

Aurora Academies Trust

Post-audit Management Report

Year ended 31 August 2017



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Executive summary

PURPOSE OF THE EXTERNAL AUDIT

- Our work during the audit was performed with a view to expressing an opinion on the financial statements of Aurora Academies Trust (the Academy Trust for the year ended 31 August 2017 and to issue a regularity assurance opinion.
- Our audit work also included consideration of the internal controls relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control.
- The matters being reported are limited to those that were identified during the audit and that we conclude are of sufficient importance to merit being reported to those charged with governance.
- We appreciate that you will already be aware of some of the matters contained in this letter. However, in accordance with the Education and Skills Funding Agency (ESFA) requirements and International Standards on Auditing (UK and Ireland) (ISAs) we are communicating them to you formally.
- This report and its contents were submitted in draft form to David Baron (Finance Director) for comment prior to finalisation.

AUDIT PROGRESS

We are pleased to report the audit, from our perspective, ran smoothly and that the timetable for the overall completion of the audit has been met. We would like to take this opportunity to thank all those with whom we dealt during the audit for their assistance and co-operation, in particular David Baron, Jenny Harrison, Gaydree Wrigley, Imogen Skelley, Debbie Whitmore and Kym Lewis.

EXPECTED OPINIONS

Subject to the satisfactory receipt of the outstanding items and confirmations noted below, we intend to issue the following opinions:

Financial statements opinion:

Clean

We expect to express our judgement that the financial statements give a true and fair view and have been properly prepared in accordance with the Academies Accounts Direction 2016 to 2017 issued by the ESFA, Companies Act 2006 and that the information in the Directors' report is consistent with the financial statements. The format and structure of the audit report has been updated this year to accord with the latest technical guidance.

Regularity assurance opinion:

Clean

We intend to state that in the course of our work, nothing has come to our attention which suggests that in all material aspects the expenditure disbursed and income received during the year ended 31 August 2017 has not been applied to purposes intended by Parliament and the financial transactions do not conform to the authorities which govern them.

Key audit findings

ACCOUNTS FORMAT AND COMPLIANCE

The financial statements follow the principles and format prescribed by the ESFA in the Academies Accounts Direction 2016 to 2017 (the Accounts Direction). Compliance with the Accounts Direction also ensures that the requirements of Companies and Charities legislation are met.

There have been only a small number of changes introduced by the 2016/17 the Accounts Direction. The notable changes of relevance to the Academy Trust were as follows:

- A sensitivity analysis should be provided as part of the disclosures relating to the Local Government Pension Scheme setting out the impact of small changes to the actuarial assumptions on the overall pension liability.
- Where the Academy Trust makes a contribution towards the Apprenticeship Levy, the value of this contribution should be separately analysed within the staff costs note.
- Additional analysis is required of the assets and liabilities acquired upon a school joining a multi-academy trust from another trust including details of the value of the asset or liability previously reported by the transferring school and the impact of any fair value adjustments made to those values.

In all respects, the Academy Trust's annual report and financial statements have complied with the new requirements.

ACCOUNTING POLICIES, ESTIMATES, AND DISCLOSURES

Our work included a review of the adequacy of disclosures included in the financial statements and consideration of the appropriateness of the accounting policies and estimation techniques adopted by the Academy Trust. We believe that the disclosed accounting policies, significant accounting estimates and the overall disclosure and presentation to be appropriate for the Academy Trust and in compliance with the Accounts Direction. We have no further comment to make in this regard.

AUDIT ADJUSTMENTS AND UNADJUSTED MISSTATEMENTS

Under Auditing Standards, we are required to provide you with details of any adjustments identified during the course of our audit work which have been made to the figures presented to us for audit.

Audit adjustments

Details of the adjustments which have been made to the figures presented to us for audit are provided at Appendix 1. These have all been discussed and agreed with David Baron. We will obtain written representations from you, as Directors, that you concur with these adjustments.

Unadjusted misstatements

There were no unadjusted audit differences.

AUDIT OBSERVATIONS AND RECOMMENDATIONS

We are pleased to report that we found no significant deficiencies in the accounting and internal control systems during our audit.

The table below summarises the details of any observations made concerning weaknesses in the Academy Trust's accounting and internal control systems. Observations included in the "A" grade (red) banding indicate that, in our opinion, immediate action is required. Conversely, observations included in the "C" grade (yellow) banding indicates that the matter, although important, does not warrant urgent attention.

