



POLICY ON RELATED PARTY TRANSACTIONS

Approved: September 2018

To be reviewed: As required

Background

In 2014, the Public Accounts Committee report relating to the DfE and the ESFA financial statements for the previous year (2012-13) suggested a need for an overall review of systems and procedures for financial accounting within the DfE and ESFA. In relation to connected party transactions (which are at their basic an extension of related party transactions), the report instructed both organisations to ensure that they extract and analyse complete information on transactions, and to use the analysis to determine risk-based interventions. As such, this can only happen where both agencies have complete information from schools/trusts.

KGA will consider related party transactions to reduce any potential risk of abuse and reputational damage, both to the Trust and to the wider sector. Points the Trust will consider before entering into any such transaction are:

- would it be deemed contentious by ESFA
- is it within market norms
- if details of the transaction were in the public domain would they be newsworthy?

Recent Developments

The Public Accounts Committee has recommended that Academy Trusts should seek ESFA approval for all related party transactions. Further guidance will be issued, and new regulations are likely to come into place from September 2018.

Key Risk Areas

Following ESFA's review of related parties (see Annex A for background), 3 key risk areas have been identified, and the Trust will be mindful of these risks when entering into agreements:

1. Procurement process
Some trusts had not followed proper procurement processes. KGA will follow its scheme of delegations when obtaining quotes (and taking heed of OJEU for large contracts). Where there is a conflict of interest, suitable safeguards will be established, for example the individual will be removed from the tendering and reviewing process and each tender will be robustly evaluated, and decisions made documented within minutes.



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2. Not observing 'at cost' requirements
'At cost' is explained in more detail below. KGA will ensure it has the correct procedures in place to help identify and mitigate the risk.
3. Off payroll arrangements
Non-compliance with HM Treasury's (HMT) tax requirements for senior employees being paid off payroll. HMT previously conducted a review into tax arrangements of public sector appointees and found that whilst there may be the odd time such arrangement is appropriate, for standard roles payments should be on-payroll, which also helps ensure that the individual is meeting their tax obligations. KGA will not pay senior employees off payroll.

At cost arrangements

The Academies Financial Handbook states that a Trust must pay no more than 'cost' for goods or services provided to it, including from individuals or organisations connected to the academy trust. The Trust will be mindful that that the definition for a connected party (discussed below) and part 3.2 of the Academies Financial Handbook 2015 or subsequent updates must be reviewed carefully. Where this extent of control or the connection is such that the need for 'at cost' is triggered, an individual or company can supply good and/or services up to £2,500, cumulatively, in any financial year which can include profit. Beyond £2,500, all transactions must be 'at cost' without profit. Where 'at cost' is triggered, a statement of assurance will be required from the supplier to support the arrangement, which the Accounting Officer will review to ensure that there are no issues with the transaction.

The Trust will also need to determine whether there is an element of profit for individuals providing services on a self-employed basis, by either:

- Taking other tenders for services. If the transaction with the connected party is cheaper this will help demonstrate less profit being made (a so called discount factor), due to market value rates; or
- Assessing the cost in respect of what the Trust would pay for that person if it were employing them.

The Trust will assess the reasonableness of the transaction, bearing in mind the de minimis limit and making sure that the reasons for the transaction and the individual are fully documented.

Auditors and Regularity

The Trust's auditors will check compliance with KGA's schemes of delegation and with the rules set out in the Academies Financial Handbook. Where 'at cost' transactions have occurred they will check whether there is a statement of assurance, and what work the Accounting Officer has undertaken to satisfy himself there is no element of profit. Section 9.4 of the Academies Accounts Direction explains a series of tests that will more than likely be undertaken (see checklist in Annex B).

If there are any issues with the transactions this will need to be noted firstly on the Accounting Officer's statement of 'regularity, propriety and compliance' and then within the auditors' regularity report

The role of the Academy Trust Accounting Officer



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Trust Accounting Officers in academies are ultimately accountable, via the EFA, to Parliament, 'for regularity, propriety, and value for money in the use of public funds' and this has been well documented in the ESFA Chief Executive's annual 'Dear Accounting Officer' letters.

The roles of directors and trustees

The Department for Education's Governors Handbook sets out the structure of governance in academy schools. An academy trust is a charitable company limited by guarantee. Within academies, there are members of the Trust, akin to stakeholders, as well as governors, who are directors and trustees of the charitable company/the Trust. Governors have duties as directors under company law, and trustees under charity law.

Managing conflicts of interest

The management of conflicts of interest is important in terms of statutory duties of directors, and maintaining confidence and trust in the academy in relation to the use of public funds and overall reputation. The Charity Commission provides useful advice in how to mitigate this issue.

KGA maintains and publishes a list of the pecuniary interests of its Trustees and Governors, to aid the identification of conflicts of interest.

In accordance with the Academy Accounts Direction, connected party transactions are disclosed in the Trust's financial statements, and if there have not been any such transactions this is also disclosed.



