

acie

**association
of charity
independent
examiners**

Consultation Paper on the Charity Accounting Regulations from the Scottish Executive, April 2005

Response from the Association of Charity Independent Examiners (ACIE)

1 Introduction

- 1.1 ACIE recognises the need to revise the regulations for charity accounting in Scotland as outlined under Option 1 ('doing nothing is not an option') on page 34 of the Consultation, and welcomes and supports the five key principles outlined in the Background section (page 9).
- 1.2 ACIE is the UK-wide organisation for people who carry out the Independent Examination of charity accounts, offering support, advice, training and the possibility of a professional qualification. It has 500 members, including 24 in Scotland and others with direct experience of working with Scottish charities. Whilst numerically small, these members include some well known and well respected Scottish charity advisors. ACIE's Convenor for Scotland, as well as being a member of the ACIE Council, is a member of the ICAS Council and the ICAS Charity Working Party. She is a general practitioner partner in a medium sized independent Glasgow firm with a large number of charity clients and she also trains in the charity sector. Further information about ACIE is given at Appendix 1.

2 Summary of main issues

- 2.1 ACIE has 6 key issues arising from this Consultation:
- 1 the level of the threshold for Receipts and Payments accounts (see section 3 below)
 - 2 the impact of the proposals on UK-wide charities (section 4)
 - 3 the proposed imposition of requirements over and above those of SORP and possibly in contradiction to SORP in some instances (section 10) and therefore
 - 4 the choice of Option 3 (as per letter from the Scottish Executive of 31 May 2005) in the RIA (see section 11 below)
 - 5 the training implications of the proposals (section 11.3.2)
 - 6 the lack of any reference to the duties of Independent Examiners (section 12.5)
- 2.2 ACIE has also commented below on all sections of the Consultation Paper, in the order that the topics were presented.

3 Thresholds

- 3.1 We understand that the proposals about thresholds are an attempt to keep the regime 'simple and consistent' (page 13). However, in attempting to do this, we feel that another principle - proportionality - has been sacrificed, especially in respect of the threshold for Receipts and Payments (R&P) accounts.
- 3.2 We agree that the current Scottish threshold of £25k is too low; but would disagree with the statement that, 'a charity as small as £250,000 ... will rarely have transactions of a complexity that would make receipts and payments accounts misleading' (page 13).
- 3.3 On the whole, charities at £250K are not small and simple. They will quite often have, for example, multiple funders (possibly on various reporting years) and a number of staff, with consequent employment responsibilities and liabilities, both of which would suggest the need for accruals accounting rather than R&P.
- 3.4 We therefore disagree with the idea that £250K is the proportionate threshold for R&P accounting. Moreover, the consultation document seems to overlook the fact that, even when charities are doing accruals accounting under the SORP, the SORP itself includes many useful simplifications for charities below the audit threshold. In England and Wales, most charities with incomes between £100K and £500K will be able to take advantage of these provisions, and we would argue that Scottish charities should have the same opportunity.
- 3.5 We thus believe that the threshold for accruals accounting and adhering to the SORP should be £100K, but recognising that such charities will automatically have a relaxation from some of the more complex SORP requirements. This is a sensible compromise position.
- 3.6 The threshold for R&P accounting is set in England and Wales at £100K, and there is no proposal to alter this in the current debate. This may seem - especially in the light of the next section - simply about lining everything up with what already happens in England and Wales. This is not our argument however: it is about thresholds that are genuinely proportionate to the size and complexity of the relevant charities and not losing this in the pursuit of simplicity. It is about both sound internal financial management for charities that have complex responsibilities and liabilities, and public confidence that the accounting requirements placed on such charities are sophisticated enough to reflect this complexity.

4 UK Charities

- 4.1 There are three issues here:
- 1 the need for a single set of thresholds across the UK (and the lack of any justification for any variation, other than possible transitional arrangements);
 - 2 the need for reporting requirements to be standardised and shared across the two/three UK regulators;
 - 3 the training consequences of variable requirements for UK-wide charities.

