
Corporate

Charities

Audit and Independent Examination

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Introduction

1. The Institute of Financial Accountants (IFA) welcomes the opportunity to respond to the consultation on Charities: audit and independent examination issued by the Cabinet Office on 9 December 2014. This response focuses on the questions included in the consultation document.

Who we are

2. The IFA is an internationally recognised professional accountancy membership body whose members work for small and medium-sized enterprises (SMEs) or who run or work in small and medium-sized accounting practices (SMPs) that advise SMEs.
3. The IFA is a full member of the International Federation of Accountants (IFAC), the global body for the accountancy profession. As such, the IFA takes its place alongside the UK and Ireland's six chartered accountancy bodies, as well as 135 national and regional accountancy organisations representing 125 countries and jurisdictions.
4. Founded in 1916, the IFA supports over 9,000 members and students in more than 80 countries with a programme of professional qualifications and education. As well as resources, events, training and seminars. IFA members uphold high standards of conduct, confidentiality and ethics and undertake annual continuing professional development (CPD) activities.
5. The IFA's capacity to regulate its members for the purposes of the Money Laundering Regulations 2007 is recognised by HM Treasury and is also formally recognised as an awarding organisation by Ofqual, the UK public body responsible for maintaining and monitoring standards for general and vocational qualifications and examinations.
6. On 16 December 2014, the IFA announced that it will be amalgamating with the Institute of Public Accountants (IPA) of Australia, a 26,000-strong membership organisation, with effect from 1 January 2015. As a result both Institutes will maintain their respective brands and local autonomy and operate as part of the IPA Group, which will have a worldwide membership, including students, in excess of 35,000 across more than 80 countries. The coming-together of the IFA and IPA creates the world's biggest SME-focused accountancy organisation.

General Comments

7. Our responses to the specific questions in the consultation are in light of general principles referred to below.
8. First, the IFA supports government initiatives to remove disproportionate legislative and regulatory requirements and to cut 'red tape' and bureaucracy for SMEs and SMPs, including the charity sector. In particular, unnecessary or unduly onerous legislative and regulatory requirements results in charities having to use their valuable and limited resources to meet these requirements instead of using these resources for greater benefit.
9. Secondly, legislation and regulation must be proportionate to the size of the organisations and must be robust enough to underpin an effective financial reporting regime. An effective financial reporting regime strengthens accountability and transparency which are crucial for inspiring confidence and trust in charities.

10. The IFA believes that audit and independent examinations are both important types of assurance engagements for external scrutiny of a charity's annual report and accounts. The principles that underpin these different types of assurance engagement are the same, whether an audit or independent examination. These principles are: three party relationship; agreed subject matter; suitable criteria; sufficient, appropriate evidence; and a conclusion expressed in a written report. However, it is important to recognise that there are some key differences between an audit and an independent examination, for example, the type of work conducted during these engagements and the conclusions in the report. We think that it is important that charities have greater flexibility in choosing the right type of assurance engagement that is best for their charity, be it audit or an independent examination.

Responses to questions

1. Do you agree that the income threshold at which charities should have to have their accounts audited should be increased from £500,000 to £1million?

11. Yes, we support the increase in income threshold for charities to be required to have audits from £500,000 to £1 million.
12. We are of the view that, at times, for smaller charities, the audit costs outweigh the benefits and that an independent examination could be extended beyond charities with an income of £500,000 to those with an income of £1million.
13. Independent examinations are an alternative assurance review engagement which can offer a more cost effective and appropriate solution for smaller charities, allowing them to spend more resources and time on their causes rather than external scrutiny.
14. As mentioned in paragraph 10, we recognise that there are differences in the level of assurance being provided by an audit and an independent examination. An audit provides positive assurance on whether the annual report and accounts are 'true and fair' while an independent examination provides negative assurance 'nothing has come to my attention ...'. However, we believe that, for smaller charities, the board of trustees should have greater flexibility in their choice about what type of assurance engagement is suitable for their charity.
15. While taking into account legislative and regulatory requirements, the board of trustee's decision regarding this matter may be influenced by a number of other factors including constitutional arrangements of the charity, donors and funders requirements and the level of assurance that the board feel they need regarding the charity's annual report and accounts. We would strongly support giving the board of trustees more opportunity to make decisions regarding the types of assurance engagements that are most appropriate and cost effective for their charity.

2. Do you agree that the aggregate group income threshold at which parent charities should have to have group accounts audited should be increased from £500,000 to £1million?

16. Yes, we would support increasing the aggregate group income threshold at which parent charities should have to have group accounts audited from £500,000 to £1million. We think it would be inappropriate to have a discrepancy between the audit thresholds for the parent and the group. Furthermore, having different thresholds would result in not having a level playing field for charities which have chosen adopt different legal structures for strategic and operational reasons rather than legislative or regulatory requirements. Many charities have trading subsidiaries to raise income for their causes and it would seem unfair that these charities would only be required to have an independent examination if the audit income threshold remained at £500,000 while other charities that don't have this legal structure and are above the audit income threshold would be required to have an audit.

