

REPORT OF THE COMPTROLLER AND AUDITOR GENERAL TO THE HOUSE OF COMMONS

This is the first year in which the Department for Education (the Department) has produced Academy Sector Accounts which consolidate the results of the 3,013 academy trusts that were open during the year ended 31 August 2016. Previously, the results of academy trusts were consolidated into the Department's own group accounts. This was very challenging for the Department as academy trusts have a financial year-end (31 August) that does not match that of the Departmental group (31 March). From 2013-14 to 2015-16, I issued adverse opinions on the truth and fairness of the Departmental group's financial statements as I had identified a level of misstatement and uncertainty that I considered to be material and pervasive. I recommended that the Department and HM Treasury work together to identify a solution to the causes of my qualification.

In response to my recommendation, the Department developed proposals to remove the academy trusts' financial results from the Departmental group's financial statements, which would reflect only grants paid to academies. The Department would then prepare a separate aggregated account for academies as at 31 August. These proposals were reviewed and approved on behalf of Parliament by the Education Select Committee, Liaison Committee, Alignment Review Committee and Scrutiny Unit, and have been implemented in this financial year. My findings from the audit work conducted following the introduction of the 2015-16 Academy Sector Accounts are set out below:

The Department has significantly improved the timeliness and quality of its financial reporting. The introduction of the Academy Sector Accounts enabled the Department to publish its group accounts in July 2017. This was several months earlier than in previous years. The removal of the academy trusts' financial results allowed me to issue an unqualified audit opinion on the group financial statements.

The Department has made good progress in addressing issues relating to accounting for land and buildings but significant weaknesses remain which have led me to qualify my audit opinion on the Academy Sector Accounts. From 2012-13 to 2015-16, I limited the scope of my audit opinion in respect of the value of land and buildings held by academy trusts that was recognised in the Departmental group accounts and I continue to do so for the 2015/16 Academy Sector Accounts. Academy trust land and buildings with a valuation of £45 billion have been recognised as at 31 August 2016

The Department has capitalised all land and buildings used by academy trusts within the consolidated statement of financial position, which may not comply with the requirements of the relevant financial reporting framework. Academy trusts prepare their accounts in accordance with *Accounting and Reporting by Charities: Statement on Recommended Practice* (the Charities SORP). The Academy Sector Accounts are prepared in accordance with the Government Financial Reporting Manual (FReM), which has different requirements on asset valuation from the Charities SORP. Rather than consolidating the balances recognised by academy trusts in their own accounts, the Department has therefore made a central adjustment for land and buildings, assuming that all land and buildings used by academy trusts should be capitalised. This may not comply with the requirements set out in the FReM, for example where buildings are occupied on a short term lease or are owned by another entity, such as Church bodies. The Department does not have robust evidence to demonstrate that its assumption is appropriate.

The Department is unable to provide me with sufficient, appropriate evidence that the carrying value of the academy trust land and buildings it has recognised is a materially accurate reflection of the fair value of the underlying estate. In my report on the 2015-16 Departmental group accounts, I noted a number of weaknesses in the Department's approach to valuing its land and building assets. The Department has made good progress in addressing these issues for the 2015/16 Academy Sector Accounts. It has reviewed its valuation methodology and strengthened its controls over its professional valuation

process. However, significant weaknesses remain, particularly around the Department's processes to ensure that the asset valuations included in the accounts reflect the current condition of the sector's estate. As I reported in my February 2017 report *Capital funding for schools*, the Department's first property data survey estimated that in total it would cost an estimated £6.7 billion to return all school buildings across both the academy and maintained sectors to satisfactory or better condition. The survey was completed in 2014 and covered 85% of the school estate. In 2016, the Department commissioned a second property data survey. The first results are expected to be available at the end of 2017.

Further improvements are needed if the Department is to achieve an unqualified audit opinion on future accounts, as well as to maximise the usefulness of the Academy Sector accounts for Parliament and other stakeholders. The introduction of the Academy Sector Accounts has allowed the Department to publish information on the academic performance of academies in the same document as the sector's financial position for the first time. Further improving the timeliness and accuracy of the accounts will support more effective Parliamentary scrutiny of how taxpayer's money has been spent and what has been achieved. The Department can also make greater use of the data it collects to prepare the Academy Sector Accounts to inform its oversight of academies and to help academies improve their financial management. This is particularly important given the current financial challenges facing schools, and the issues the Department faces in identifying and addressing the risk of financial failures in schools, that I reported on in my report of December 2016 *Financial sustainability of schools*.

Recommendations

The Department has made significant progress in addressing the sources of error and uncertainty that I noted in my report on the 2015-16 Departmental group accounts and has plans in place for further improvements in the future. To continue this progress, the Department should:

- a. Gather evidence to support its recognition of land and building assets in the Academy Sector Accounts. To address this, the Department is collecting information from academy trusts on the basis on which they occupy the land and buildings that they use, such as freehold, leasehold or licences. The Department then plans to use this information to inform its decision on which land and buildings should be recognised in the Academy Sector Accounts.
- b. Continue to make improvements to its processes for valuing the land and buildings that it recognises in the Academy Sector Accounts. In particular, it needs to provide evidence that the valuations included in the accounts reflect the current condition of the sector's estate.
- c. Build on the improvements it has made to its accounts production process to enable it to publish Academy Sector Accounts for future years on a more timely basis, working towards its commitment of producing them before the Parliamentary summer recess.
- d. Work with HM Treasury to finalise their proposals on how the results of academy trusts will be incorporated into the 2016-17 Whole of Government Accounts, which has a year-end of 31 March.
- e. Continue its efforts to minimise the reporting burden for academy trusts by streamlining the accounts production process and further enhancing its engagement with the sector.
- f. Consider how it can ensure that it is deriving maximum value from the data it collects to produce the Academy Sector Accounts to support its oversight of academies, as well as to provide information to academies that could help them to improve their financial management.
- g. Consider whether there is additional information that could be included in future Academy Sector Annual Report and Accounts, such as trends in financial performance, which could be of use to Parliament in holding the sector to account.

Sir Amyas C E Morse
Comptroller and Auditor General

Dated 24th October 2017