

Invitation to Comment

Reporting matters of material significance to a UK charity regulator

Revised guidance for auditors and independent examiners

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Section 1

Key facts

Subject of consultation:	A proposed new list of material matters to be reported to the regulators by Auditors and Independent Examiners.
Scope of this consultation:	The invitation to comment sets out the proposed new list of material matters to be reported. It then asks a series of questions around the suitability of the matters and the wording of the matters. The results of the consultation will be used to agree the final list of matters to be reported by auditors and independent examiners to a UK charity regulator.
Who should read this consultation:	Auditors and Independent examiners and those interested in their reporting duties.
Period of consultation	The consultation runs for 16 weeks from 19 May to 11 September
Secretariat	Claire Morrison, OSCR. OSCR is acting on behalf of the UK charity regulators
How to respond to consultation:	By e mail matters@oscr.org.uk By post Claire Morrison OSCR 2nd Floor, Quadrant House, 9 Riverside Drive, Dundee DD1 4NY

Section 2

Foreword

Our shared goal as regulators is to have a charity sector in which the public have confidence and where charities can flourish. Our experience of regulation is that most charities operate within the legislation and provide invaluable services to their beneficiaries. There are however, as in every sector, some areas where regulatory intervention is required. We aim to ensure that all intervention is proportionate and targeted. Information from auditors and independent examiners is invaluable to us to undertake our work effectively.

Under legislation in England and Wales, Scotland and Northern Ireland, auditors and independent examiners have a duty to report certain matters to their respective charity regulators. Although the legislation varies in each jurisdiction the broad requirement is that where an auditor or independent examiner becomes aware of any matter, through the course of their work, which they believe is of material significance for the regulator in the exercise of their functions then this must be reported to the regulator.

The matters of material significance are not set out in the legislation or by way of regulation and it is therefore part of the role of the UK charity regulators to inform auditors and independent examiners of the matters which should be reported.

The Charity Commission for England and Wales (CCEW) and the Office of the Scottish Charity Regulator (OSCR) previously developed a single list of matters which was consistent for England and Wales and Scotland. We believe it is important to have a single list to simplify reporting requirements and ease the burden upon auditors or examiners acting for charities which work in multiple jurisdictions. It also means that guidance to auditors and independent examiners can be consistent across jurisdictions. With the establishment of the Charity Commission for Northern Ireland (CCNI) and also with the experience of regulation to date we believe it is appropriate to review the list of matters to be reported.

This Invitation to Comment (ITC) sets out the proposed list of matters to be reported. These build on our regulatory experiences, the types of matters which are reported and the areas of concern we see through our casework.

We would encourage all stakeholders to provide their views on the list of matters included in this ITC.



Laura Anderson
Head of Enforcement

OSCR



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Head of Accountancy
Services

CCEW



Myles McKeown
Head of Compliance and
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CCNI

Section 3

Background

3.1 Auditors and independent examiners have a duty to report significant matters which they discover through the course of their audit or examination work to the charity regulator in their jurisdiction.

3.2 In England and Wales, the Charities Act 2011 sets out this duty in section 156. There is a requirement for auditors and examiners who become aware of a matter which they believe would be of material significance to the Charity Commission in exercising certain of its inquiry functions, to immediately make a written report on the matter to the Commission.

3.3 In Scotland, the Charities and Trustee Investment (Scotland) Act 2005 sets out this duty in section 46. There is a requirement for auditors and examiners who become aware of a matter which they believe would be of material significance to OSCR in exercising its functions to immediately report the matter to OSCR.

3.4 In Northern Ireland, the Charities Act (Northern Ireland) 2008 sets out this duty in section 67. There is a requirement for auditors and examiners who become aware of a matter which they believe would be of material significance to the Commission in exercising its functions to immediately make a written report on the matter to the Commission.