Priority	No of points	Relating to
A Grade	None	<ul style="list-style-type: none"> n/a
B Grade	1	<ul style="list-style-type: none"> Review of payroll
C Grade	3	<ul style="list-style-type: none"> Signing of an employment contract Starter forms* Leaver forms

AUDIT OBSERVATIONS AND RECOMMENDATIONS (continued)

Items marked with an asterisk are observations which were also made and reported in our post-audit report to you last year, but which remain unresolved.

We are, however, pleased to report that the following observations made last year have been satisfactorily dealt with:

Priority	Relating to
A Grade	<ul style="list-style-type: none"> Authorisation of purchase invoices
B Grade	<ul style="list-style-type: none"> Authorisation of petty cash Review of journals Credit card expenditure
C Grade	<ul style="list-style-type: none"> Review of bank reconciliations

KEY AUDIT RISKS AND OUTCOMES

As part of our pre-audit planning process, we identified those areas where we believe there is a higher possibility that a material error may appear in the financial statements. In the pages which follow we have provided a brief summary of the outcome of our audit work in relation to those higher risk areas.

KEY AUDIT RISKS AND OUTCOMES (CONTINUED)

Risk area	Summary and conclusion
Revenue recognition	<p>There is an inherent risk in all organisations in relation to revenue recognition, i.e. that income may be accounted for in the wrong period.</p> <p>We carried out detailed analytical review against expectations based on our understanding of the Academy Trust and against the prior year. Reasonable explanations were obtained from management and significant variances identified which were substantiated as appropriate. No significant issues arose during our sample based checks including on our work on ESFA and non-ESFA income.</p>
Regularity	<p>Regularity and the use of government funding continues to be a substantial focus of the ESFA and National Audit Office. Ensuring regularity within the Academy Trust is the responsibility of the Board and all of the current focus on regularity in the academy sector has only increased the level of responsibility for the Board to monitor and document management of risk including risk of irregularity.</p> <p>The regularity self-assessment was provided for audit, which was completed by the Academy Trust's finance team and reviewed by the Accounting Officer. The regularity self-assessment confirms the processes in place to ensure regularity, propriety and compliance within the Academy Trust. In particular, the self-assessment confirms that:</p> <ul style="list-style-type: none"> • Procedures are in place in connection with general procurement, use of credit cards and expenses; • Procedures are in place in order to ensure appropriate remuneration of payroll staff, agency staff and consultants; and • Procedures are in place to ensure that conflicts of interest and related party transactions are identified and disclosed in the financial statements where appropriate. <p>The Academy Trust has not informed us of any material control weakness or irregularity in these areas. Based on our review of the self-assessment questionnaire and the work undertaken to verify the responses provided, we are satisfied that the conclusion reached in our regularity assurance report is appropriate.</p>

KEY AUDIT RISKS AND OUTCOMES (CONTINUED)

Risk area	Summary and conclusion
Related party transactions	<p>In all organisations, there is an inherent risk that transactions with related parties could be undertaken on terms that benefit those who control the entity at the expense of other stakeholders or the entity itself. For this reason, UK Accounting Standards and the ESFA Academies Accounts Direction requires transparent disclosure of all transactions and balances arising between the Academy Trust and its related parties. In addition, the ESFA Academies Handbook places restrictions on the permissibility of certain related party transactions.</p> <p>The Academy Trust's procedures for identifying related parties and associated transactions were reviewed. This includes the requirement for each of the Directors and member of the Academy Trust Senior Management Team to update their declaration of interests annually, and to declare any interests they have at the commencement of business meetings. Based on the work undertaken, we have no concerns over the completeness of related party transaction disclosures. We will obtain written representations from you also, asking the Board and management to confirm their satisfaction with the completeness of the disclosures made.</p>
Business Combinations – acquisition of the Gatwick School	<p>As part of its conversion from a Local Authority maintained school to an Academy Trust certain assets and liabilities previously held by the Local Authority have been transferred to the newly incorporated legal entity, including the freehold property used by the Academy Trust, any budget surplus previously accumulated, and deficit in the Local Government Pension Scheme.</p> <p>We have considered the accounting entries and disclosures made in relation to the net assets transferred including substantiating the value attributed to the assets and liabilities acquired and any fair value adjustments made by the Academy Trust post-acquisition. These were found to be appropriate and we have no material concerns in this regard.</p>
Capital project	<p>During the year, the Academy Trust commenced a major project to develop the Gatwick School. Given the significant financial value attached to the project, it is important that the costs are correctly capitalised or expensed as appropriate.</p> <p>We have reviewed the amounts expended in relation to the capital project and sample checked the expenditure to gain assurance over the accounting treatment. The amounts sample checked were considered capital in nature and the treatment was deemed appropriate. We also reviewed the repairs and maintenance expenditure for the year to identify potential costs expended on the project which may have been incorrectly written off. This review did not reveal any additional costs which should have been capitalised. We also reviewed cut-off, i.e. the financial period in which the expenditure has been recognised, and the disclosures made surrounding the year end capital commitment.</p>

