

assurance adviser

Grant Thornton 

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International Financial Reporting Standards

New Zealand is poised to adopt international financial reporting standards (IFRS) with effect from 1st January 2007. This assumes that you are not required to 'early adopt' due to the influence of some off-shore subsidiary or parent company. Comparative financial information will also need to comply with IFRS's.

For a 31 March balance date this effectively means an entity should, from 1 April 2005, assess the impact and disclosure of the new reporting standards so that a comparative 31 March 2006 statement of financial position can be prepared.

Rules have been written to help preparers of financial statements determine how International standards should be applied for the first time they adopt. Rules are contained in IFRS 1, which has been issued in New Zealand as ED NZ IFRS 1. As changes are made to IFRS 1 these will likely result in amendments to our ED NZ IFRS 1.

The main emphasis of IFRS 1 is to provide guidance on the changes required to the opening balance sheet that will form the starting point for accounting under international standards.

The focus of IFRS 1 is on four main areas.

- Recognise all assets and liabilities as required by IFRS's
- Not to recognise items of assets and liabilities if not permitted by IFRS's
- Reclassify items that previously complied with GAAP yet are disclosed as a different type (asset, liability or equity) under IFRS's
- Apply IFRS's in measuring all recognised assets and liabilities.

As IFRS's are applied retrospectively an entity is expected to implement the new standards as if they always existed.

Audit Ramifications

The introduction of IFRS's will result in increased complexity, judgement and disclosure. It has been estimated that there is 20% of additional disclosure under IFRS's than that under our existing regime. All these factors have implications for the presentation of your financial statements..

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IRD Audit Adjustments

International Financial Reporting Standards (Continued from page 1)

The initial transition to IFRS's require an entity to prepare the opening balance sheet with comparatives and require additional disclosure which will be required to be audited if a current external audit is being performed. Detailed reconciliations are also required to be disclosed in the first IFRS annual financial statement.

Entities may well benefit from having the transition date balance sheet audited well in advance of the preparation of the first IFRS financial statements.

Proposal Adoption of International Standards on auditing

The Institute of Chartered Accountants of NZ has recently disclosed its consideration to adopt Internal Standards on Auditing (ISAs) in the near future. This is a reaction to the fact that a number of jurisdictions have announced their intention to adopt ISAs including United Kingdom, European Union, Australia and South Africa.

Adoption would ensure NZ is aligned internationally giving international credibility.

While adoption of ISAs does not directly effect reporting entities with respect to financial statement presentation or disclosure, it does impact upon the audit and may involve additional procedures. More will be reported once any submissions received by the Institute have been considered.

The following income tax issues are common problem areas identified during IRD audits.

Depreciation - Specific areas where errors are made include:

- Assets available for use or owned for a part year only being depreciated for a full year
- The 20% loading rate for new assets being applied to second hand assets and to buildings
- Recovery on disposal either incorrectly calculated or not returned
- Incorrect depreciation rate used
- Excessive value of asset used when transferred between associated persons
- Claiming loss on disposal for buildings.

Bad Debts not written off at balance date - A deduction is permitted only for bad debts which are actually written off as bad in the income year in which the deduction is claimed.

The Commissioner will accept that a debt has been written off in the following circumstances:

- If you maintain a computerised debtors' ledger, the balance for individual debtors has to be reduced by the amount of the bad debt.
- In other cases, specific actions need to be taken by the creditor evidencing the creditor's belief that the debt is bad. Usually, this will include appropriate book keeping entries.

Capital Expenditure - IRD has given examples where they consider capital expenditure has been incorrectly deducted:

- Costs of importing, transporting and installing new assets; including employees' wages
- Building enlargement expenses
- Some building relocation expenses
- Improvements / renovation to buildings.

Cut Off Issues - Often the cut off for revenue and expenditure at balance date has not been accurately completed. Common errors include an omission of cash on hand from sales, income which has been derived but has not been invoiced at balance date (e.g. there is an entitlement to bill) and cutting off prior to the end of month.

Fines and Penalties - IRD's view is that fines and penalties are not deductible for income tax purposes.

Entertainment - IRD often finds that entertainment expenses have not been treated correctly. This is particularly so in relation to deductions for food and drink. These types of expenditure are normally 50% deductible for income tax purposes. However, there are exemptions which you should be aware of. It is also important to ensure that appropriate documentation is maintained in support of any claim.

