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CHARITY NEWSLETTER

□ □ □ SUMMER 2006

Introduction

Welcome to the late summer edition of our Charity Newsletter. I was hoping to be able to include a commentary on the new Charities Act but sadly this is still delayed in its slow process through parliament.

Once again we have taken the opportunity to include information about a wide range of subjects that effect charities in the county so I hope there will be something for everyone. We are continuing to look at some practical issues relating to the new SORP, this time with regard to the Statement of Financial Activities, and consider the ever-present risks of fraud from which charities along with all other businesses are not immune.

Finally advance details are shown on the last page of our forthcoming charity seminar which I hope you will be able to attend.

Richard Robinson
Partner

8 September 2006

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Internal Controls and fraud

Internal controls are essential in all but the smallest of charities to ensure that the assets of the organisation are safeguarded. If adequate controls are not in place then there is increased risk of inefficiency in the organisation, or possibly fraud.

In smaller charities it is necessary for the trustees to be more involved in the day to day running of the charity, particularly in respect of authorising significant transactions.

Recent well-publicised frauds involving charities have included the following:

- * *Internet* – obtaining donors details, including credit card information from a secure server.
- * *Internal* – allowing one person to record and process a complete transaction can leave a charity vulnerable to fraud. Simple controls such as having dual signatories for cheques can greatly reduce this risk.
- * *Bogus donor* – this commonly involves the charity receiving a substantial donation. A letter is then received from the donor stating that too much was donated due to an administration error. This letter then requests repayment of the overpayment, which is refunded to the donor. The cheque originally sent will often then bounce leaving the charity out of pocket. It is important that charities are aware of their responsibilities when accepting significant donations from unknown sources.
- * *Professional fees* – this involved the manipulation of contracts, and inflated fees. This kind of fraud involves a great deal of collusion.
- * *Bank details* – this fraud involves payments being siphoned from a charity bank account. The bank details were obtained from a gift aid declaration form. This emphasises the importance of keeping charity accounts up to date, reconciling the bank account regularly, and reviewing for unexpected payments.

UK organisations are losing between 3% and 5% of their income through fraudulent activity. Employees carry out the majority of fraud. In order to be satisfied that all major frauds are identified charities need to put in place controls that will identify any possibly suspicious activity.

Governance

A new publication, ‘Good Governance: The code of Governance for the voluntary and community sector’ has recently been published. The code includes a list of the main principles of good governance.

The aim of the code is to improve governance of charities and other not for profit organisations. The code is a guide that will help charities to develop good practice. The seven key principles within the code are as follows:

- * Board leadership
- * The Board in control
- * The high performance Board
- * Board review and renewal
- * Board delegation
- * Board and trustees integrity
- * Board openness

The Charity Commission is working in partnership with the Governance Hub, which endorses the above publication and also the National Occupational Standards for Trustees and Management Committee Members, which provides further advice for trustees.

SORP 2005

In our last newsletter we looked at Incoming Resources within the SOFA. As promised we continue our look into the Charities SORP, this time with a review of the SORP requirements in respect of Resources Expended.

One of the major changes between SORP 2005 and SORP 2000 is the way in which expenditure is allocated in the Statement of Financial Activities (SOFA). The main headings under Resources Expended are now as follows:

Costs of generating funds □ raising funds to spend on the charity's activities

Charitable activities □ achieving the charity's objectives □

Governance costs □ overseeing the work of the charity □

The starting point when trying to analyse a charity's costs between these headings is to identify any directly attributable costs, and then include these costs under the relevant headings. Examples may include grants payable and operational staff wages.

Once these costs have been taken into account the remaining overhead costs, which cannot be attributed to one particular heading, need to be allocated. One common example will be managers' salaries. Under SORP 2000 these salary costs may have been included in administration expenses. This is not acceptable under SORP 2005 because Governance costs have replaced management and administration expenses, and this category has a much narrower definition. Therefore under SORP 2005 it is necessary to allocate the salary costs between the above headings. In this example the fairest way of doing this is likely to be based on the percentage of time spent by staff working in each area.

Governance costs, as its title indicates, includes a relatively small number of costs, in respect of overseeing the charity. This is likely to include audit fees, legal fees, trustees' expenses and board meeting costs. It is also acceptable for some staff costs to be apportioned to this category (for example in respect of attendance at and preparing for board meetings).

When all income and expenses have been allocated to the relevant SOFA headings it is important for the trustees to review this to ensure it reflects the actual activities undertaken. It is also a SORP requirement to include an analysis of how costs are analysed between each category and the method of allocation. The new SORP should result in easier comparability between income and expenditure, on a project by project basis.

As well as costs being analysed between the headings of the SOFA a further analysis may need to be included in the notes to the accounts by activity.

In our next newsletter we plan to look into how the trustees' report has changed following the new SORP and how successful this will be in providing more information about the charity to a reader of the accounts.

Trading subsidiaries and gift aid donations

The new charity SORP adopts the principles of Financial Reporting Standard Number 21 (FRS 21) which was issued recently by the accounting standards board. The main way in which this will affect charities will be where a trading subsidiary gifts its taxable profits to a charity on an annual basis.

Tax rules state that a gift aid donation needs to be paid over within nine months of the year end for tax relief to apply. FRS 21 rules mean that for a liability to be included at the year end an obligation must have existed at that date. In the case of a charity subsidiary a board meeting minute dated prior to the year end would be sufficient. If the passing of profits to a charity is by way of a deed of covenant or is a term of the subsidiary's memorandum of association the obligation automatically exists and therefore no further evidence is needed.

