Key Audit Issues Memorandum

Light Hall School

For the year ended 31 August 2018

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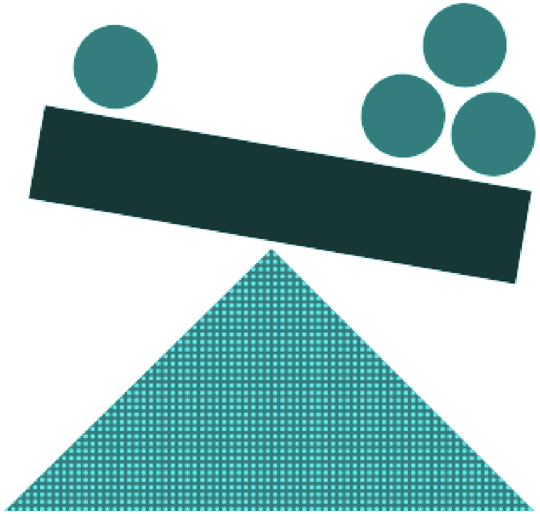

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The purpose of this memorandum is to highlight the key issues arising from the audit of Light Hall School and the preparation of the financial statements for the period ended 31 August 2018. It is also used to report to those charged with governance to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We take responsibility for this memorandum, which has been prepared on the basis of the limitations set out in 'Terms and Conditions Limitations' (Section 8).

We would like to take this opportunity to record our appreciation for the kind assistance provided by the staff of Light Hall School during our audit.

UHY Hacker Young (Birmingham) LLP

Contents

1. Audit Scope, Objectives and Strategy

1.1 Engagement objectives

Our engagement objectives are as follows:

- to carry out a statutory audit of the financial statements of Light Hall School in accordance with International Standards on Auditing (UK and Ireland), with the aim of forming an opinion whether:
    - the financial statements give a true and fair view of the state of the academy trust's affairs as at 31 August 2018 and of the academy trust's result for the year then ended;
    - the financial statements have been properly prepared in accordance with FRS 102;
    - the financial statements have been prepared in accordance with the requirements of the Companies Act 2006, and the Annual Academies Accounts Direction issued by the Education and Skills Funding Agency; and
    - the information given in the Trustees' Report for the financial year is consistent with the financial statements.

to produce a concise and constructive report of key issues (our Key Audit Issues Memorandum) to Light Hall School; and

- to draw to your attention to any material weaknesses in internal control that come to our attention during our audit work.

1.2 Risk-based audit

We carried out a risk-based audit approach used throughout the audit to efficiently and effectively focus the nature, timing and extent of audit procedures to those areas that have the most potential for causing material misstatement(s) in the financial reports.

The risk-based approach required us as auditors to first understand the entity and its environment in order to identify risks that may result in material misstatement in the financial reports. We performed an assessment of those risks at both the financial report and assertion levels. The assessment involved considering a number of factors such as the nature of the risks, relevant internal controls and the required level of audit evidence.

1.3 Risk-based limited assurance engagement

In addition to our audit opinion we are also required to perform a limited scope assurance engagement, reporting both to you and to the Education and Skills Funding Agency (ESFA), considering whether the expenditure disbursed and the income received by the trust during the period 1 September 2017 to 31 August 2018 has been applied to the purposes identified by Parliament and that the financial transactions undertaken by the trust conform to the authorities which govern them. This latter point is concerned with looking at compliance with the requirements of the various frameworks that apply to trust, including your memorandum and articles, your funding agreements, the Academies Financial Handbook extant for the relevant period, the Accounts Direction 2017 to 2018, the Charities Act 2011 and the Companies Act 2006.

1. Audit Scope, Objectives and Strategy (Continued)

Our approach was once again risk-based. We began by developing our understanding of the trust's own approach to ensuring the proper application of funds received and to ensuring compliance with relevant legal and contractual frameworks. We developed an understanding of the trust's governance arrangements and internal control procedures, planning our work accordingly to allow us to gain sufficient evidence to give the required limited assurance opinion. Our assurance procedures included reviewing and commenting on the Accounting Officer's Statement on Regularity, Propriety and Compliance, and the trustees' report and governance statement.

1.4 Materiality

An item would be considered material to the financial statements if, through its omission or non-disclosure, the financial statements would no longer show a true and fair view.

Materiality is set at the outset of planning to ensure that an appropriate level of audit work is planned. It is then used throughout the audit process in order to assess the impact of any item on the financial statements. These are assessed individually and in aggregate, discussed with you and, if you do not adjust, signed off by you in your letter of representation to us, confirming your view that they are immaterial to the financial statements.

