

Charities and financial reporting

The financial reporting requirements for charities that were in place prior to the the Charities Act 2005 continue. These requirements can be found in one of two places, namely the founding document, trust or constitution of the charity itself and any legislation the charity is subject to.

An unincorporated charity has no statutory requirement to meet any particular financial reporting standard. Where a charity is incorporated under the Incorporated Societies Act it is required by that Act to send to the Registrar of Incorporated Societies each year:

- a statement of the income and expenditure for the latest financial year;
- particulars of the assets and liabilities of the society at the close of the year;
- details of any securities or charges affecting the property of the society.

Where a charity is incorporated under the Charitable Trusts Act it has no particular obligations for financial reporting under that Act. Where a charity is incorporated under another Act, that particular Act should be studied for any specific financial reporting requirements.

Charities applying for grants may find that, regardless of their constitutional arrangements, the funding agency to which they are applying may require the provision of financial statements prepared to a certain standard, and possibly audited or independently reviewed.

Registration and reporting under the Charities Act 2005

When a charity submits an application to register under the Charities Act it will be asked to provide some simple and straightforward financial information on the application form. After registration charities will need to submit an "annual return". It is probable a copy of the charity's financial accounts will need to be appended.

Financial Reporting Act 1993

For most charities the reporting standards arising out of the Financial Reporting Act 1993 do not apply. There are some specific exceptions, for example those charities that are "issuers" in terms of the Securities Act. While a further review of the Financial Reporting Act 1993 is expected to happen this year, we understand that the Government will not be making any decisions arising from this review until after there has been further consultation with charity stakeholders. Any changes arising from this review will have a long transition period before coming into force. We have been advised that the earliest possible date for any change would be for financial years beginning on or after 1 January 2010.

What accounting standards should charities apply

The New Zealand Institute of Chartered Accountants has established a framework of financial reporting and auditing standards, and members of the Institute are required by their professional ethics to observe those standards when they are involved either in preparing financial statements or auditing them. While the standards are applicable to all types of organisations, certain smaller entities are exempted from some standards because of the entities size. This is known as "differential reporting".

If an organisation is not incorporated, and/or is not required to prepare financial accounting reports for consideration by agencies external to the organisation, then it may use whatever standards it chooses in preparing internal financial reports. However, if a Chartered Accountant is involved the standards of the Institute will be applied.

Some guidance on applying "Generally Accepted Accounting Practice to Not-for-Profit Organisations" appears in a booklet prepared in 1999 by the New Zealand Institute of Chartered Accountants called "Financial Reporting by Voluntary Sector Entities" (also called R-120). The Institute is currently updating R-120 and expects to release the new version in late 2006.

If you require further information on any of these topics or would like details on other accounting matters, contact your local Grant Thornton office:

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assurance adviser

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What different types of assurance engagements are there?

There are basically three key forms an assurance engagement can take. These are outlined below. What particular type of engagement is most appropriate depends upon statutory requirements and the needs and requirements of management and stakeholders.

Type of assurance engagement	Purpose of the engagement	The outcome or product delivered
External (attest) audit	<ul style="list-style-type: none"> • Designed to provide a high, but not absolute, level of assurance on financial statements of an entity. • Provides positive assurance that the financial statements have been prepared, in all material respects, to present a "true and fair view". • Note that where the auditor has concerns, either a qualified audit opinion can be issued or an unqualified opinion that contains an explanatory paragraph. 	<ul style="list-style-type: none"> • An audit report to the stakeholders of the organisation, attached to the financial statements (the intention is to provide a positive level of assurance). • The auditor also furnishes a management letter addressing key findings from the audit, (this should also be presented to the governing body).
Review engagement	<ul style="list-style-type: none"> • Provides a moderate level of assurance. • Examines the financial information with the objective of providing a report that nothing has come to the attention of the auditor that causes them to believe that the financial information does not present a true and fair view. 	<ul style="list-style-type: none"> • A negative assurance report to the stakeholders of the organisation. • A management letter should also be furnished.
Agreed upon procedures engagement	<ul style="list-style-type: none"> • Where the auditor is engaged to carry out procedures of an audit nature in order to meet the client's needs for particular information. • Provides a report of factual findings. 	<ul style="list-style-type: none"> • A report on the factual findings of the engagement (no assurance is expressed).

Our experience is that the term audit is often misused. Many organisations and stakeholders request an audit or specify an audit in documentation when this is not really required. The correct choice of assignment will depend on the circumstances and your Grant Thornton adviser will be pleased to assist.