KEY AUDIT RISKS AND OUTCOMES (CONTINUED)

Risk area	Summary and conclusion
Management override of controls	<p>There is an inherent risk in all organisations that management may be in a position to override controls or agreed protocol. Such actions may be taken in order to conceal or process unauthorised or inappropriate transactions, or may occur due to weaknesses in the control environment. Such actions could lead to either deliberate or inadvertent misstatement of the results portrayed by the financial statements.</p> <p>Journal entries were reviewed, particularly those surrounding the year end and explanations were sought for any large or unusual items. All items tested and discussed with management were deemed to be appropriate. No suspense accounts were noted as being used during the year.</p>
Accounting estimates	<p>Certain accounting entries within the financial statements are made on the basis of an estimate and changes in the underlying assumptions could lead to a shift in the reported results. The most material estimates within the Academy Trust's financial statements include the estimate of the useful economic life of tangible fixed assets (and hence the depreciation charges) and the estimation of the pension liability made by the actuaries in respect to the Local Government Pension Scheme.</p> <p>As noted earlier in this report, we are satisfied with the estimation techniques utilised. Testing of depreciation was satisfactory with all items tested being depreciated in accordance at an appropriate rate. The year-end liability in respect of the Local Government Pension Scheme is consistent with the estimate provided by the scheme's actuary and the assumptions used appear reasonable.</p>

Financial performance and position

AUDITED RESULTS

Based on the audited financial statements, the Academy Trust's total reserves increased by an amount of £12,675,000 (in 2016 there was a decrease of: £1,766,000) during the year providing net assets of £30,930,000 at the balance sheet date (2016: £18,255,000).

Excluding movements on tangible fixed assets, the defined benefit pension liability, and other non-recurring items, the Academy Trust's "operational" deficit for the year was £44,000 (in 2016 there was a deficit of: £2,000), as reconciled below.

	£'000
Overall net movement in funds	12,675
Less: movement attributable to the tangible fixed assets fund (note 1)	(3,212)
Less: income from Gatwick acquisition	(8,230)
Add: LGPS actuarial gain (note 3)	(1,711)
Add: LGPS service cost adjustment (note 3)	367
Add: LGPS interest cost adjustment (note 3)	67
Operational deficit for the year	(44)

AUDITED RESULTS (continued)

Note 1 Movement on tangible fixed assets fund

Movements on the tangible fixed assets fund broadly mirrors the movements on the Academy Trust's tangible fixed assets, reflecting the utilisation of funding towards the purchase of tangible fixed assets and the annual depreciation charge against the Academy Trust's assets.

Note 2 Other non-recurring income for the year

The surplus inherited on the Gatwick School joining the Trust has been excluded from the operational deficit as this is a one-off income item this year.

Note 3 LGPS (Local Government Pension Scheme adjustments)

The Academy Trust is one of several employing bodies included within the West and East Sussex Pension Fund. The scheme's actuaries, Hymans Robertson, have prepared a valuation of the assets and liabilities which are specific to Aurora Academies Trust so that the net liability may be included on the balance sheet. For the purposes of determining the "operational" surplus, the non-cash adjustments necessary in accounting for the change in the liability since 1 September 2016 have been excluded.

COMPARISON OF KEY FINANCIAL RATIOS

For your information, we have included at Appendix 3 to this report a comparison of the Academy Trust's key financial ratios for 2014, 2015, 2016 and 2017 and also against the sector averages for 2014, 2015 and 2016.

Other information

LETTER OF REPRESENTATIONS

We take this opportunity to enclose a final draft of the letter of representations which we will ask management and the Directors to sign at the same time as the approval and signature of the annual report and financial statements.

