



Education  
Funding  
Agency

# **Review of related party transactions in academies**

**November 2014**

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## Executive summary

The Education Funding Agency (EFA) carried out a rigorous, risk-based analysis of all related party transactions disclosed in academy trusts' financial statements for the 2012 to 2013 academic year. This document explains what is meant by related parties and explains the policy. It also summarises the findings and provides case studies and further information to assist academy trusts in complying with the requirements. The conclusion is that the vast majority of transactions are properly managed and disclosed.

The review provides:

- case studies which demonstrate beneficial relationships with connected parties
- case studies where the nature of the transactions was more questionable and the subsequent actions taken by EFA
- examples of best practice when undertaking related party transactions
- information on the impact of the introduction of the 'at cost' policy
- further measures to improve understanding and compliance with the policy
- a comparison with how other publicly-funded sectors manage such transactions and potential conflicts of interest

Of the 2,256 financial statements received from academy trusts covering the 2012 to 2013 reporting period, 1,350 related party transactions were disclosed by 976 trusts.

The disclosures made by 922 trusts (94.5%) were sufficient to enable us to conclude that the transactions were properly entered into. EFA identified the disclosures made by the remaining 54 trusts (5.5%) as requiring further follow-up work to enable EFA to reach a conclusion. EFA's review of the disclosures made by these 54 trusts concluded that the related party transactions at the vast majority of trusts (98.3%) were compliant with EFA's accountability framework. Transactions at 17 trusts (1.7%) were found to be irregular and/or improper. In the small number of cases where transactions were found to be irregular or improper, EFA has taken appropriate and robust action.

The review also found examples of related party transactions that offered tangible benefits to academy trusts as well as being compliant with the Academies Financial Handbook.

The introduction of the Department for Education's 'at cost' policy, combined with the recent investigation and enforcement activity EFA has undertaken has reinforced the importance of this issue. The package of additional measures identified in this report will ensure the understanding of the current policy is improved and enhance compliance.

## Background

### What is a related party transaction?

1. Related parties arise where one party has control or influence over the other, or where the parties are subject to common control. This includes parent companies and their subsidiaries, key management personnel including company directors, their close family members and other entities in which these parties have a controlling interest. Accounting standards require transactions between related parties to be disclosed in company financial statements as related party transactions.
2. Such transactions are permitted under company law, charity law and under the Academies Financial Handbook, provided that open and transparent procurement procedures have been followed, and any potential conflicts of interest are adequately and appropriately managed.
3. Due to the nature of academy trusts' operations and the fact that many academy trustees are drawn from local public and private sector organisations, it is unsurprising that some related party transactions occur. Our review of the related party transactions disclosed by trusts identified the most common types of related transactions to be the purchase, sale, lease or donation of goods, services, property, or money.

### Disclosure requirements

4. The disclosure of related party transactions is standard accounting practice across the private and public sectors. Such disclosures provide accountability and transparency to the public and Parliament and demonstrate that potential conflicts of interest are being identified, managed and reported.
5. Accounting standards require related party transactions to be disclosed in a reporting entity's financial statements so that users can gain a full understanding of the transactions which have taken place, and any factors that might have influenced them.
6. EFA's Academies Accounts Direction sets out that, for academy trusts, related parties include:
  - parties with control over, or controlled by, the entity (for example 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
  - others subject to control or significant influence by any individual referred to above

7. Where related party transactions had occurred, the Academies Accounts Direction, section 7.6.10 stipulated that disclosure must be made and should include:

- the names of the related parties
- a description of the relationship between the parties
- a description of the transactions
- the amounts involved
- the amounts due to or from related parties at the balance sheet date, and any provisions for doubtful debts or amounts written off

8. The 2013 Academies Accounts Direction (sections 7.6.13 to 7.6.18) also requires a separate related party disclosure for the remuneration and expenses paid to a principal, staff trustees and other trustees. This disclosure is in line with the Charity Statement of Recommended Practice. Whilst trustees cannot usually be paid for their work as trustees, they can claim expenses.

9. Academy trusts are required by company law to have the disclosures made in their financial statements subject to independent audit by a registered auditor. The trust's auditors are also required to undertake a regularity review which covers the regularity of both expenditure and income. This review provides assurance to Parliament and the public that income and expenditure have been applied for the purposes intended.