An item of low value may be judged material by its nature, for example any item that affects the disclosure of directors' emoluments. An item of higher value may be judged not material if it does not distort the truth and fairness of the financial statements.

The final level of materiality was £66k based on 1% of total income.

1.5 Internal controls

Auditing standards require that we evaluate the design effectiveness of internal controls over the financial reporting process to identify areas of weakness that could lead to material misstatement. Therefore, we will focus our control review on the high-risk areas of the financial statements.

We are also required to assess whether the controls have been implemented as intended. We will do this through a combination of inquiry and observation procedures, and, where appropriate, systems walkthroughs. However, our work cannot be relied upon necessarily to identify defalcations or other irregularities, or to include all possible improvements on internal control that a more extensive control review exercise might identify.

1. Audit Scope, Objectives and Strategy (Continued)

1.6 Significant Risks

As part of our audit procedures we are required to consider the significant risks that require special audit attention. Auditing Standards require us to consider:

- Whether there is a risk of fraud;
- Whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
- The complexity of transactions;
- Whether the risk involves significant transactions with related parties;
- The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and
- Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.

2. Audit Opinion and Regularity Conclusion

2.1 Audit Opinion

In our opinion the financial statements:

- Give a true and fair view of the state of the Academy Trust's affairs as at 31 August 2018 and of its incoming resource and application of resources including its income and expenditure for the year ended;
- Have been properly prepared in accordance with the FRS 102;
- Have been prepared in accordance with the requirements of the Companies Act 2006 and the Annual Accounts Direction 2017 to 2018 issues by the Education and Skills Funding Agency (ESFA).

2.2 Assurance Report on Regularity

During the course of our work, nothing has come to our attention that suggests that in all material respects the expenditure disbursed and income received during the period 1 September 2017 to 31 August 2018 has not been applied to purposes intended by Parliament and the financial transactions do not conform to the authorities which govern them.

3. Issues Identified During the External Audit

We are required to report to you, in writing, significant deficiencies in internal control that we have identified during the audit. These matters are limited to those which we have concluded are of sufficient importance to merit being reported to you. As the purpose of the audit is for us to express an opinion on the trust's financial statements, you will appreciate that our audit cannot necessarily be expected to disclose all matters that may be of interest to you and, as a result, the matters reported may not be the only ones which exist.

As part of our work, we considered internal control relevant to the preparation of the financial statements such that we were able to design appropriate audit procedures. This work was not for the purpose of expressing an opinion on the effectiveness of internal control.

We confirm that we have not identified any significant deficiencies in internal control during the audit.

We confirm that we have identified some areas where minor improvements could be made in section 3 of this report.

We are also required to communicate other significant audit findings such as:

- where we consider a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate in the particular circumstances of the entity;
- significant difficulties, if any, encountered during the audit; or
- other matters, if any, arising from the audit that, in our professional judgement, are significant to the oversight of the financial reporting process are communicated to those charged with governance.

We confirm that we have nothing to report to you in any of the above three areas.

3. Issues Identified During the External Audit (Continued)

Ref	Issue	Recommendation	Academy Response	Timescale for Action	Risk / Severity
3.1	There are no independent checks of changes to bank sort codes for BACs payments made by the Academy. Changing bank sort codes to transfer payments to a non-supplier organisation and then reverting back to the original details, is the most frequent type of fraud transaction. It is noted that there is no evidence of these transactions taking place at Light Hall School.	**It is recommended** that an audit report produced from Corero identifying changes to supplier accounts details, are reviewed by an individual without access to the finance system. The details should be referred periodically to the Audit Committee and retained for audit purposes.	Accepted. Corero will be asked to provide details of how this Audit Report can be obtained from the system. The report will be reviewed by an individual without access to the finance system and referred periodically to the Strategy & Finance Committee.	December 2018	Low
3.2	The reserves policy states that the level of available reserves should be the equivalent to 1 week's expenditure, i.e. approximately £100k. With reserves at just 1 week's expenditure, this leaves little contingency to deal with unforeseen issues. It is noted that Light Hall School currently holds free reserves of £453k.	**It is recommended** that the reserves policy is adjusted for the level of free reserves held to be at least 4 weeks' expenditure, to reflect the need to adequately meet unforeseen issues.	Accepted. Reserves Policy will be reviewed and amended for Governors' approval.	January 2019	Low