Annex A: Background to related party transactions

ESFA review of related party transactions

In November 2014, ESFA published its review of related-party transactions from over 2,200 academies for the period 2012-13. Over 43% (976) declared at least one related-party transaction (1350 RPTs took place within these academies).

The review document provides the following indications on what the EFA looked for when investigating the RPTs: 'Indicators of risk considered by ESFA 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.'

Examples the EFA found in its review

The RPTs in the review found to be potentially irregular/improper demonstrated the following issues:

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.

Where the EFA did subsequently identify irregular/improper¹ transactions in some of the cases, a Financial Notice to Improve (or FNTI) was issued.



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¹ ESFA definitions: 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.

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.

ESFA case studies: The ESFA review document also contains case studies relating to these Trusts, and it is worth reviewing these.



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What is a connected party?

The Academies Financial Handbook defines connected parties as:

- any member or trustee of the academy trust
- any individual or organisation connected to a member or trustee of the academy trust. For these purposes the following persons are connected to a member, or trustee:
 - a relative of the member or trustee
 - an individual or organisation carrying on business in partnership with the member, trustee or a relative of the member or trustee
 - a company in which a member or the relative of a member (taken separately or together), and/or a trustee or the relative of a trustee (taken separately or together), holds more than 20% of the share capital or is entitled to exercise more than 20% of the voting power at any general meeting of that company
 - an organisation which is controlled by a member or the relative of a member (acting separately or together), and/or a trustee or the relative of a trustee (acting separately or together). For these purposes an organisation is controlled by an individual or organisation if that individual or organisation is able to secure that the affairs of the body are conducted in accordance with the individual's or organisation's wishes
- any individual or organisation that is given the right under the trust's articles of association to appoint a member or trustee of the academy trust; or any body related to such individual or organisation
- any individual or organisation recognised by the Secretary of State as a sponsor of the academy trust; or anybody related to such individual or organisation

Who is a relative?

This is often a grey area, and confusion can arise as to how far relationships extend. Under FRS102 (appendix 1) close members of the family are defined as:

- that person's children and spouse or domestic partner
 - children of that person's spouse or domestic partner
 - dependents of that person or that person's spouse or domestic partner
- What about siblings and other members of the family? Well it would depend on the level of influence in the person's dealings, but again caution needs to be had where a transaction is entered into where there could be a potential conflict of interest, and how that would look in the public domain.



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Annex B: Tests undertaken to check compliance

These tests have been lifted from the Academies Accounts Direction; however you may find them a useful checklist

| Issue | Comments |
|---|----------|
| Declarations of business interests have been completed (for those in a position to influence the academy trust, including key staff) and published on the academy trust's website | |
| Contracts with connected parties have been procured following the academy trust's procurement and tendering process | |
| Where contracts are entered into or renewed on or after 7 November 2013 the academy trust has obtained statements of assurance (confirming no profit element was charged) and the academy trust has followed their internal processes in reviewing this | |
| The academy trust has requested, under the open book arrangement, a clear demonstration that the charges do not exceed the cost of supply | |
| Governors who provide consultancy services to the academy trust are not receiving a profit for their services and the correct procurement and tendering process is being followed | |
| No connected party gains from their position by receiving payments under terms that are preferential | |
| If employees are providing external consultancy that the income is being received into the academy trusts accounts if the work was performed within the academy trusts normal working hours | |
| Disclosures of the transactions are in accordance with the Accounts Direction | |



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Annex C: What to do to avoid issues

The following checklist may be used when considering connected party transactions, and reviewed at the very minimum annually:

Checklist: Academies should be ensuring that they know the following information:

| Issue | Comments |
|---|----------|
| Is there a connection between parties? | |
| The position of the connected party (or parties) and their capacity to control and influence decisions relating to the transaction(s), and the extent of the control (20% is the baseline to work from/ where 'at cost' is triggered) | |
| The value of the contract and when it started | |
| Are transactions for goods and services being procured properly according to statutory regulations? | |
| Other risk factors known by the trust | |



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Checklist: Dealing with and understanding conflicts of interest

| Issue | Comments |
|--|----------|
| Check Directors' statutory duties so complies with company law | |
| Ensure Trustees understand how to manage conflicts of interest underpins RPTs | |
| Understand a chair and AO with more influence can distort perception, and ensure the Trust is aware that transactions with a chair/AO will attract more scrutiny | |
| Keep an up to date register of interests | |
| Have an agreed and actively monitored policy on trading with connected parties | |
| Understand and document who completes the risk register | |
| Understand and use publishing protocols | |
| Annually update the register of interests | |
| Declare interests at each meeting | |
| Encourage culture of disclosure in interests of transparency | |
| Remove any affected individuals from tendering processes/discussions/decisions to avoid influence | |
| For transparency, publish the register of interests on the school/trust website/ have a full end of year disclosure | |
| Ensure strong VfM and transaction in the interests of the Trust, and have an Open book/statement of assurance in place | |
| Ensure full disclosure in audited financial statements (go beyond minimum with such transactions) | |
| Check the list of the school's top suppliers and review with Trustees and members | |