# Findings from review of academy trusts' financial statements

## Approach

10. EFA received 2,256 financial statements from academy trusts covering the 2012 to 2013 reporting period. Related party transactions were disclosed in the financial statements submitted by 976 (43.3%) academy trusts. In total 1,350 related party transactions disclosures were made by those 976 trusts. The table below summarises the initial judgements made by EFA.

Related Party Transactions Disclosed	Total	%
Sets of financial statements disclosing one or more related party transactions.	976	100
Disclosures sufficient to enable us to conclude the transactions are not a 'potential risk'.	922	94.5
Transactions assessed as a 'potential risk', meaning further work was required.	54	5.5

**Table 1 – Financial statements with related party transactions disclosed and initial judgements**

11. All were reviewed for compliance with the requirements of the 2012 to 2013 Academies Accounts Direction and to confirm that they were undertaken at arm's length and followed transparent procurement procedures.

## Reasonableness of transactions

12. When scrutinising related party transaction disclosure notes, EFA applied judgement over whether any transactions posed a 'potential risk' to public funds. For example, if disclosures were insufficient to demonstrate that transactions were properly entered into and were reasonable in nature.

13. Indicators of risk considered by EFA included the number, value and nature of the transaction, as well as the position of the connected party within the trust, their capacity to control and influence the decision making process and other known risk factors at the trust. Potential risks were highlighted in respect of 54 financial statements. This represents 5.5% of the financial statements which had reported related party transactions or 2.3% of all financial statements received. EFA undertook further work to ascertain whether the transactions were regular and proper.

14. The key reasons why follow-up work was necessary in these cases is that the related party transactions had not been fully explained, the value of transaction, the type of transaction, or the individual with the related party (for example principal, accounting officer, chair of the board of trustees or chief executive officer) were a cause for concern.

15. The vast majority, 48 of the 54 cases (89%), were not flagged as an issue by academy trusts' auditors in either their audit report on the financial statements, or their report on regularity.

16. In five cases related party transactions were identified within the auditor's regularity reports. The conclusion of the report covers the regularity of both expenditure and income and is included within the trust's financial statements. Trusts' financial statements are published on the Department for Education's web pages and the Academies Accounts Direction requires trusts to publish them on their own websites.

17. In one case the auditor issued a 'disclaimer of opinion' as they were not in a position to express a specific opinion on the overall status of the financial records. This was due to the trust's failure to maintain adequate accounting records and because the trust's trustees were unable to provide adequate representations.

## **Follow-up work undertaken**

18. Whilst the vast majority of transactions disclosed were not assessed as a potential risk, the disclosures made by 54 trusts were judged to be potentially irregular/improper due to the number, value and nature of the transactions disclosed.

19. A definition of irregular and improper transactions is at Annex A.

20. EFA undertook extensive dialogue with accounting officers, chairs of trustees and/or principal finance officers to understand the nature of each transaction, the procurement or recruitment processes undertaken, and the measures trusts had in place to prevent and manage any potential conflicts of interest.

21. This follow-up work found that the majority of trusts (37) were able to demonstrate that they had applied satisfactory procurement procedures and that the transactions did not represent an irregular or improper use of public funds.

22. Table 2 below summarises the outcomes of the 54 cases followed up:

View on transaction	Number of trusts	Nature of the issues identified
Trusts where all transactions were deemed to be regular and proper	37	N/A
Trusts with transactions deemed irregular and / or improper	13	Potential conflict of interests in procurement or non-compliance with the trust's own procurement procedures
	1	Honorarium payment made without prior EFA approval. Payment made 'on-payroll'
	1	Honorarium payment made to senior staff. Payment made 'off-payroll'
	2	'Off-payroll' payments made to senior staff as consultants
	<b>54</b>	

**Table 2 – Findings of follow-up cases and emerging themes**

23. EFA is working with those 17 trusts where issues were identified with procurement procedures and/or the management of potential conflicts of interest to ensure that their procedures and internal control arrangements are improved. EFA is requiring those trusts which have made honorarium payments to seek retrospective approval. In a small number of cases EFA is considering whether there has been a breach of HMT guidance on the tax arrangements of public sector appointees.