INTEGRITY, OBJECTIVITY AND INDEPENDENCE

In accordance with our profession's ethical guidance and further to the External Audit Strategy document issued to you as part of the pre-audit planning process, we confirm that there are no further matters to bring to your attention in relation to our integrity, objectivity and independence as auditors.

OTHER WORK UNDERTAKEN AS PART OF THE 2016/17 AUDIT CYCLE

As set out in our External Audit Strategy to you we have also been engaged to provide you with the following services:

- **Teachers' Pension End of Year Certificate (EOYC) assurance**
We can confirm that we have concluded our work on this area. Our assurance report was issued to Teachers' Pensions along with the final End of Year Certificate. Our work did not raise any significant concerns which need to be drawn to your attention.

OTHER WORK UNDERTAKEN AS PART OF THE 2016/17 AUDIT CYCLE (continued)

- **ESFA Accounts Return assurance**
Our work on the Accounts Return assurance will begin in early December. We do not have any concerns at this stage and we will work with management to ensure that the Accounts Return together with our assurance report is filed ahead of the 19 January deadline.

USE OF THIS REPORT

This report has been prepared for the Academy Trust's private use only. It has been prepared on the understanding that it will not be shared to any third party, other than the ESFA, or quoted or referred to, without our prior written consent and we can therefore assume no responsibility to any other party.



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Appendix 1: Audit adjustments and unadjusted misstatements

AUDIT ADJUSTMENTS		Statement of financial activities		Balance sheet	
Description		Debit	Credit	Debit	Credit
1	DR Deferred income CR Prepayments <i>Being the removal of intercompany balances within deferred income on consolidation</i>			13,650	13,650
2	DR Cash CR Creditors <i>Being a cancelled cheque within Oakwood to be included in creditors</i>			4,850	4,850
3	DR LA other funding (Oakwood) DR Other nursery income (Heron Park) DR Other nursery income (Glenleigh) CR LA nursery income <i>Being the presentational adjustment to move the Nursery Health Improvement Grant to Other Government Grants from other areas of income to ensure the same treatment across all schools</i>	5,000 5,000 5,000	15,000		

