Diploma in Charity Accounting – sample script 2: Practice

1. POLICY, LAW AND REGULATION (15 MARKS)

1b.
- i) Describe one development in policy, law or regulation;
- ii) Explain the impact of this development on your client(s); and
- iii) Explain the advice you gave to enable implementation or compliance.

Payments from subsidiaries to parent charity

Where a charity undertakes trading activities which are not deemed to be 'primary purpose trading' and above the small-scale exemption from Corporation Tax, it is usual for them to create a wholly-owned trading subsidiary to undertake such activities. When there are sufficient reserves, the wholly-owned trading subsidiary can then Gift Aid its profits to the parent charity, thereby avoiding a charge to Corporation Tax.

In advance of update Bulletin 2 to the Charities SORP (5 October 2018), trading subsidiaries would recognise donations in the year if they were physically paid within nine months of the year end. The update driven by Financial Reporting Standard 102 means that Gift Aid payments can only be recognised in the subsidiary's accounts when physically paid. unless there was a legal obligation to donate profits to the charity. Although there was a change in accounting treatment, the tax treatment of the donation remained the same.

I work with a charity (income £1.2m, net assets £932k) set up to preserve the fabric of a palace to advance work of the Church of England. The charity also has a subsidiary which donates profits to the parent charity. As a result of the changes in accounting treatment and the fact that there was no legal obligation to donate profits to the charity, the charity could no longer show the donation in the accounts as being made in the year.

I contacted the client to discuss the regulation changes to the treatment of the donation and how this would be reflected within the accounts unless a legal obligation was established between the two entities. The client wished to explore creating a legal obligation to continue recognising the donation within the year. I explained that an obligation could be created through changes in the Articles of Association or a Deed of Covenant; however, this would restrict the trading subsidiary's ability to control the level of reserves that it holds, which could cause an issue in future years should there be a reduction in the subsidiary's performance.

On confirmation from the client that it did not wish to create a legal obligation, the change was reflected in the accounts. This resulted in a restatement to the prior year donation and reserves to ensure compliance with the new regulations.

Before the change in accounting treatment, the donation declared on the Corporation Tax return matched that in the financial statements. With the change in regulation, this is no longer the case and therefore additional narrative was provided to the client to help it understand the difference in the donation declared for tax purposes.

The advice given helped the client make informed decisions whilst ensuring compliance with the new regulation.

Word count, excluding question titles and requirements: 452

2. RESOURCE MANAGEMENT (15 MARKS)

2b.

i) Describe one issue of resource management at a client;

ii) Explain how you addressed the issue; and

iii) Explain how this enabled you to recommend improvements to the client.

Advising and implementing changes to an accounting software

A newly-appointed treasurer of a small bereavement charity (income £460k, net assets £513k) contacted us as he was concerned about the way in which the charity was tracking restricted funds. The previous treasurer kept records of this external to the accounting package, which usually resulted in a year-end process to incorporate the information in the statutory accounts. This was time-consuming and, with an anticipated expansion of activities, the new treasurer and CEO were keen to seek advice on updating systems and implement processes to incorporate the tracking of restricted funds.

Initially, I consulted the CEO to understand the current process and to identify where improvements could be made. This involved understanding the nature of the funding and looking into the chart of accounts currently being used. I assessed the software that was in place and its functionality to meet the charity's requirements.

Once the initial assessment had been completed, I discussed with the treasurer and CEO that some systems within the cloud-based software could be used to monitor income and expenditure relating to restricted funds. It also would require management to implement a process of coding invoices by nominal and class to ensure that the external bookkeeper is aware of the allocation when inputting data into the software. I prepared a quote for the work and this was approved by the client.

A session was arranged to demonstrate the functionality within the software. This provided an opportunity for the client to ask questions and ensure that the changes were tailored to its specific needs. As part of this process, I also reviewed the chart of accounts with the client to capture information that would be required for statutory accounts purposes. The processes of authorising, coding and then posting invoices to the system were considered and streamlined to ensure efficiency and good governance. I provided further support as part of the agreement and we were in frequent communication to resolve any initial queries.

This process enabled me to find new ways to use software to enhance the client's method of tracking and ensuring that it met the charity law requirements on restricted funding. It has instilled further confidence in the client that it is complying with the restrictions outlined by donors and it has also meant that better management information can be provided in relation to fund balances through better use of resources. The client has provided feedback that the process of coding invoices has improved the efficiency and accuracy of the data being input into the system. The year-end process has also been simplified with the fund balances being integrated into the software.