## Transactions deemed to be irregular and / or improper

24. Whilst the enquiries made were dependent on the specific nature of the transactions disclosed at each trust, they can be broadly categorised as seeking to establish:

- further detail on the nature of the transactions
- how the trust managed potential conflicts of interest
- what procurement procedures were undertaken by the trust
- whether the procurement complied with the trust's own financial/procurement regulations
- how the decision to transact with the related party was taken and if there was any involvement by the related party during this process
- how the trust ensured that it received value for money
- if the transactions were ongoing



25. The issues in relation to the 17 transactions identified as being irregular and/or improper include the following:

- One academy trust failed to apply appropriate procurement procedures before the appointment of consultants during the set-up phase of an academy trust. Payments to the managing director were off payroll, but this person is now employed by the trust.
- One academy trust did not pay its chief executive officer through the payroll system (avoiding PAYE) in contravention of HMT guidance.
- One academy trust received services from an accountancy firm in which a trustee (the finance director) is the sole director and partner, an expansion of the services supplied was not subject to a tendering process.
- Two academy trusts paid honorariums; one was made to a chair of governors, the other to an individual employed by the trust. The payment to the chair of governors was not made through the payroll system in contravention of HMT guidance. Ex-gratia payments/honorariums require EFA approval in advance of the payments being made. However in these cases prior approval had not been sought.
- One academy trust paid staff working on activities that exclusively benefited the related party company. This expenditure was determined to be irregular and funds recovered.
- One academy trust employed several family members of the principal without undertaking proper recruitment procedures. The same trust also paid the chair of the board of trustees for services provided as both chair and interim business manager. Funds have been recovered.
- Ten academy trusts failed to follow sufficient procurement procedures when entering into related party transactions and/or failed to demonstrate that potential conflicts of interest had been adequately managed.

26. Where EFA has identified either irregular and/or improper transactions, it has undertaken proportionate enforcement action. This can include issuing a Financial Notice to Improve, recovering funds, requiring trusts to retender contracts or issuing letters to trusts to formally inform them of the areas of non-compliance, requiring them to improve their tendering processes and/or improve the management of potential conflicts of interest.

27. The type of the enforcement activity undertaken depended on the nature and severity of the issue identified. EFA will continue to monitor closely the remedial measures undertaken to ensure compliance.

28. The case study below illustrates the nature of some of the issues identified during the review process, the subsequent action taken by EFA and the current position.

## Case study 1 - Related party transactions at an academy trust

The chair of the trust's governing board was paid more than £90k in respect of his role as chairman; a close relative of the chair received £28k in respect of rent and insurance for a property; there were related party transactions with companies in which the chairman has a controlling interest; and two governors claimed £45k in expenses and other supplies and services.

EFA informed the trust that the case was flagged as a risk and the trust was subsequently subject to a review of financial management and governance. The review took place in March 2014 and identified an absence of oversight by the board of trustees and control at trust level. The review also identified that a robust management and control framework was not in place and a number of significant breaches of the Companies Act 2006, Charity Commission regulations and Academies Financial Handbook had occurred.

### The key findings from the investigation:

- Charity commission rules and the DfE's current model articles do allow trustees, who are employed as CEOs, or Staff Directors/ Governors to be paid in respect of their executive position. However, only in exceptional circumstances can a trustee be paid for carrying out the role of a trustee, and in all cases prior consent to amend its articles to allow it to do this must be obtained from the Charity Commission. This requirement to obtain consent is set out in S198 (c) of the Charities Act 2011.
- However, in this particular case, the trust's Articles of Association prohibit the chair of the board of trustees being an employee and also receiving payment for carrying out the role of chair. Therefore, the trust was in breach of its articles.
- The trust was also in breach of its Articles of Association as more than 50% of the board had received benefit from their trust. The trust's Articles of Association specifically prohibit this.
- The trust had not complied with the Academies Financial Handbook, for example it had not reported a fraud to EFA; no adequate system of internal control was in place; and a separate audit committee had not been established.
- The trust did not have an appropriate internal control framework.
- Family members of trustees and senior employees were employed without due process.
- Breaches of the trust's own policies were identified (for example its expenses policy).
- The trust was not able to demonstrate openness and transparency in accordance with the Nolan standards of public life.
- The trust was unable to demonstrate that it is obtaining value for money.
- The trust had incurred expenditure which EFA found to be irregular.