4.2 ACIE produced the following table in response to a recent consultation on the introduction of charity regulation in Northern Ireland:

	England & Wales	Charities Bill proposals (E&W)	Scotland - current	Scotland - proposals	Northern Ireland proposals
R&P option	up to £100K	as is	up to £25K	up to £250K	up to £25K
IE bracket	£10K to £250K (optional under £10K)	£10K to £500K (optional under £10K)	0 to £100K	0 to £250K	0 to £100K
Audit threshold	£250K	£500K	£100K	£250K	£100K

4.3 As can be seen, there is the possibility of ending up with three sets of thresholds across the UK. ACIE has no evidence that charities in Scotland are so different in their funding and financial management from those of E&W (or Northern Ireland, come to that), that there is a justification for these different thresholds. And in particular, there is no justification for the imposition of extra workloads and costs on charities which work across the UK, especially when all the regulators say they are looking to minimise regulation wherever it can be done appropriately.

4.4 Two further points about thresholds:

- 1 In its submission on this issue in respect of the Charities and Trustee Investment (Scotland) Bill, ACIE recognised the need for Scottish charities perhaps to move in stages towards alignment with the E&W audit threshold of £500K, and therefore supported this threshold being set at £250K for a stated interim period;
- 2 Our comments on the requirement for IE for charities under £10K can be found at 12.3 below.

4.5 With regard to the reporting and regulatory requirements,

- 1 It is fairly obvious that it would make things much easier for UK-wide charities if they do not have to produce two, or even three, sets of accounts or, more likely, opt for the highest common denominator, which is also therefore likely to be the most time-consuming and expensive.
- 2 In terms of the current proposals, the group of charities who would be most obviously affected by this in respect of thresholds, would be those in the £250K to £500K bracket, who are about to be eligible for IE in E&W but would have to continue with audit in Scotland.
- 3 With regard to the differences in the nature of the reporting (as opposed to the issue of thresholds), see section 10 below.

- 4 The option to present Scotland-only accounts will only be practicable to a certain percentage of UK-wide charities and, again, will entail extra work, in both establishing and maintaining separate accounts.
- 5 With regard to reporting to the charity regulators, we would ask for consideration to be given to either a) common paperwork or b) the use of a lead regulator (dependent on the registered address of the charity?) which confirms a charity's compliance with the other regulator(s).

4.6 One of the very practical consequences for UK-wide charities of having different thresholds and reporting regimes is the need to train key members of the charity and its advisors in two sets of requirements - and for separate guidance and training materials to have to be issued by OSCR and the Charity Commission (again, potentially compounded further by the Northern Ireland variation) - which amounts to a duplication of effort and resources which could be better used in the pursuit of both the charities' and regulators' primary activities.

4.7 Finally, in this section, it can be assumed that UK-wide charities are large entities and should therefore have the capacity to deal with any extra reporting that arises from differences between the regulatory systems in different parts of the UK. However, using ACIE as an example, our total income in 2004 was £58K+ and we have 1.6 full-time equivalent staff. We would therefore appreciate anything that rationalises the regulatory demands placed upon us.

5 Exemptions

5.1 The proposal for Registered Social Landlords (RSL) and Higher and Further Educational Institutions to report accordingly to their own specialist SORP's, with OSCR having discretion to grant variations as necessary, seems pragmatic to us.

6 Designated Religious Charities

6.1 We welcome the introduction of DRC's into the regulatory framework for charity finance and think that it will improve accountability and transparency.

7 Charitable Companies

7.1 We agree - if it is legally possible - with moving the audit threshold for charitable companies in line with other charities in Scotland, ie, at £250K. However, see also our preference at 4.4.1 above for this threshold to be a transitional one on the way to common thresholds across the UK.

7.2 Similarly, we welcome the option of IE for charitable companies under £250K. However, see also our comments on IE for charities - and therefore for charitable companies - under £10K (12.3 below); and the training consequences of this proposal (at 11.3.2.3 below).