Establishing a moral compass through ethical behaviour, values and goals

"I am very sorry to have to report to you today that our organisation has uncovered a major embezzlement." Such statements conjure nightmares throughout the not-for-profit industry. But the reality is that risks are inherent in any business.

Establishing solid business ethics, however, can help not-for-profits mitigate debacles that can put organisations into a tailspin. Higher expectations from regulators and donors have made ethics a hot topic in the industry. Stakeholders are pressuring organisations to ensure ethical behaviour is a core part of their mission, values and actions.

This increased focus on ethics also affects the day-to-day operations of many not-for-profits. There is something to be said for operating in a congenial, informal way, but stricter regulations are causing not-for-profits to put formal practices into place. Creating internal controls, monitoring them and reporting results to the board are good business practices that can lead to a more ethically run business, not-for-profit or otherwise.

The Ethical Board

To create an ethical culture, tone from the top is essential. Board members especially should be committed to, and passionate about, the mission of the organisation. This commitment from the top will trickled down throughout the organisation.

Board members can actively express their commitment to the organisation by placing loyalty first with the organisation, not management.

There is a covenant between the not-for-profit, the board and the large community that is based upon a trust that the organisation with ethically serve its mission and goals.

This trust can be challenged, however, when conflicts of interest arise. For example, where a board member owns a company and urges the organisation to use that company's services. The situation is ethical if that director's company offers the best value. But if it is not the best offer available, there is a conflict of interest here and the pressure from the director should be resisted.

Code of Ethics

Ethical situations including conflicts of interest are typically covered in the not-for-profit's code of ethics. The code is the primary tool to convey an organisation's value message, both internally and externally.

The code is more than a list of objectives on a piece of paper. It is a living document that defines the organisation's values, ethical culture and environment of integrity.

Producing a code that is consistent with the organisation's values and mission statement is more complex than copying another not-for-profit's code and

releasing it. Not only is that approach in itself unethical, but it does not allow you to tailor the code to your organisation's specific needs and goals. Using several templates as examples, however, is a good starting point for organisations to flesh out areas that are relevant to their specific mission.

Once the code of ethics is established, employees should be educated about its meaning and how the code applies to them and their responsibilities. Part of this process is educating employees about possible areas of pitfalls, including conflicts of interest, embezzlement and harassment issues.

Codes should also be refreshed annually to reflect any changes in regulation or the organisation's mission.

Encouraging an ethical environment

In addition to establishing a code of ethics, there are many other ways organisations can encourage an ethical environment.

- Establish a channel for communicating concerns: Define a channel through which staff can raise concerns and issues to the board.
- Communicate the mission: Inform employees of the organisation's purpose and mission to ensure their actions are in line with the objectives of the not-for-profit.
- Hire well: Hiring well and conducting background checks can minimise risks.

Incorporated Societies and Charitable Trusts - Website

On 2 November the Companies Offices launched a new website for incorporated societies and charitable trusts - www.societies.govt.nz.

This website has been launched with the intention of improving service delivery to organisations operating in the voluntary sector.

The new website will enable the Companies Office to implement online document registration services, and ensure better targeted information and resources to incorporated societies and charitable trusts.

If you have any questions about the website, contact the Companies Offices on 0508 SOCIETIES (0508 762 438).

Post Graduate Diploma in Management of Not for Profit Organisations

Waikato University offer a Post Graduate Diploma in Management of Not for Profit Organisations.

The course contributes to the enhanced management of organisations that together make up the community (not-for-profit, ngo and voluntary) sector and the sector's overall contribution to sustainable wellbeing. Examples of the organisations and networks of interest are those committed to

- social, political, cultural, educational, religious or spiritual enhancement
- environmental restoration
- the promotion of arts, leisure and fun
- the creation of employment and careers opportunities
- international networking, citizen awareness and so on

The organisations and their networks may be small and local, or national or international in their scope. They may be reliant on erratic funding regimes or command large budgets, well supported by charitable donations, fees for service, substantial government or private grants, contract work and so forth. Common to them all is their desire to achieve their goals – to make a difference in the lives of their members or society more generally. Managing their aspirations and their resources wisely requires insight, skill, and commitment. Their research and teaching agenda seeks to contribute to this work.

Whether you currently work in the Not for Profit sector or are interested in the sector, this course will be of interest.

For further information visit: www.mngt.waikato.ac.nz/community

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