## Subsequent action:

Following EFA's review the trust's chair resigned.

The significant weaknesses in financial management and governance identified in the review were reported to the trust in March 2014 with the report and findings subsequently published by EFA. Although the trust was able to demonstrate that it had begun to make progress on some of the concerns raised by April 2014, significant issues were still to be addressed resulting in the issuing of a Financial Notice to Improve. This resulted in all of the delegated authorities identified in the Academies Financial Handbook being revoked and all transactions by the trust of this nature (regardless of size) requiring prior EFA approval.

## Current Position:

- The trust has provided monthly updates to EFA on actions taken to address the weaknesses identified.
- The trust has been revisited in August 2014 to evidence progress against the recommendations in the Financial Management and Governance report and the requirements of the Financial Notice to Improve.
- The visit confirmed that significant and substantial progress had been made in addressing the recommendations, and in some instances the trust had gone beyond the requirements set out in the report.
- Whilst strong progress has been made, there are outstanding items which require completion prior to the lifting of the Financial Notice to Improve. It is anticipated that these actions will be completed in the next two months.

## Beneficial related party transactions

29. After consulting with the sector (via the sector representatives on the [Academies Finance and Assurance Steering Group](#)), it is evident that trusts both value and benefit significantly from the relationships they have with related parties.

30. Academy trusts have provided numerous examples of how such relationships can be beneficial to trusts (on a financial, operational and/or governance level), to the local community, the quality of education delivered and thereafter educational outcomes for pupils.

31. The two detailed case studies below show ways in which related party transactions can be beneficial. Annex B provides additional more concise illustrations of the potential benefits of a number of such transactions.

## Case study 2 – Beneficial related party transactions at an ‘Outstanding’ primary academy trust

**Context of the relationship** – the trust's executive head, executive deputy head and chair of governors are also directors of a registered, not for profit, childcare charity. The academy is a two form entry primary, and the charity runs childcare provision for five day nurseries, eight out-of-school clubs and a child-minder agency. The executive head, executive deputy and principal finance officer are also directors of a new primary teaching school which specialises in early years training. The three organisations work closely together, share many similar strategic goals and a co-focus on the education and care of young children.

**Benefits of the relationship** – the trust identified a number of benefits to the close relationship the organisations share and the resulting transactions:

**1. Sharing experienced staff to benefit from economies of scale:** part of the head, deputy, finance director, admin team, payroll and IT staffing costs are recharged to each of the three venues, calculated using actual hourly rates (including ‘on costs’) and the approximate time spent on each entity per month. This allows a primary academy to have a similar experienced support team as a larger secondary school. It also allows the senior teaching team to spend more time out of class to observe performances of teachers throughout the school to ensure outstanding practice. This is how the academy maintains its Ofsted ‘Outstanding’ rating. The members of staff and related parties made no personal profit as a result of these arrangements with any surplus being reinvested back into the charity.

**2. Gaining access to children at a younger age to ensure they are ready for school:** the senior team members within the charity and school work closely together and highlight any children who may be at risk (in terms of safety, behaviour or general development) and work with these children and the relevant outside agencies early to ensure they have the best possible start in life and they are ready to enter the world of education when they join primary school. The teaching school will be concentrating on development (both in terms of recruiting, training and continuous professional development) of early years teachers and other early years practitioners.

**3. Greater community cohesion:** the trust provides its pupils and its partner schools with pre-school wrap around and full out-of-school care provision, it aids parents to return to work safe in the knowledge that their children are safe and well cared for (all the charity venues are either Ofsted outstanding, for the more established venues, or good working towards outstanding for the newer venues). The trust is able to establish relationships with the parents of the children within the nursery before they progress to the academy.

**4. Wider economies of scale and additional income:** materials, teaching resources, I.T equipment can be purchased at a better price when negotiating with suppliers due to

the size of the organisations combined. The academy also benefits from rental income of its hall for the onsite out-of-school club.

### **Case study 3 – Beneficial related party transactions at an ‘Outstanding’ secondary academy trust**

**Context of the relationship** – a knowledgeable and experienced deputy head retired after a long service record. Rather than lose the individual’s experience and expertise the trust asked them to remain as a school governor.