Sage Accounting Update

Sage Line 50 2007 is to be launched this month. Since the introduction of the charity functionality in version 12, some improvements have been made, which include the following:

- * HM Revenue & Customs will now accept the gift aid report printed from Sage
- * SOFA categories can be assigned to multiple nominal codes
- * Within the customer ledger, you can select a customer type, for example a member, and store all of their details

If you would like any further information please contact Susie Viles on 01872 276116.

Friendly and Industrial and Provident Societies

The audit exemption limits for these societies have increased for year-ends 2 months or more after 5 April 2006 (in effect June 2006 year ends).

The new audit exemption limits are as follows:.

- * Assets must not exceed £2.8 m (previously £1.4 m)
- * Turnover must not exceed £5.6 m (previously £350k)

STOP PRESS – self employment status of workers

HM Revenue & Customs have recently been changing their policy when dealing with organisations that should have been treating self employed workers as employees. Previously the Revenue has been flexible in allowing any taxes paid by the worker under self-assessment to be netted off the PAYE settlement. Following a recent case this has not been allowed and the organisation had to settle the full liability, even though the tax may have already been settled under self-assessment. It is then up to the organisation to recover the potential self-assessment refund from the employee by mutual agreement. If this method is to be avoided the employee needs to sign a mandate confirming that a set off can be made.

In the case of charities, where often staff are only employed for fixed term contracts this may not be possible, if the worker concerned has left the post. Therefore it is vital from the start to ensure that workers employment status is reviewed to reduce the likelihood of a problem arising.

VAT corner

The Children's Society

This much-publicised case has led to many charities potentially being able to recover VAT on fundraising costs, something that has not been possible in the past. However the Revenue have argued that fundraising costs are not an overhead for the purposes of calculating the recoverable VAT percentage under the partial exemption calculation. Therefore the recovery of VAT could be much lower than anticipated.

Mayflower Theatre Trust

Following the Mayflower Theatre Trust case a proportion of VAT under the partial exemption rules can be reclaimed on the cost of hosting productions following a High Court judgement. The argument was that the fees paid to production companies to host a production are not entirely related to the exempt ticket sales, but also in generating taxable income from programme sales, refreshments and sponsorship.

Listed places of worship

The listed place of worship scheme has been extended from March 2008 to March 2011. This was announced in the budget. The main criteria remains the same, in that the scheme repays as grant aid the difference between five per cent and the actual VAT suffered on repairs that are eligible. The eligible expenditure has been extended and now includes professional fees, and certain fixtures and fittings from 22 March 2006.

Charities Bill

The Charities Bill report stage is unlikely to happen until parliament returns in October. Much attention will be placed on how the 'public benefit test' can be applied to private schools and other charities that charge fees.

The Charity Commission will also need to interpret this public benefit test.

The Bill is expected to increase the audit requirement threshold to £500k income or where gross assets are over £2.8m with income over £100k. A qualified independent examiner's report will be required for income over £250k.

Trustee protection

Under the Companies (Audit, Investigations and Community Enterprise) Act 2004 the articles of association of a charitable company can be amended to allow the company to pay for trustees' legal costs if they are sued. This money must be repaid if the trustee loses any legal case. Permission needs to be obtained from the Charity Commission for this change to go ahead.

Charity Commission Direct

The Charity Commission has launched a new enquiry service. This service is based in Liverpool and will act as an initial contact point for all enquiries by phone, e-mail, post or fax.

The contact details are:

Telephone: ☐ ☐ 0845 3000 218
Fax: ☐ ☐ ☐ 0151 703 1555
E-mail: ☐☐☐ ☐ enquiries@charitycommission.gov.uk
Post: ☐ ☐ ☐ Charity Commission Direct, PO Box 1227, LIVERPOOL, L69 3UG

Charity registration on-line

A new on-line charitable registration process should shortly be available from the Charity Commission. The aim will be to make the process of registration more accessible. The number of questions asked will not be reduced.

Greater scrutiny for trustees of charities with vulnerable beneficiaries

The Charity Commission is now requesting sight of copies of Criminal Records Bureau checks on all trustees prior to registering charities, where there are vulnerable beneficiaries from 1 June 2006.

End of one year contracts

The local government association has pledged an end to one year contracts with charities. The chairman of the LGA, Sir Sandy Bruce-Lockhart, has called on all councils to offer three year deals. This should mean that charities can plan ahead with more certainty regarding income generation.

Charity Repayment Claims

As we mentioned in our last newsletter the Revenue has increased the emphasis on its audit of gift aid claims and their website now contains updated information regarding this process. This includes information on the audit itself, such as the records which will be needed to be available for inspection, as well as what the audit is likely to involve, and other information that the Revenue auditor will be looking for. There is also guidance on statistical sampling, in particular the methods used when dealing with large charities and applying any errors arising in the sample to the whole population of repayment claims. Further information is also available on how the audit will be concluded.

The website address is <http://www.hmrc.gov.uk/charities/guidance-notes/chapter7/audit-background>

Advance Announcement Robinson Reed Layton Charity Seminar

Our next charity seminar will be held at the Penventon Park Hotel at 2pm on 24 October 2006.

In addition to covering a number of topical issues such as SORP 2005 and Corporate Governance we have invited as a guest speaker, George Winters, the chief executive of Seven Investment Management (7IM) who will be talking about the trustees responsibilities under the Trustee Act and the investment options available to charities who wish to make the best use of surplus funds. 7IM are well respected investment advisers to charities throughout the UK and have achieved considerable media exposure through their marketing director, that well known TV pundit Justin Urquhart Stewart.

Further details will be issued shortly.

Charity Contacts

If you would like further information regarding any of the issues raised in this newsletter please contact a member of our Charity Team:

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