17. In addition, this approach would be in line with current audit threshold requirements in the Charities Act 2011 which does not distinguish between an individual charity and a group of charities.

3. Do you agree that the income component of the asset threshold should be increased from £250,000 to £500,000?

18. Yes, we would support increasing the income component of the asset threshold from £250,000 to £500,000. While it is not likely to affect many charities, for those that it does, increasing the income component of the asset threshold would be a welcome initiative. Currently some charities are forced to have an audit because their assets are above £3.26 million but have an income of less than £250,000. As mentioned earlier, we are of the view, that the board of trustees should have greater flexibility in their choice of assurance engagement. Increasing this threshold would give them the opportunity to make a decision regarding this matter.

19. Furthermore, increasing the income component of the asset threshold to £500,000 would be in line with increasing the income threshold for charities from £500,000 to £1 million.

4. Do you think that the asset component of the asset threshold should stay at £3.26 million in line with company law (option 1) or increase to £5 million (option 2)?

20. We would support maintaining the asset component of the asset threshold at £3.26 million because it ensures consistency between the charity asset threshold and the current company law asset threshold.

21. As part of the EU Accounting Directive implementation plans, the Department of Business Innovation and Skills (BIS) has consulted on raising the threshold for small entities¹. It was proposed that the asset limit for small entities be increased from £3.26 million to £5.1 million. Depending on the outcome of this consultation, this may result in further change to the asset threshold in order to ensure consistency with company law. So the asset threshold may change in a short period of time which would add further complexity to the requirements.

5. Do you envisage any difficulties arising from these proposed changes to the threshold? If so, please provide evidence to support your view.

22. While we support the increase in income audit threshold for charities, we are concerned that this increase would only apply to charities operating in England and Wales. A cross-border charity, operating across the UK, will be subject to different charity law and company law requirements regarding accounting and external scrutiny. While we appreciate the charity law is devolved, simplifying the multi-jurisdiction accounting, reporting and external scrutiny framework for charities in the UK would be a very welcome initiative by charities and their advisers.

23. The current Charity SORPs link disclosure requirements in the Trustees' Report to the audit threshold. If these proposals are approved, the joint SORP-making body will have to consider whether to continue linking these disclosure requirements to the Trustees Report or not. The SORP making body is currently awaiting the outcome of the FRC consultation on the Future of Financial Reporting for Small Entities. This proposal included withdrawing the FRSSSE, which, if approved, would have implications for the SORP (FRSSSE). If possible, future consultation on the SORP resulting from FRC's proposals should also take into account the effects of increasing the income threshold on disclosure requirements in the Trustees' Annual Report.

¹ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/350864/bis-14-1025-implementation-of-eu-accounting-directive-chapters-1-to-9-consultation.pdf

6. Do you agree with the estimated costs and cost savings outlined in Part IV? It will be helpful if you can provide actual examples of the difference in costs between the two forms of examination.

24. This is a difficult area for the IFA to comment on since our members are not registered auditors and currently our members are not eligible to undertake independent examinations for charities with income above £250,000 under section 145 of the Charities Act 2011.

25. However, many of our members are treasurers, trustees and some undertake independent examinations below the £250,000 income level. Based on anecdotal feedback, for the smaller charities, the £4,750 average costs of an audit and £2,250 independent examination which have been included in your assessment of cost savings seem reasonable.

7. Do you have any other comments about the proposed changes to the threshold?

26. No other comments.

8. Do you agree that the preparation threshold for group accounts should be consequentially increased in line with the audit threshold from £500,000 to £1 million?

27. Yes, the threshold for preparing group accounts should be in line with the proposed increase in audit threshold.

9. Is there a recognised professional accountancy membership body that you propose could be added to the list of those whose appropriately qualified members can carry out independent examinations of the accounts of charities with incomes that are more than £250,000?

28. As you are aware, we have made a submission to you requesting that full members of the IFA be eligible to undertake independent examinations for charities in England and Wales with income above £250,000 under section 145 of the Charities Act 2011. Full members of the Institute of Financial Accountants have the following designatory letters: Associate Member (AFA) and Fellow Member (FFA).

10. If you have suggested a body to be added to the list of those whose members should be able to act as independent examiners, please provide detailed explanation of how they meet the criteria outlined in this document.

29. As outlined in our request to the Cabinet Office to be listed in the section 145 of the Charities Act 2011, the IFA has exacting criteria to routes to membership, which involves qualification, experience and training. IFA students and members have obligations and duties to the IFA, as a professional body, which includes demonstrating high standards of ethical and professional competence, complying with our standards and guidance and meeting ongoing Continuing Professional Development requirements. The IFA provides support to its members for training and development and also has a robust monitoring, disciplinary and sanctions regime to protect the public. Further details of all these areas have been included in our request to be listed in the section 145 of the Charities Act 2011.