Independently from the appointment, the trust was seeking to undertake a one-off project but identified that it didn’t have the ‘in-house’ capacity to complete the work to the requisite standard and within the required timeframe. The trust investigated several options for resourcing the project (such as purchasing temporary cover for staff to release them to undertake the work or employ an external agency) which, when costed, proved to be prohibitively expensive.

The trust then approached the ex-deputy head and negotiated the individual to work as a consultant (at a much reduced rate than their previous deputy head role). Itemised invoices were submitted detailing time spent and work completed and the individual was paid on an hourly basis.

**Benefits of the relationship** – the trust identified a number of benefits to the relationship and the resulting transaction:

**1. Existing knowledge of the trust operations and its objectives:** the work undertaken required minimum supervision due to the individual’s existing extensive knowledge of the school and its values. This allowed for a minimum of ‘lead in’ time for the commencement of the project and therefore reduced overall costs.

**2. Established working relationships with the trust’s senior management team:** this negated the need to use resource (from both the project team and the trust’s senior management team) to build effective working relationships, therefore allowing the project to begin immediately. This ensured that the desired outcomes were delivered within the required timeframe.

**3. Known quality of outcomes:** the knowledge and experience of the related party allowed the work to be completed quickly and to an extremely high standard. This generated real ‘cash’ savings for the trust over the course of the project and subsequently led to additional income streams for the trust which can be reinvested in educational delivery.

## Managing procurement and potential conflicts of interest

32. From the review undertaken it is possible to highlight areas of best practice when transacting with related parties and attempting to manage potential conflicts of interest:

- **Declarations of an interest** – under company and charity law the directors of academy trusts have a duty to declare any personal interest in proposed transactions and avoid conflict of interest.
- The Academies Financial Handbook goes further by requiring trusts to maintain a register of interests which *‘must capture relevant business and pecuniary interests of members, trustees, local governors of academies within a multi-academy trust and senior employees’*.
- Trusts should also consider whether to include the interests of other individuals in the register of interests (for example other employees or relatives of close family members of individuals already on the register). If in doubt the best practice would be to include an interest in the register. Boards of trustees should keep their register of interests up-to-date through regular review.
- **Removal from the decision making process** – where a potential conflict of interest is identified, the individual concerned should remove themselves from the decision making process for the duration of the transaction. This will include, but is not limited to, the original decision to enter into a contract with the related party, periodic contract performance reviews and/or contract renegotiation/renewal.
- **Competitive procurement procedures followed** – the Academies Financial Handbook requires trusts to be able to demonstrate that funds have been applied to the purposes intended by Parliament, that they have achieved value for money and that a competitive tendering policy is in place and applied.
- Whilst trusts are responsible for establishing the detail of their own procurement procedures, they should formalise those procedures by gaining approval for them from the trust’s governing board, fully apply them to all related party transactions and ensure that an audit trail for compliance to their own financial regulations is maintained.
- During the reviews undertaken, the vast majority of trusts were able to demonstrate robust procurement procedures.
- **Decision making based on a value for money assessment** – the Academies Financial Handbook requires trusts to be able to demonstrate that *‘spending decisions represent value for money’* and for value for money to form part of an academy’s decision making process.

## Case study 4 - Managing procurement and potential conflicts of interest

**Context of the relationship** – the trust’s sponsor (a charitable foundation) provided the trust supply teachers, with a value of £93k in the year. The sponsor also provided training courses for staff for which no charge was made. This was a related party due to a number of joint trustees.

**Declarations of an interest** – all joint trustees declared the interest within their annual declaration of interest. In addition all trustees declared the interest at governing board meetings where the transactions were discussed.

**Removal from the decision making process** – the connected trustees all removed themselves from meetings when discussions and decisions were made in regards to the related party transactions. Ensuring that the decision making process was undertaken at arm’s length.

**Competitive procurement procedures followed** – three written quotes were obtained for the supply of the services. All transactions are on a non-profit basis and the procurement procedures undertaken followed the trust’s own financial regulations.

**Decision making based on a value for money assessment** – when assessing the bids submitted, the trust selected its preferred bidder based on the quoted cost and quality of staff available. This ensured that the trust obtained the best possible outputs for the least cost.