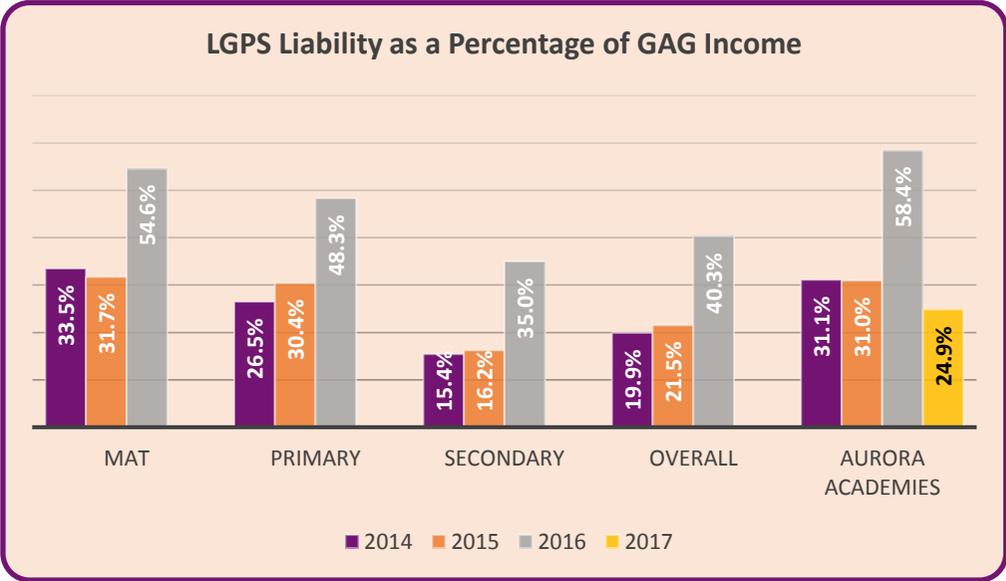
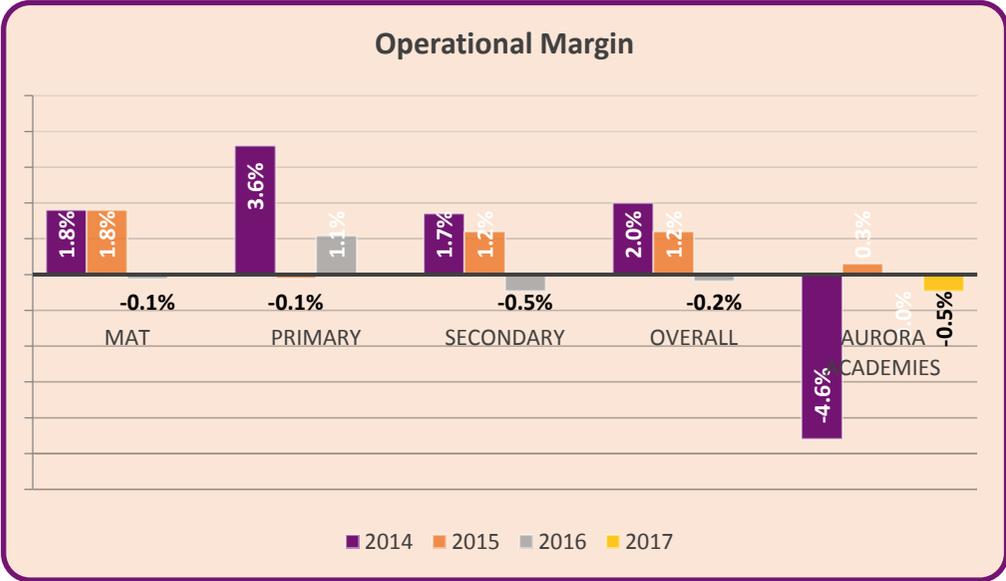
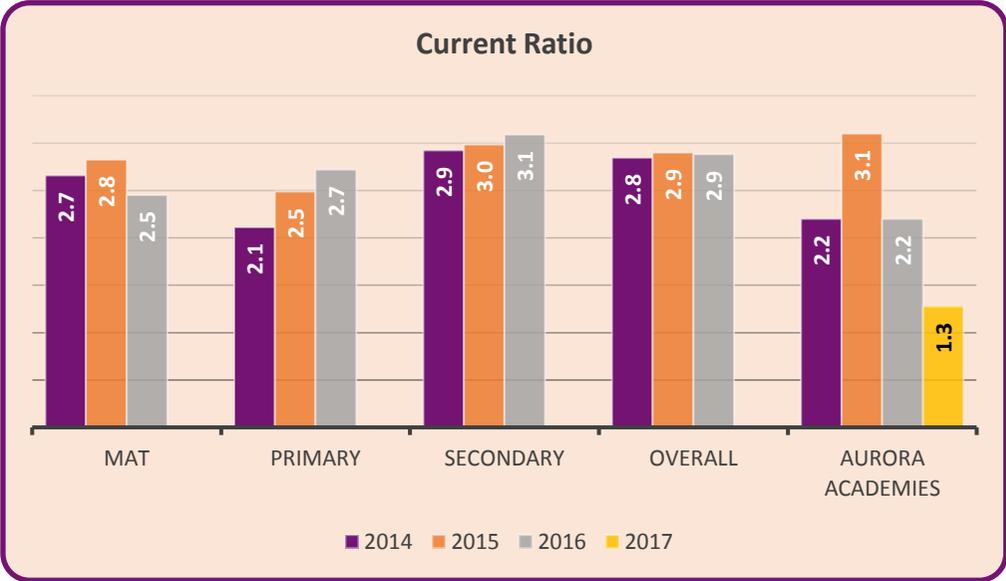
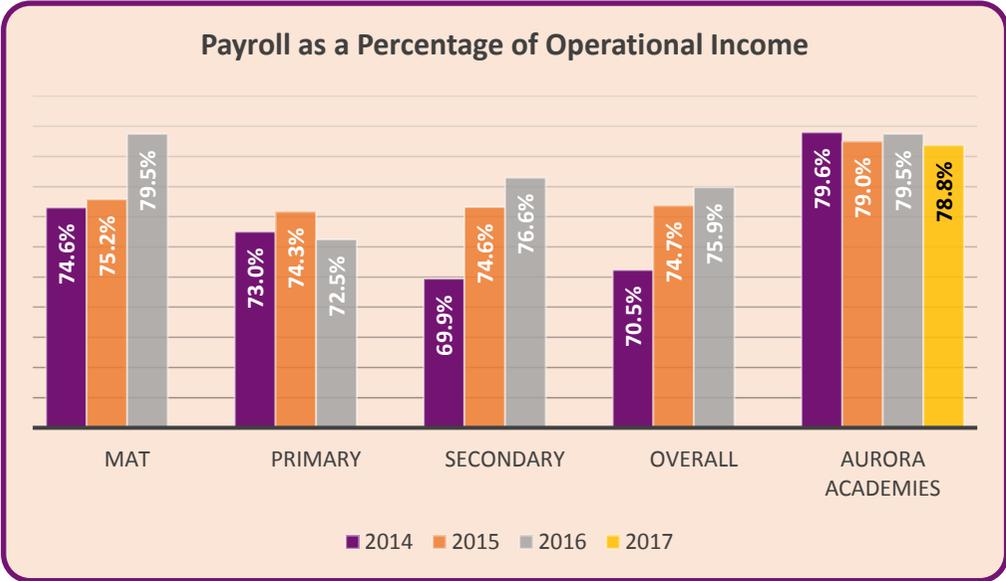
The above adjustments have a nil impact on the Academy Trust's overall reserve balances.