8 Accounting Periods

- 8.1 These proposals, both in terms of a) a charity wishing to change its accounting period and b) the period for submitting the Annual Report and Accounts to OSCR, seem sensible to us. We assume that the proposed actions by OSCR for the failure to submit Annual Report/Accounts will be used in proportion to the circumstances of the offending charity, eg, will be different for a small charity with a good track record of reporting which is 2 weeks late as opposed to a large charity which is six months late and about whose probity concerns have been raised.

9 Accounts in Gaelic

- 9.1 We agree that accounts should be produced in English, with a Gaelic version being optional. Our agreement is based on the principle of the accessibility of the accounts of all charities to the public and in acknowledgement that the percentage of Scottish people who are fluent enough to read accounts in Gaelic will be small.

10 The Charities SORP

- 10.1 In choosing Option 3, the proposals represent a form of overkill. We see no need to re-state SORP and would suggest that trying to do so in some ways devalues it and can cause confusion. The only places in which we would suggest there need to be extra requirements is:

- 1 in respect of R&P accounts, where SORP 2005 does not go into detail (although SORP 2000 does - at paragraph 354);
- 2 any area not covered by SORP, eg, Annual Reports.

- 10.2 However, given that R&P accounting is supposed to represent a proportionate approach for smaller charities, we find it strange that SOFA classifications - and related notes - are proposed requirements (page 31). Further, confusion is then introduced by offering the use of 'natural classification' but only in respect of staff and admin costs. If the SOFA approach is going to be required then it needs to be fully adhered to, but we would suggest that it is burdensome for (and even contrary to the concept of?) R&P accounts. Indeed, it is worth noting that SORP is applicable only to accounts that give a 'true and fair' view, which is not a claim that is made for R&P accounts.

See also our comments at 3 above about ACIE's preferred R&P threshold of £100K and our related preference for the application of the simplified SORP for the resulting accruals accounts in the £100K to £250K range.

- 10.3 In respect of the proposals for Trustees' Annual Reports, we would suggest that:

- 1 Point xii on page 23 should be covered in the notes to the accounts, and possibly xi as well, so does not need including in the TAR;
- 2 There is no reason for charities under £250K not to disclose their bank and Auditor/Examiner - and it is not onerous to do so, and there are possible advantages in terms of transparency in doing so (point xiii on page 23).

11 The Draft Regulatory Impact Assessment (RIA)

11.1 The revised preference for Option 3 on page 42 - see letter from the Scottish Executive of 31 May 2005 (which concurs with the preferred stated option on pg 17, although it was numbered 2 on that page) - seems a correct description of what the proposals are attempting to do, but as described at 10 above, not one we agree with. We see no need to re-state the SORP, other than in the specific cases named above, and then with greater clarity/consistency, and we are not convinced that there is 'specific Scottish consideration' to be taken into account in respect of charity finance (page 42).

11.2 It is also worth noting that the RIA as stated is based on one significant threshold that we don't agree with, ie, R&P accounts up to £250K.

11.3 Compliance costs

1 Audit costs as compared with the costs of IE

Any attempt at this comparison is always invidious, but here are some comments:

When we are asked at ACIE about how much an IE should cost, we give the example of a fairly straightforward charity of £200K pa and an average IE fee of £800. The audit fee for a similar charity is likely to be anything from £1,500 to £2,500.

This has to be wrapped round with all sorts of caveats, which, in the end, come down to who is doing the audit/IE and what they choose to charge. As mentioned in the Consultation Paper, IE can be done for free - but we would suggest this is at the smaller end of charities - and we have seen IE fees from £0 to several £1,000's ...

In principle, an IE should be cheaper than an audit, but there's no research to confirm this or to put figures on it - and there are always the exceptional cases.

NB: one of the other benefits of IE is that it allows charities a wider choice in who carries out their IE: they do not have to go to a firm of chartered accountants. It may also be that, in some instances, the work is undertaken more speedily by the non-chartered accountant who does not have to give priority to more profitable work.