## Introduction of the ‘at cost’ policy

33. In November 2013 the Department for Education (DfE) introduced an ‘at cost’ policy for related party transactions. The policy requires related party transactions, as defined in the Academies Financial Handbook, to be at cost only, with no profit allowed. For the accounting period 2014/15, to reduce bureaucracy, a *de minimis* limit of £2,500 has been introduced, but transactions above that limit must still be ‘at cost’.

34. We are not aware of any other public sector organisations where arrangements are in place which limit related party transactions to being delivered ‘at cost’.

35. The ‘at cost’ arrangements came into effect on 7 November 2013 and therefore did not apply to the 2012/13 financial statements reported as part of this review. Compliance with this policy will not be tested until the 2013/14 financial statements are received. However where we have undertaken follow-up work and identified instances of non-compliance, these issues have been assessed with the trusts concerned.

36. The Department for Education has recognised that more could be done to help academy trusts to be clear about what is required and to ensure that academy trusts are sufficiently clear of the requirements placed upon them and the consequences of not meeting those obligations.

37. The package of measures to enhance awareness of and compliance with the policy on academy-related party transactions includes the following:

- EFA’s oversight regime has been strengthened to ensure more extensive compliance with the policy. Action has already taken place on this through the reporting requirements for related party transactions set out in the Academies Accounts Direction, with increased emphasis on trusts being able to indicate how they have managed the transactions (for example by describing the procurement process they have followed).
- EFA is continuing to stress the importance of the issue of related party transactions through guidance to external auditors to ensure that they prioritise it in their audits of trusts.
- EFA has promoted and communicated the current policy to academy trusts through revised guidance in the Academies Financial Handbook, online training and webinars and the information that new trusts receive with their academy order.
- EFA has published generic examples of acceptable and unacceptable transactions and a ‘statement of assurance’ template to help provide greater clarity to academy trusts. The template is at Annex C.
- The revised Academies Financial Handbook draws to the attention of trusts the relationship between related party transactions and the provisions relating to novel and/or contentious transactions and obligations on members and trustees not to derive personal gain from their positions.



- The Academies Financial Handbook makes it clear that EFA has the discretion to issue a Financial Notice to Improve to a trust which has breached the policy, and where they have done so, the trust may be prohibited from entering into future related party transactions without prior approval from EFA for the duration of the financial notice.
- EFA will consider when issuing a Financial Notice to Improve, for an issue other than breach of the policy on related party transactions, whether to require as part of the notice that the trust must seek EFA approval for related party transactions for the duration of the financial notice.

## **Publication of updated guidance**

38. The 2014 edition of the Academies Financial Handbook has sought to strengthen the safeguards against potential conflicts of interest by stipulating that trusts must maintain a register of interests for members, trustees, local governors and senior staff.

39. The handbook makes clear the obligations placed upon trustees through company law; that they must avoid conflicts of interest, not accept benefits from third parties and declare interests in proposed transactions. It highlights that these requirements are especially relevant when entering into transactions with connected parties.

40. The 2014 edition also requires trusts to publish on their websites relevant business and pecuniary interests of trustees and members to improve transparency. This additional requirement is aimed to further enhance transparency.

41. Throughout the Academies Financial Handbook great emphasis is placed on effective governance and oversight within academies. The handbook seeks to ensure the correct equilibrium between checks and balances upon the executive and trustees whilst permitting trusts the autonomy they need to deliver excellent education to their pupils and value for money to the taxpayer.

42. The guidance in the 2013/14 Academies Accounts Direction has also been updated in order to enhance the narrative of related party transaction disclosures. In particular, enhanced disclosure on the procurement procedures undertaken with regards to the related party transactions disclosed is sought.

## **How other tax-funded bodies manage related party transactions**

43. A review of the provisions relating to a range of publicly-funded bodies (including the NHS, local government, further education and higher education) has been undertaken.

44. This identified that whilst all of these bodies have clear rules for managing conflicts of interest, registering members/trustees interests, disclosure of related party transactions and where appropriate require adherence to charity law, none have an 'at cost' policy on related party transactions.