Appendix 2: Audit observations and recommendations

	Observation	Implication	Recommendation	Management comment
B	<p>Review of payroll</p> <p>During our review of payroll of central office staff, we noted that all of the payroll summaries prepared by Capita were not evidenced as reviewed by the Trust Financial Director in accordance with the Academy Trust's financial procedures.</p>	<p>If the review has not taken place, this increases the risk of the Academy Trust making incorrect payments to individuals, be this inadvertent or deliberate. If a review has taken place, then the lack of a clear audit trail makes it difficult to hold the appropriate individuals to account.</p> <p>Given that the Trust Financial Director is remunerated through the central office payroll, the policy for the Financial Director to authorise their own payroll may not be appropriate.</p>	<p>We recommend that the monthly payroll summary be reviewed by a responsible staff member outside of finance and signed as evidence of this review ahead of making a payment.</p>	<p>The monthly payrolls for the central office will be evidenced as reviewed and approved by the CEO as well as the Financial Director.</p>
C	<p>Employment contract – Heron Park Primary</p> <p>During our sample testing on staff costs, one of the two members of staff sampled at Heron Park did not have their employment contract signed.</p>	<p>If employment contracts are not signed, this increases the risk of the Academy Trust should any employment disputes occur regarding that member of staff.</p>	<p>We recommend that all employment contracts are signed by both the employee and the Head of School as evidence of employment.</p>	<p>The contract in question was a fixed term additional contract for an existing member of staff and the contract was signed by the Headteacher but not the employee. However, we agree that all contracts of employment need to be signed as agreed by the employee as well and will work with the school to ensure that this does not re-occur.</p>

	Observation	Implication	Recommendation	Management comment
C	<p>Starter forms</p> <p>As with last year, it was noted during our salaries testing that no new starter forms were used at HPA. Information is entered on the accounting software based on the advertised position. Capita then generate the contract from this information.</p> <p>It was also noted that the new starter forms were not authorised at KPA.</p>	<p>There is a risk that the information being entered into the accounting system is incorrect leading to errors to the employment contracts and incorrect payments processed through payroll.</p>	<p>We would recommend that new starter forms are implemented at HPA and that starter forms are appropriately authorised.</p>	<p>We have now implemented New Starter, Contract change and Contract Termination forms for use across all Trust schools.</p>
C	<p>Leaver forms</p> <p>We noted that there was no leaver form for individuals at TGS.</p>	<p>There is a risk that incomplete HR files could lead to error when processing pay data.</p>	<p>We recommend that leaver forms are implemented at TGS and that all personnel files are reviewed to ensure they contain relevant up to date documents.</p>	<p>We have now implemented New Starter, Contract change and Contract Termination forms for use across all Trust schools.</p>

Appendix 3: Comparison of financial ratios



INTRODUCTION

The above charts present some key financial ratios for the Academy Trust for the past four financial periods. We have also provided corresponding ratios* for the sector for 2014, 2015 and 2016. The ratios presented may differ from your own ratios where a slightly different formula is used.