3. Issues Identified During the External Audit (Continued)

Ref	Issue	Recommendation	Academy Response	Timescale for Action	Risk / Severity
3.3	During the audit it was identified that land had previously been depreciated over the 125-year lease (£54k per annum). FRS 102 states that land should not be depreciated as it is considered to have an indefinite useful life. The most recent re-valuation of land and buildings was in February 2012.	**It is recommended** that an ESFA desktop valuation is obtained to ensure the value of land and buildings is recorded at 'fair' value within the financial statements.	Accepted. ESFA desktop valuation will be obtained to ensure the value of land and buildings is recorded at 'fair' value within the financial statements.	January 2019	Low
3.4	There are a significant number of "scam" invoices being issued to all organisations, including examples of VAT being charged inappropriately. VAT numbers are currently not checked to an independent source for verification.	**It is recommended** that a sample of invoices, particularly with those using a PO address, are investigated by using VIES which verifies the VAT code as being correct. https://europa.eu/youreurope/business/taxation/vat/check-vat-number-vies/index_en.htm	Accepted. VIES website will be used to verify VAT codes are correct.	January 2019	Low

In our Audit Service Plan, management override, related party transactions, revenue recognition and regularity of income and expenditure were identified as risks of error in the financial statements. Our audit procedures have not identified any areas of concern in respect of these.

4. Independence

4.1 Independence

We confirm that:

- there are no changes in our assessment of independence;
- we complied with the Auditing Practices Board's Ethical Standards for and in our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.
- we are not aware of any relationships that may affect the independence and objectivity of the firm that we are required by auditing and ethical standards to report to you.
- we consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so.
- we have met the reporting requirements to the Audit Committee, as 'those charged with governance' under International Standards on Auditing (UK and Ireland) 260 – Communication with those charged with governance.

5. Corrected Audit Misstatements

A list of journals for the corrected audit misstatements has been provided to management separately on 15 November 2018.

6. Uncorrected Audit Misstatements

We are required to bring to your attention audit adjustments that the trustees are required to consider. A schedule of such adjustments is included below. We understand that management consider these identified misstatements to be immaterial in the context of the financial statements taken as a whole, and have asked you to confirm this in written representations. We concur with this judgement, and believe that the effects of the uncorrected misstatements are immaterial to the financial statements taken as a whole. Final materiality is £66k based on 1% of total incoming resources.

A review of after date invoices identified 6 additional items where the costs should have been included within the 2017/18 financial statements totalling £2,303.

Light Hall School has only transferred IT capital equipment from revenue finance ledger codes to capital at the end of the financial year. This has resulted in no depreciation being calculated for the months in between the purchase and the financial year end, which totals £3,696.

The adjustment for the above 2 highlighted points would be as follows and the impact would be to reduce the net income of £261k recorded in the audited financial statements by £7k to £254k:

	Dr (£)	Cr (£)
SOFA	2,302.73	
Balance Sheet – Accruals		2,302.73
Journal to accrue additional invoices identified.		
SOFA	3,696.36	
Balance Sheet – Tangible Fixed Assets		3,696.36
Journal to post additional depreciation identified.		

7. Emerging and Topical Issues for Academies

New related party rules from 1 April 2019

The new Academies Financial Handbook (AFH) introduces some key changes in respect of related party transactions. Whilst the remainder of the AFH is effective from 1 September 2018, the related party rules come in later to give trusts time to adapt.

From 1 April 2019 trusts will be required to report all transactions with related parties in advance of the transaction taking place, via the ESFA's online form. Since this is a 'must' requirement.

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

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

Management accounts

The AFH effective from 1 September 2018 introduces some specific detail in respect of the preparation of management information, and how often this is shared with trustees.

Management accounts must now be prepared every month and shared with the Chair of Trustees. They must also be shared with other trustees at least six times a year.

Additionally, there is a requirement to select and use key financial performance indicators and measure performance against them regularly.

National Funding Formula (NFF)

The DfE announced in July that the transition period will be extended to include 2020-2021, thereby delaying full implementation of the hard funding formula by another year.

It is obviously important for all trustees to fully understand the impact of this delay on their longer-term budgets. The timing of the Government announcement was unfortunate since it arrived just as many trusts were finalising and submitting their Budget Forecast Returns which included 3 years' worth of figures for the first time on 2018.

Figures for 2020-21 will need to be revisited and we recommend that boards of trustees ensure they know how the delay to the hard implementation of the NFF will impact their trusts. New forecasts for 2020-21 should be presented to boards during the first term of 2018-19 so that any strategic decisions that may depend on the finances in that year can be re-assessed.

Frequency of board meetings

The new 2018 AFH introduces a specific requirement for full boards to meet at least three times a year. This should not be a problem as virtually all boards will meet at least this regularly.

However, the rules extend to suggesting that board should be meeting at least six times per financial year. Whilst it will be permitted for boards to meet less than six times, from 2018/19 the financial statements will need to include disclosures to explain how the board 'maintains effective oversight' with fewer meetings.