3.5 There is no definition in legislation as to what constitutes a matter of material significance.

3.6 Previously the CCEW and OSCR issued a joint list of matters which they considered to be of material significance. This was done to aid the understanding of auditors and examiners of the matters which should be reported. The list was prepared jointly to ensure consistency.

3.7 As the Charity Commission for Northern Ireland (CCNI) is now in place and charity law in Northern Ireland has requirements in this area similar to those in England and Wales and in Scotland, the three regulators agreed it would be beneficial to harmonise reporting requirements and update the list of matters to cover all three jurisdictions.

3.8 Some time has passed since the original list was developed and it was agreed by CCEW, OSCR and CCNI that it would be beneficial to review the list of matters in light of developing themes and also regulatory experience.

3.9 The list of matters proposed in this Invitation to Comment document have been agreed by all three charity regulators as matters which they would consider material and therefore must be reported.

Section 4

Proposed matters of material significance

4.1 The proposed matters of material significance are displayed in the table below. The current matters are shown together with the proposed amendments and the rationale for change.

	Current list	Proposed amendments, additions and deletions	Comments
1	Matters suggesting dishonesty or fraud involving a significant loss of, or a major risk to, charitable funds or assets	Matters suggesting dishonesty or fraud involving a material loss of, or a material risk to, charitable funds or assets	'Significant' is changed to 'material' to align with the terminology used in SORP
2	Failure(s) of internal controls, including failure(s) in charity governance that resulted in a significant loss or misappropriation of charitable funds, or which leads to significant charitable funds being put at major risk	Failure(s) of internal controls, including failure(s) in charity governance that resulted in, or could give rise to, a material loss or misappropriation of charitable funds, or which leads to material charitable funds being put at major risk.	To align terminology to that used in the SORP
3	Matters leading to the knowledge or suspicion that the charity or charitable funds have been used for money laundering or such funds are the proceeds of serious organised crime or that the charity is a conduit for criminal activity	During the audit/independent examination knowledge or suspicion that the charity or charitable funds or the charity's bank account(s) have been used for money laundering or such funds are the proceeds of serious organised crime or that the charity is a conduit for criminal activity	Adding in section about bank account as there have been instances of charities allowing others to use their bank account to move money

<p>4</p> <p>Matters leading to belief or suspicion that the charity, its trustees, employees or assets, have been involved in or used to support terrorism or proscribed organisations in the UK or outside of the UK</p>	<p>Matters leading to the knowledge or suspicion that the charity, its trustees, employees or assets, have been involved in or used to support terrorism or proscribed organisations in the UK or outside of the UK, with the exception of matters related to a qualifying offence as defined by Section 3(7) of the Northern Ireland (Sentences) Act 1998</p>	<p>Small update to change the word ‘belief’ to ‘knowledge’. Update to include specific references in respect of Northern Ireland. This change is intended to negate the need to report qualifying offences that occurred prior to 1998 in relation to the Northern Ireland conflict.</p>
<p>5</p> <p>Evidence suggesting that in the way the charity carries out its work relating to the care and welfare of beneficiaries, the charity’s beneficiaries have been or were put at significant risk of abuse or mistreatment</p>	<p>During the audit/independent examination evidence suggesting that in the way the charity carries out its work relating to the care and welfare of beneficiaries, the charity’s beneficiaries have been or were put at significant risk of abuse or mistreatment</p>	<p>Amended to clarify that the evidence would be obtained during the audit/independent examination</p>
<p>6</p> <p>Significant or recurring breach(es) of either a legislative requirement or of the charity’s trusts</p>	<p>Single or recurring breach(es) of either a legislative requirement or of the charity’s trusts leading to material charitable funds being misapplied</p>	<p>Text amended to clarify that it is material breaches which must be reported, and that this may be in the form of a single or recurring breach.</p>
<p>7</p> <p>A deliberate or significant breach of an order or direction made by a charity regulator under statutory powers including suspending a charity trustee, prohibiting a particular transaction or activity or granting consent on particular terms involving significant charitable assets or liabilities</p>	<p>During the audit/independent examination evidence suggesting a deliberate or significant breach of an order or direction made by a charity regulator under statutory powers including suspending a charity trustee, prohibiting a particular transaction or activity or granting consent on particular terms involving significant charitable assets or liabilities</p>	<p>Amended to clarify that the evidence would be obtained during the audit/independent examination</p>