Word count, excluding question titles and requirements: 441

3. FUNDRAISING, INCOME GENERATION AND INCOME DISTRIBUTION FOR PUBLIC BENEFIT (15 MARKS)

3b.

i) Describe one fundraising, income generation or income distribution campaign/strategy undertaken by a client;

ii) ii) Explain the advice you gave in connections with the campaign; and

iii) iii) Explain how this benefited the client.

Obtaining funding during COVID-19

During the coronavirus pandemic (March 2020), the government implemented policies which meant that non-essential retail shops were required to close for a period of time to prevent the spread of the virus. An international aid charity (income £837k, net assets £100k) which generates 80% of its income through charity shops therefore lost a large source of income.

Understanding that it had significant fixed costs, most notably employment and premises costs, I contacted the client to understand its situation, discuss income generation strategies and explore funding that it might be entitled to apply for.

From the discussion, I suggested that it would be able to apply for grants through the Coronavirus Job Retention Scheme. This would help the charity retain well-trained staff and enable it to furlough staff and to reclaim 80% of salary costs for all shop assistants who were paid up to £2,500 per month.

I advised the charity to identify how many employees were needed to maintain and sustain its activities after the pandemic had passed.

Once it had been decided who would be furloughed, I advised that this be agreed in writing with the employees to ensure contractual agreement of the situation and confirmation that no work could be undertaken during the furlough period.

The client set up an online account with HMRC on my instruction. I then provided the GOV.UK guidance to the client on calculating furlough payments, highlighting some more technical areas of text. I reviewed the calculation, allowing the client to submit its claim by the deadline. Confirmation was obtained that the submission has been made successfully, with the grant being received into the bank once the application had been processed.

This benefited the client as it was able to obtain funding to meet salary costs that it would not have been able to cover without the grants, and to retain staff that were fundamental to the shops' operating and reopening. Without the furlough payments, the charity would potentially have had to bear redundancy costs.

It would have also needed to recruit new staff when the shops were able to reopen, which would have incurred additional cost and time. The time spent by the senior management team was therefore spent furthering the charitable activities of the charity as opposed to employing and training new staff.

Word count, excluding question titles and requirements: 385

4. STRATEGY AND GOVERNANCE (15 MARKS)

4b.

- i) Describe one issue of strategy or governance at a client;
- ii) Explain how you addressed the issue; and
- iii) Explain how this benefited the client.

Reconstruction and merger accounting

The trustees of an unincorporated charity (income £283k, net assets £437k) contacted me as the charity's activities were expanding exponentially and they were concerned about the financial risks liable to themselves as trustees. With new funding agreements, the addition of employees and a higher level of charitable activities, the trustees wanted an assessment of the current structure based on the charity's size.

From our discussions about the legal form that the charity could take, it was determined that its assets and trade would be transferred to a new charitable company. The unincorporated charity operated with a 31 December year end but the trustees wanted to change it to 31 March to be in line with most of its funding. I extended the year end to 31 March to ensure coterminous periods; this also meant that the first set of accounts would represent a twelve-month period in both the current year and prior year comparative, in line with the client's expectations.

To ensure that the transfer of assets could take place, it was important to establish that the beneficiary class had not significantly changed and that the objectives of the two entities were aligned. I was concerned that any funding provided to the unincorporated charity might be misallocated against the donor's restriction when transferring funds between the entities. I reviewed some of the contracts to identify the restrictions before ensuring that the trustees knew their responsibilities over governance in spending the funding in line with the donor's wishes. The trustees of both entities were the same and therefore no conflicts of interest were present in the nature of the funds or their intended use. The two entities' objectives were the same and no non-controlling interest in the net assets of the charity would be altered by the transfer.

The financial statements were prepared to include the names and descriptions of the combining charities. I provided an analysis of the prior year SOFA comparatives to highlight the amounts represented by each entity, along with the aggregate carrying amount of net assets held by each entity at the date of the merger. I also briefed the trustees on the disclosure requirements necessary within the Trustees' Report.

My work helped the charity navigate its way through the merger, whilst ensuring good governance and safeguarding the charity's assets. The reconstruction has meant that the trustees are more content with the charity's structure and how they support their beneficiaries in line with the charity's objectives. The change in accounting period has also helped trustees track performance of contracts for better strategic decision-making.