Executive pay

The ESFA are focusing on executive pay in the sector and have written to trusts paying over £150k to their CEO and to trusts employing 2 or more individuals on salaries of over £100k.

They are attempting to strengthen expectations about the processes that trusts adopt for setting executive pay.

All trusts should ensure that they have clear records justifying executive pay for their senior leadership teams, and for the very highest levels of remuneration in particular. Trusts that received the ESFA letters were required to respond and explain their reasons, and we understand that the ESFA were not content with the answers they received in the majority of cases.

TPS Employer rate update

Some academies have received an email indicating that the rate will increase from the current 16.4% to over 23% from September 2019 (rather than from April 2019), but that the additional costs will be funded until March 2020.

Apprenticeship levy

Trusts with an annual pay bill in excess of £3 million have been paying this levy since April 2017. A reminder that funds collected and the government 10% top expire if not used within 24 months of being credited to your employer's account.

7. Emerging and Topical Issues for Academies (Cont'd)

Integrated Curriculum Financial Planning (ICFP)

ICFP is the new 'buzz' phrase for the sector. Many expanding MATs are finding that they need to commit to ICFP to gain access to development grant funding, but the process is useful for all academies.

ICFP is a data-driven approach to planning a school's staffing structure, which involves making decisions that are informed by key data/metrics and benchmarking against schools in similar circumstances.

ICFP models look at target v actual class sizes across year groups, the contact ratio for different levels of staff and average salary costs.

GDPR

All trusts by now should be well on the way to ensuring compliance with the GDPR which came into force on 25 May 2018.

Your appointed Data Protection Officer should have sufficient time to undertake this role, and should receive regular training. The importance of the role cannot be underestimated and should be treated as of similar stature to the Designated Safeguarding Lead.

The DPO should regularly report to the highest levels of management and governance.

Disclosure of payment practices

Only larger academy trusts will be caught because of the size criteria within the legislation. Any companies will be within the scope of the requirement for a financial year if, on their last two balance sheet dates, they exceeded two or all of the thresholds for qualifying as a medium-sized company under the Companies Act 2006. Currently these thresholds are:

Over £36 million annual turnover (incoming resources);
Over £18 million balance sheet total (aggregate of the amounts shown as fixed assets and current assets in the balance sheet)
Over 250 employees.

For MATs responsible for several academies bullet point 2 is easily breached due to the value of the school land & buildings, along with bullet point 3.

The legislation has been introduced to combat late payments issues which thousands of businesses across the country have to deal with. Smaller businesses often find themselves at the mercy of larger organisations who are able to withhold payments, or agree lengthy payment terms, because of the importance of their custom to the supplier. This can cause businesses administrative and financial problems, where ultimately the adverse impact on cashflow can put businesses at risk.

For those trusts affected, it will be necessary to publish the required information within 30 days of the end of the mid-year and year-end reporting date i.e. the report for the six months to 28 February will be due by 30 March 2019, and the next report will need to be published by 30 September 2019.

Making Tax Digital (MTD)

Academy trusts which are formally registered for VAT will need to comply with MTD from 1 April 2019. MTD is a significant change in taxation and affects the way businesses transfer data to HMRC. This affects all VAT registered businesses (unless they are registered voluntarily).

In theory all software providers need to ensure that their systems are capable of meeting the MTD requirements before the deadline. Many leading software companies have been working with HMRC over the past few years, however it is notably that the HMRC list currently excludes much of the software used by academies. Trusts affected should talk to their software companies now to ensure they will be compliant by 1 April 2019.

Any multi-academy trusts affected and which have different software in use across the trust will be particularly affected.

Trusts using the s33 reclaim mechanism will not need to comply with the MTD rules.

Gender pay gap reporting

New requirements were introduced from 6 April 2017 for all companies with more than 250 employees, and many academy trusts are caught by these changes. Many trusts would have been exempt initially by virtue of their size, but as MATs expand as academes join them more will find themselves affected by these requirements.

Once caught this is an annual requirement, and so trusts will have to publish their gender pay gap statistics on their websites by April 2019; if affected you should be working with your payroll provider now to ensure you can meet your obligations.

8. Terms and Conditions Limitations

The matters raised in this report are only those which came to our attention during our external audit work and are not necessarily a comprehensive statement of all the weaknesses that exist, or of all the improvements that may be required. Whilst every care has been taken to ensure that the information provided in this report is as accurate as possible, based on the information provided and documentation reviewed, no complete guarantee or warranty can be given with regard to the advice and information contained herein. Our work does not provide absolute assurance that material errors, loss or fraud do not exist.

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