45. A comparison of policies and legal duties relating to related party transactions and the management of conflicts of interests for academies and other publicly funded bodies is at Annex D.

46. This demonstrates that the provisions already in place in respect of academies are more demanding than those in place for other tax-funded bodies.

## Conclusions

47. The analysis of the related party transactions disclosed in the 2012/13 financial statements confirms that the vast majority of related party transactions are established for sound business reasons and are properly managed and disclosed.
48. In the small number of cases where arrangements are not compliant with EFA's policy framework, there are sufficient checks and balances in place to ensure that they are identified and appropriate action is taken.
49. Given the small number of trusts at which issues have been identified we should not assume that all related party transactions in the sector are inherently questionable.
50. Academy trusts are granted more freedoms than local authority-maintained schools, but with these freedoms come additional responsibilities and accountability. Academy trusts already have stronger requirements placed on them than their local authority counterparts as they are required to produce annual financial statements which are independently audited. Trusts' auditors must also comment on the regularity of the expenditure incurred.
51. The introduction of the 'at cost' policy in November 2013, the publication of updated guidance and the package of measures set out in this report combine to further strengthen the framework within which trusts operate. Whilst making clear to trusts the requirements placed upon them and the consequences of not meeting those obligations.
52. This represents to trusts an unprecedented level of transparency, accountability and scrutiny, to parents, the public, EFA and to Parliament to balance those freedoms we all want to see drive innovation in education.

## **Annex A - Definitions of irregularity and impropriety**

### **Irregularity**

Irregular transactions are those that fail to meet the requirement to deal with all items of income and expenditure in accordance with legislation, the terms of the trust's funding agreement and the Academies Financial Handbook, and compliance with internal trust procedures. This includes spending public money for the purpose intended by Parliament.

### **Impropriety**

Improper transactions are those that fail to meet the requirement that expenditure and receipts must be dealt with in accordance with Parliament's intentions and the principles of parliamentary control. This covers standards of conduct, behaviour and corporate governance.

## Annex B: Examples of beneficial related party transactions

If managed properly the following transactions can be beneficial:

- **Diversification** – where trusts establish subsidiary companies, to manage services provided by a trust (for example to deliver school to school support, or to run nurseries or other trading activities such as cleaning or a sports facility that also benefits the wider community). These generate additional income, but in doing so trusts may need to recharge staffing, accommodation and other costs. Regularly, directors are common to both the academy trust and the subsidiary, hence this arrangement will often give rise to related party transactions.
- **Shared services** – for example, with local authorities and sponsors (that can offer facilities management services or catering) – these may offer reduced costs through economies of scale. However, we recognise the potential for lax procurement practices (e.g. lack of market testing) and conflicts of interest.
- **Shared accommodation** – may fall into the same bracket as shared services, perhaps more-so in relation to head office functions in MATs.
- **School improvement support** – this is sometimes offered by trusts where the head teacher may be a trustee at both of the institutions involved in the transaction. In most cases the financial transactions would be between the institutions involved and would be to cover the cost of supply cover for the member of staff providing support, this would be within the current rules as the transaction would be deemed to be ‘at cost’.
- **‘In house’ expertise** – where a trust is related to a recognised national lead in a given area, who is able to provide consultancy support (for example, school improvement support) ‘at cost’ and is selected by open and transparent procurement. Sufficient controls would be in place to manage any conflicts of interest. This may be an economic way for trusts to procure such services. The cost to the trust is likely to be less than procuring exclusively from the open market and/or the quality of the services provided will be high.
- **Diocesan education authorities** – may receive a voluntary contribution from academies if the diocese provides a service to the academy which is connected with securing a school’s religious nature and ethos.
- **Donations** – when a charity, sponsor or other philanthropist contributor is represented on a trust’s board (or has a connection to someone that does) and makes donations such as funds, equipment, accommodation. These donations

would be identified as related party transactions within the trust's financial statements.