2 Training costs

2.1 We would suggest that the training costs per charity are set too low. In particular, we are not convinced that however small their charity, half a day of personal study will equip a volunteer/Treasurer with the information and understanding they need. Indeed, it could be argued that it is exactly these people and charities that will need extra support, as no relevant professional training can be assumed.

2.2 There is also a huge gap in the proposals re training, which is the training of the auditors and Independent Examiners. Even if this body of people is up to date with current requirements (and not all of them are), at a minimum they will need to be brought up to date with the final regulations. Whilst some of

this may be absorbed as business costs (see below), in terms of IE in particular, where there should be encouragement of competent people from within the charity sector taking on this role on a voluntary or nominal-fee basis, consideration needs to be given as to how this need is going to be met and who will bear the cost.

- 2.3 Further, if IE for charitable companies under the audit threshold of £250K is going to be introduced, then there is a significant piece of training for Independent Examiners to be undertaken. Firstly, in that Examiners - in terms of their IE work - don't work with charitable companies at the moment. They may well need to learn about company accounting, therefore, to work with a charitable company.

Secondly, given that IE has not been applied to charitable companies so far, there will be a need to work out how IE does apply, and then to train accordingly.

3 Small businesses/Competition

We would suggest that the introduction of these regulations will not be without impact on the financial services element of the small business community and, depending on the use of 'competition' here, would not be neutral in that respect either.

12 Other comments

12.1 Assets threshold for dormant charities

There is mention of an asset threshold for dormant charities on page 13 of the Consultation Paper and again at page 32, where the starting threshold for the audit/IE of a dormant charity is proposed at £25K.

Whilst we very much welcome the explicit inclusion of requirements for dormant charities, we do not agree that they should have any different entry point for audit/IE than active charities. Presumably this proposal was based on a calculation of, say, £25K income in a dormant charity equates to interest on capital of £500K (at 5% interest). However, we would suggest that even capital sums of under £500K represent money given by the public at some point that should be properly accounted for.

We would suggest, therefore, that the entry threshold for the audit/IE of dormant charities is that same as that for active charities. If that threshold is finalised at £10K (see below at 12.3), then dormant charities with income below that threshold would still have to complete and file proper accounts. Further, the Charity Commission has the power to investigate any dormant charity in E&W which has had no expenditure on charitable purposes for several years and, presumably, OSCR will be given similar powers.

12.2 'Income' or 'income and expenditure'?

In the examples on page 13 of the Consultation Paper, 'income' and 'income and expenditure' appear to be used interchangeably. This may be simply a matter of oversight, but there needs to be clarity and consistency in which it is meant to be - presumably 'income only' in line with Scottish practice to date.

NB: in E&W, the current proposals move from thresholds defined by 'Income and Expenditure' to thresholds based on 'Income alone'.

12.3 Independent Examination for charities under £10K

One of the reasons for this group of charities not to have to have an Independent Examination in England and Wales is again one of proportionality. Taking the figures in Table 1 of the Consultation Paper:

- 1 There are potentially 13,500+ charities in this bracket
- 2 If most Independent Examiners working at the smaller end of charities works with 2 or 3 charities a year, then that is 4,500-6,000+ Examiners needed
- 3 And is OSCR going to check all these returns (and be properly staffed/resourced to do so)?
- 4 And even if all 13,500 charities are actually at the £10K limit (rather than dealing in lesser amounts) then their total income is still less than 2% of the total income of the charities in the top bracket in the Table, ie, those over £10m (again, assuming all those charities are at £10m, not above £10m)
- 5 So where do you use scarce resources if you want to a) minimise actual abuse of charity finance and b) reassure the public?

12.4 The use of the word 'audit' in governing documents/constitutions

This is presented in the Consultation Paper as a bar to IE, which technically it is. However, the Charity Commission certainly looks favourably on charities wanting to amend their governing documents to allow for IE, when appropriate, in particular if the governing document pre-dates the formal introduction of IE in 1992. Whilst this may not be directly relevant to the Regulations, it may be something that OSCR would also want to promote.