Can internal audit assist your organisation?

Overview

Internal audit is a management tool. It is an exercise in risk management whereby the governing body of an organisation, usually via an audit committee, seeks assurance that the organisation's governance and internal control systems are effective. It generally supplements any assurance obtained from the external audit process, as one of the main responsibilities of an external audit is to provide an opinion on whether the statutory financial statements are fairly reflected. External audit reports are to the stakeholders of an organisation, whereas the reporting responsibility of internal audit is to the audit committee.

Whilst world events have highlighted major shortcomings in the governance and internal control systems of some large international companies, the risks are certainly not confined to global corporations. The responsibilities that now encumber governing bodies and stakeholders of both public and private sector organisations are substantial. There is a growing awareness within the business community of corporate governance and internal control issues. The focus on the requirement for effective systems and procedures, accountability provisions, transparency and independent review has intensified.

Internal control systems

Internal control is a control process put in place by an entity's governing body and management. Internal control systems are designed to provide reasonable assurance that the following objectives are being achieved:

- effectiveness and efficiency of operation
- reliability of financial reporting
- compliance with laws and regulations.

The internal control systems therefore include all the policies and procedures (internal controls) adopted by the management of an entity to assist in achieving the objective of ensuring, as far as practicable, the orderly and efficient conduct of its business. This includes adherence to management policies, the safeguarding of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial and non-financial information.

Widening the scope of internal audit

Internal audit has traditionally focused on auditing financial and internal control systems. However the role of internal audit continues to evolve. In terms of scope, effective and well-resourced internal audit functions generally extend their focus into areas of efficiency and effectiveness. This approach generally increases the potential to add value, in terms of an organisation's overall risk management framework.

Areas that can be reviewed by an effective internal audit function include:

- reviewing internal control systems and procedures
- reviewing and implementing financial and non-financial reporting systems
- addressing concerns in relation to fraud
- reviewing delegated authorities and expenditure approval processes, including credit card usage
- performing efficiency and effectiveness reviews
- reviewing developing KPIs (Key Performance Indicators)
- reviewing and implementing risk management systems
- assessing the appropriateness of financial policies and compliance with Financial Reporting Standards
- reviewing the effectiveness of systems to facilitate legislative compliance
- considering the implications of new accounting and auditing standards.

Key attributes

An effective internal audit function generally has the following key attributes:

- absolute independence
- total credibility, along with the ability to develop constructive working relationships within the organisation
- sufficient expertise and experience to perform the role effectively, and the support structure to train and upskill staff as required

- a robust internal audit methodology that provides a sound framework for:
 - o performing the risk assessment that underpins the development of the internal audit programmes
 - o planning, performing and evaluating the work
- an ability to report in a timely and effective manner
- the flexibility and resources to respond to changing demands, areas of focus and priorities of the role
- a strong level of professional judgement, integrity and, where necessary, resilience.

Independence

To be fully effective, the internal audit function needs to be independent. As a general rule internal audit staff should not:

- have professional or personal relationships or monetary or other interests which may give rise to a conflict of interest
- have undue limitations placed on the scope of their work
- review areas in which they have some operational interest
- account or report to a person whose work may be the subject of appraisal by internal audit.

Summary

In terms of risk management, an effective internal audit function can provide considerable assistance in:

- improving the effectiveness and efficiency of an organisation's operations
- enhancing the reliability of financial information
- ensuring the governing body's directives are followed
- ensuring adequate systems are in place to facilitate compliance with relevant laws and regulations.

Grant Thornton performs a number of internal audit assignments, and would be pleased to discuss your requirements with you.

New registration dates for Charities

The Charities Commission has recently announced a new start date for the registration of charities. The registration of charities under the Charities Act will begin next year on 1 February 2007. The date registration is required to be completed by in order to maintain taxation benefits has also been changed. While registration is voluntary, existing charitable organisations will need to register between 1 February 2007 and 1 July 2008 to maintain income tax and gift duty exemptions. This allows charitable organisations 17 months to register before any existing tax exemptions are affected.

Although you cannot register until 1 February 2007, there are certain things you can do now to prepare for registration as a charitable entity. We recommend you ensure your rules or governing documents are available. You should review them to see if they need updating. It is worth checking if your charitable purpose is clearly stated and your organisation is meeting the charitable purpose. Your Grant Thornton advisor has extensive experience with charitable organisations and the new legislation. We will be able to assist you with this review and the registration process.