## Annex C: Pro-forma statement of assurance

This form is for completion by an individual or organisation (the 'supplier'), defined in the [Academies Financial Handbook](#) (the 'handbook') as a 'connected party' to an academy trust. Individuals and organisations supplying goods or services to a connected trust must charge no more than cost (defined at the end of the form). This form will also help trusts comply with their funding agreement obligations

### Section 1: Supplier details

Name and address of supplier	
Company number (if applicable)	
Start date	
End date	
Estimate of commercial price, including profit	<i>A reasonable and fair estimate</i>
Connection with trust, e.g. trustee is also a director of the supplier of goods and services	<i>Explain the nature of the connection between the supplier and academy trust</i>
Value of goods or services to trust	<i>£ At cost without profit</i>
Does this value include direct costs and indirect costs only?	Yes / No
Nature of contract	<i>Such as building supplies or professional services</i>

### Section 2: Details of contract

Explanation of how the supplier is charging the academy trust
<i>This should include a sufficiently detailed explanation setting out that the supplier understands its direct and indirect costs in such a way to demonstrate to the academy trust that it is supplying goods and services at cost, without any element of profit.</i>
<i>[Please extend the rows below if the contract is longer than three years]</i>

	Direct costs	Indirect costs	Total
Year 1	£	£	£
Year 2	£	£	£
Year 3	£	£	£
Total	£	£	£

## Section 3: Supplier certification

Certification of supplier	
<p>I certify, on behalf of [<i>name of supplier</i>] that:</p> <ul style="list-style-type: none"> <li>• the goods and services detailed in this form will be supplied to the academy trust on the basis of direct cost plus indirect costs, with no element of profit;</li> <li>• we are supplying the goods and services on an open book basis and we will provide more information on request; and</li> <li>• we will make an adjustment in the following year if we identify a miscalculation on our direct or indirect costs, and supplied goods or services which included an element of profit.</li> </ul>	

Name and position	<i>Should be sufficiently senior to sign this declaration</i>
Date	
Signature	

## Section 4: Academy signoff

Certification of academy trust	
<p>In signing this document I am satisfied that:</p> <ul style="list-style-type: none"> <li>• the goods and services being supplied comply with the requirements on trading with connected parties as set out in the handbook, and represent value for money;</li> <li>• there is full compliance with the trust's scheme of delegation;</li> <li>• open and fair procurement and compliance with the trust's procurement procedures have taken place;</li> <li>• potential conflicts of interest within the academy trust have been robustly managed;</li> <li>• the trust's register of interest captures relevant business and pecuniary interests as set out in the handbook, and will be updated to reflect this contract (if not already);</li> <li>• the supplier understands that open book arrangements are in place and they will provide more information on request, if needed; and</li> <li>• both the trust's accounting officer and chair of board of trustees have agreed to trade with this connected supplier, and that the measures and safeguards listed above are in place.</li> </ul>	

Name and position (in academy trust)	<i>Person signing must be sufficiently senior within the academy trust</i>
Date	
Signature	



## Notes

**Direct costs** means the costs of any materials and labour used directly in producing the goods or services.

**Indirect costs** means a proportionate and reasonable share of fixed and variable overheads.

**At cost** means without profit as it includes direct and indirect costs only.

**Estimate** of commercial price acknowledges that the value of such contracts varies depending on a number of factors and negotiations. The supplier should identify a reasonable and fair price, e.g. from previous similar contract

An open document text version of this form is available alongside the published report.

## Annex D: Comparison of policies for publicly-funded bodies

The following table shows a comparison of policies on related party transactions for publicly-funded bodies.

Obligations or duties	Academy trust	NHS groups	Local authority	Higher education	Further education
Obligation to openly procure services	Yes	Yes	Yes	Yes	Yes
Obligation on decision makers to declare conflicts of interest	Yes	Yes	Yes	Yes	Yes
Obligation on decision makers to refrain from voting in matters where they have a conflict of interest	Yes	Yes	Yes	Yes	Yes
Charity law obligations	Yes	No	No	Yes	Yes
Company law obligations	Yes	No	No	Yes	Yes
Obligation to maintain a register of decision makers' interests	Yes	Yes	Yes	Yes	Yes
Statutory duty on chief finance officer to report irregular payments	No	No	Yes	No	No
Statutory duty to make arrangements for proper administration of financial affairs/ management of conflict of interests	No (although general charity and company law obligations relevant here)	Yes	Yes	No (although general charity and company law obligations relevant here)	No (although general charity and company law obligations relevant here)
Obligation to pay no more than cost for supplies received from related party	Yes	No	No	No	No



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