**Figures taken from approximately 100 academies based in the South East of England and Greater London. Although the sector average figures provide a guide to how the Academy Trust compares to the sector, there is a substantial amount of diversity across the sector depending on the individual circumstances of each academy.*

PAYROLL AS A PERCENTAGE OF INCOME

Formula: Total payroll (including defined benefit pension scheme adjustment, excluding agency and severance payments) ÷ Total income (excluding capital grants, conversion balances, sponsorship and start up grants)

Staff costs represent the most significant area of expenditure for all academies and are viewed by third parties as a critical indicator of financial and operational efficiency. Despite holding teacher pay rises to 1%, staff on-cost increases in National Insurance and pensions have driven up total costs.

Typically, staff costs make up 65% - 80% of both total costs and total income. The higher the percentage, the lower the amount of resources that are available for spending in other areas, e.g. curriculum expenses, improving facilities and saving for major projects, which may impact over the longer term on sustainable school improvement.

PAYROLL AS A PERCENTAGE OF INCOME (continued)

This ratio has been increasing over the past three years and the average of 79.5% shown here is at the very top of the range. Whilst the overall average has increased by 1.2%, MAT costs are rising more steeply at 3.9% whilst Primaries managed to reduce their ratio in 2015/16.

Academies are under pressure to reduce staff costs or find alternative sources of income. Being aware of organisational capacity and having detailed workforce analysis will be essential. Adopting a model of pupil contact time in evaluating efficiency of curriculum planning has been shown to be effective.

CURRENT RATIO

Formula: Total current assets ÷ Total current liabilities

The current ratio is a measure of an academy's solvency. It compares the amount of cash and other assets with the level of current liabilities. A higher ratio will provide a greater margin of security to an academy in meeting liabilities as they fall due. However, a very high ratio may mean funds are being set aside unnecessarily rather than being used to further the work of the academy.

As expected the majority of academies and MATs are maintaining a healthy current ratio figure. Whilst there is no exact definition of a "healthy" current ratio, a figure ranging between 1.5-3.5 suggests that an academy is maintaining adequate assets to cover its liabilities that arise in the next 12 months. This is particularly important given that academies are prohibited from borrowing money.

OPERATIONAL MARGIN

Formula: Surplus (deficit) for the year before transfers excluding fixed asset fund and amounts donated on conversion ÷ Total income excluding fixed asset fund and amounts donated on conversion.

This ratio compares an academy's net surplus or deficit for the year to its total income. Unlike commercial organisations, the aim of an academy is not to generate profits on trading or capital gains but to provide quality education and fully utilise its resources in so doing.

The graph shows a significant decrease in the margin as a percentage of income from 2014 to 2016 with 2016 deficits averaging 0.2%. This trend is reflective of the difficult economic conditions in which academies are operating. Interestingly, the Primary academies in the data set have shown an improvement from a very poor previous year.

Of our sample, 47% of academies were in operational surplus compared to 64% the previous year. The general challenges in the sector would explain this but it is important to remember that specific, sometimes planned, circumstances can affect individual academies in each year. This ratio is taken before transfers to the fixed assets fund. Therefore, many academy trusts are actually drawing on their revenue reserves to a greater extent than is shown here.

LGPS LIABILITY AS A PERCENTAGE OF GAG INCOME

Formula: Pension liability ÷ GAG income

This ratio demonstrates the scale of the LGPS liability. As the pension liability is determined by independent actuaries and is the product of many factors, including the state of the wider economy and the workplace profile for individual academies, the ratio is largely outside the academy's influence. A high ratio may indicate that the drain on annual contributions will be difficult for the school to manage.

LGPS LIABILITY AS A PERCENTAGE OF GAG INCOME (continued)

The startling increase in the average academy LGPS liability as a percentage of GAG income from 21.5% in 2015 to 40.3% in 2016 was primarily as a result of changing actuarial assumptions including the extent to which the actuaries were discounting the value of the obligations to pay out pensions in the future.

As slight changes in the actuarial assumptions used can have a substantial impact on the overall net pension liability, we have provided in the table below a comparison of the Academy Trust's 2017 LGPS retirement benefit assumptions against those of other educational organisations.

	Sector Average %	Aurora Academies Trust %
Assumptions		
Price increases	2.5	2.4
Salary increases	3.4	2.95
Pension increases	2.5	2.4
Discount rate	2.5	2.5
Decrease in LGPS liability from 01/09/16 to 31/08/17	18	42
Value of LGPS liability at 31 August 2017 (£000s)	N/a	1,716
LGPS liability as a percentage of GAG income	35.8	24.9

The level of Teacher's Pension contributions from their revision date in April 2019 is not yet known. It is likely that these will also rise significantly and future planning should take account of this.