Word count, excluding question titles and requirements: 430

5. CHARITY ACCOUNTING, AUDITING AND TAXATION (15 MARKS)

5b.

i) Describe one significant charity accounting/audit/taxation issue that you encountered at a client;

ii) Explain how you addressed it; and

iii) Explain the technical knowledge/skills that you used in doing so.

Accounting issue surrounding funds held as a custodian trustee

Whilst working with a client (income £887k, net assets £423k) that provides independent advice to its beneficiaries, I realised that it was treating a grant as funds held as a custodian trustee within the statutory accounts.

The transaction comprised monies being received from a trust that were then distributed to individuals in the form of vouchers, to support them with utility costs. On reviewing this transaction, I identified that the income was being recognised differently from my understanding of the guidance and I therefore requested a representation from the client along with the funding agreement.

The client explained that it considered itself as an agent as opposed to a principal: it viewed the funder (the trust) as having the ultimate control as to who (the individual) is eligible to claim the grants.

It was clear to me, on reviewing the documentation, that the charity was in fact the principal of the funding on the basis that it had discretion and control over the selection of the beneficiaries and how the funds were distributed. I then reverted to Module 19 of the Charities SORP, which confirmed that my understanding of the transaction was correct.

When I explained the above, the client continued to dispute the treatment and asked for more confirmation. For further assurance, I discussed the accounting treatment with the partner of the firm and concluded that it was beneficial to seek further advice from the ICAEW Technical Helpline. We obtained confirmation that my assumptions were correct and that the income should be recognised within the financial statements.

I made a calculation to quantify the significant material adjustment before proposing it to the client. The transactions were previously treated as off-balance sheet items and would turn a projected deficit into a surplus for the year. Initially, the adjustment was met with resistance, but when I mentioned its implications for our independent examiner's report, the trustees were happy to make the relevant adjustments.

In dealing with the above accounting issue, I demonstrated that I was objective in the information provided by the client and maintained integrity while we discussed the issue. Referring to the Charities SORP and obtaining confirmation from the ICAEW Technical Helpline meant that laws and regulation were upheld. I was confident in my technical knowledge and was not intimidated by the client's resistance to reflect the necessary adjustment within the financial statements.

Word count, excluding question titles and requirements: 403

6. FINANCIAL MANAGEMENT (15 MARKS)

6b.
- i) Describe one issue of financial management at a client;
- ii) Explain how you addressed the issue; and
- iii) Explain how this enabled you to add value to the client.

Spreading the risk of large cash balances

A mental health charity (income £1.6m, net assets £933k) was receiving payments from customers with large contracts, in advance of the provision of service. As a result, large cash balances (£983k) were being held within one bank account. The charity had grown significantly over a short period without several of the key policies being updated. I recommended that it consider the policy for holding large cash balances to ensure that they were secure and safeguarded for the charity's use.

The client contacted me to consider the recommendation further. I advised it to complete a risk assessment of holding cash, supplying the Charity Commission guidance on holding, moving and receiving funds safely in the UK and internationally.

Once the initial assessment had been completed, it was clear that the trustees felt that they wanted to diversify their cash balances. I suggested that they look into placing some funds into current accounts with immediate access and some into short-term deposits.

My suggestion was to ensure that sufficient cash balances were held to meet operational cash flows whilst also maximising the return on the surplus cash held. As well as this, I advised the client of the £85k that the Financial Conduct Authority protects under the Financial Services Compensation Scheme (FSCS).

On my advice, the client contacted a cash deposit platform that worked with it to distribute the cash balances between 17 banks and building societies authorised under the FSCS. The client then drafted an investment policy (approved by the finance committee) for holding cash balances, and an £85k limit in any approved account was established to protect the security of the charity funds.

This added value to the charity as it had to consider how to safeguard its assets better. The charity's governance was also enhanced with the formation of the finance committee, who now have more oversight of the finance function. The security of the assets has been enhanced through diversifying the cash balances into providers that participate in the FSCS. Finally, the charity is maximising its return in terms of interest on the assets that give a greater return.

Word count, excluding question titles and requirements: 356

TOTAL WORD COUNT, EXCLUDING QUESTION TITLES AND REQUIREMENTS: 2,467