12.5 The duties of Independent Examiners

- 1 Given the 1992 Regulations will be replaced by the final version of these Regulations currently being consulted on, it is worrying that there is nothing in the proposals about the duties of an Independent Examiner. This needs addressing. Firstly, OSCR needs to be given powers to issue Directions for Independent Examiners.
- 2 Secondly, in the interest of consistency across the UK (again, where there is no apparent justification for diversity), it would make sense for OSCR and the Charity Commission (and NICC for Northern Ireland?) to work together to produce one set of Directions for the UK.

- 3 However, at the moment, although the definition of an Independent Examiner is the same in Scotland and E&W - in Scotland s/he gives a positive opinion; whilst in E&W a negative one. This needs resolving - again, in the interests of consistency for both UK-wide charities that are eligible for IE and for the training and performance of Examiners.

12.6 The qualifications of Independent Examiners

- 1 The current Charity Commission Directions re IE in E&W recommend certain qualifications for Examiners of accounts over £100K (formal accountancy qualifications or similar/equivalent gained in the charity sector), and this will be strengthened/mandatory for Examiners working with accounts over £250K under the provisions of the Charities Bill (but will still include a charity sector option - explicitly, and only, 'Fellow of ACIE').
- 2 In taking the IE option above £100K, Scotland may wish to consider a similar provision about appropriate qualifications, should it choose to establish stand-alone Directions (see 12.5 above). Appendix 2 shows the current CC guidance for charities over £100K choosing an Examiner; and the proposal for IE over £250K in the current Charities Bill (E&W).
- 3 Further, ACIE is named in the CC guidance as a source of further information and a source of Examiners for charities seeking such a person.

Appendix 1: Background information about ACIE

ACIE was set up in 1999 to be a professional body and a charity in its own right, seeking to promote the effectiveness of other charities through the support of independent examiners.

There are two levels of ACIE membership: Associate Members receive ACIE's support and advice but do not have any professional status. Full Members, who have to demonstrate substantial experience in charity accounting and the duties of independent examiners, are awarded the professional designation, currently 'MACIE'. There are different levels of Full Membership depending on the individual's experience and expertise, the highest of which is 'Fellow' - the category of Full Member who will be entitled to carry out IE over £250K assuming the provisions of the current Charities Bill (E&W) are enacted.

ACIE members include charity specialists in large national accountancy firms; sole traders who carry out IE for some of their local charities; accountancy practitioners within the voluntary and community sector ('community accountants'); and a significant number of individuals who carry out IE on an entirely voluntary basis. There is also a significant number of members who work in the church sector, thus giving the Association expertise in (currently) excepted, as well as registered, charities.

ACIE works regularly with a number of other voluntary sector umbrella bodies, eg, the Charity Finance Directors' Group (CFDG) and the National Council for Voluntary Organisations (NCVO) as well as with the Charity Commission and Home Office, as appropriate.

Appendix 2: Qualifications for Independent Examiners of Charity Accounts over £100K in England and Wales

1 Extract from current CC63 re Selecting an Independent Examiner for accounts over £100K:

'It is strongly recommended that the trustees of charities with gross assets in excess of £1,000,000 or gross income of more than £100,000 but below the compulsory audit threshold, should select a qualified accountant (or an individual with similar qualifications in charity finance at an appropriate level) to carry out the independent examination.'

Page 20, paragraph 4.3

2 Extract from the Charities Bill (E&W) re the qualifications of Independent Examiners of accounts over £250K:

(5) After subsection (3) insert—

“(3A) If subsection (3) above applies to the accounts of a charity for a year and the charity’s gross income in that year exceeds £250,000, a person qualifies as an independent examiner for the purposes of paragraph (a) of that subsection if (and only if) he is an independent person who is—

- (a) a member of a body for the time being specified in section 249D(3) of the Companies Act 1985 (reporting accountants);
- (b) a member of the Chartered Institute of Public Finance and Accountancy; or
- (c) a Fellow of the Association of Charity Independent Examiners.”

Page 28, clause 27, paragraph (5) (3a)

ACIE, 1 July 2005

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