in relation to our testing of both trustee expenses and the use of corporate credit cards by senior staff. He also stated that work would be undertaken to develop guidance to include a detailed list of allowable items.

Conclusion and Next Steps

48. In relation to the matters set out in ██████'s letter of 30 January 2013:
- Our findings in relation to potential collusion with associates regarding procurement of professional services are inconclusive and the complaint unproven. E-ACT has certainly cut a few corners in relation to the procurement of professional services and almost certainly broken EU procurement rules. While we found no direct evidence of deliberate wrongdoing, we are unable to state that processes are consistently robust or offer good value for money.
 - Expenses claims and card payments by senior managers in E-ACT have occasionally stretched the concepts of propriety and value for money. Controls have been lax and some payments have tended to extravagance. However, we found no evidence of fraud.
 - Transactions with related parties, particularly E-ACT Enterprises Limited, have not been fully recognised and it seems that there has been a flow of public monies into EEL that cannot be said to directly benefit teaching and

learning in E-ACT academies

- Good corporate governance at E-ACT is necessarily compromised by the trust's practice of having "payroll" board members and it remains to be seen as to how effective the Chair and other directors will be at holding executive management to account.
49. We also concur with the view of E-ACT's external auditors that financial control within E-ACT has considerable scope for improvement.
50. We think EFA's next steps should be:
- E-ACT should be informed of the outcome of this review (this was done at a meeting at their office on 8 March 2013).
 - Consideration should be given to whether this review has established sufficient grounds to warrant the commencement of a formal investigation into procurement of professional services by E-ACT.
 - Consideration should be given to whether concerns set out both in this review and in the draft management letter from KPMG about the weaknesses in financial control at E-ACT are of sufficient seriousness that they warrant EFA issuing a Financial Notice to Improve.
 - EFA should provide a copy of this report to E-ACT's external auditors to assist them in finalising their audit work and E-ACT encouraged to co-operate with the auditors so as to finalise their 2011/12 accounts
 - Without prejudice to the decisions required above, consideration should be given to a follow-up visit to E-ACT before the end of academic year 2012/13 to establish that sufficient progress has been made in respect of weaknesses identified.