8	<p>Any notification or matter reported to the trustees on resigning as independent examiner or matter that the examiner is aware of on resignation or ceasing to act that falls within the categories of the previously set out reportable matters, or for examiners the notification on ceasing to hold office or resigning from office, of those matters reported to trustees</p>	<p>It is suggested that this matter is removed as it was misinterpreted leading to auditors and examiners simply notifying the Regulator when they had ceased to hold office due to a change in appointment.</p>
9	<p>On making a modified audit opinion, emphasis of matter, or issuing of a qualified independent examiner's report identifying matters of concern to which attention is drawn, notification of the nature of the modification/qualification/emphasis of matter or concern with supporting reasons including notification of the action taken, if any, by the trustees subsequent to that audit opinion/examiner's report</p>	<p>This is introduced to ensure that issues identified in the audit/examiner's report are separately highlighted to the Regulator so that timely regulatory action can be taken if appropriate. This ensures that Regulators can respond to these issues as soon as notification is received and also that Auditors/Examiners are fully aware that this is a separate duty.</p>

10	Evidence that, without reasonable cause, trustees have not taken action on matters identified by the auditor or examiner in their scrutiny of accounts for a previous year	Auditors normally and examiners can choose to issue management letters. These can highlight areas of weakness in financial controls or governance. These issuing of a management letter of itself is not reportable but if the trustees fail to act upon the recommendations this may be more significant.
11	During the audit/independent examination evidence that conflicts of interest have not been managed by the trustees in accordance with guidance issued by the charity regulator and/or related party transactions have not been fully disclosed in all the respects required by the applicable SORP.	Unauthorised private benefit or incomplete disclosure of related party transactions damages public trust and confidence and leaves charity assets open to the risk of misappropriation.

4.2 Definitions

Where reference is made to 'SORP', this refers to the applicable Statement of Recommended Practice: Accounting and Reporting by Charities. In all three charity law jurisdictions adherence to the SORP is necessary for accounts prepared on an accruals basis to give a 'true and fair' view. The SORP also sets out reporting requirements for charities and defines accounting terms applicable to the preparation of accounts by charities. The SORP identifies the requirements that have to be followed to comply with the SORP by use of the term 'must'.

During the audit/ independent examination refers to the stages from initial engagement, preparation and planning, the undertaking of the audit/independent examination, and the giving of the audit opinion/examiner's report and the issuing of any management letter and presentation to the charity trustees as to the findings of the audit/ independent examination or alternatively up to the point of the resignation of the auditor/ independent examiner from the audit/ independent examination.

Section 5

Summary of key changes

The proposed changes will mean we have increased the matters of material significance from eight to ten in England and Wales and Scotland. It is important to note that this is not intended to require the auditor or independent examiner to report matters that they would not reasonably be expected to come across during the audit/ independent examination and the additional items added are intended to help auditors and independent examiners meet their duties.

The new matters are areas where regulators have an interest and where it has been found that reports are not always made or in the case of a modified audit opinion or qualified independent examination report it provides early notification of the matter ensuring a more timely intervention. It is hoped that by including these extra matters auditors and independent examiners will be clearer in the areas they should be reporting.

The full list of matters of material significance is a new requirement for auditors and independent examiners in Northern Ireland.

Section 6

Regulatory burden

The UK charity regulators are keen to understand to what extent, if any, the proposed list of matters of material significance may give rise to additional time and effort or incur significant additional cost. There is a balance to be struck between requiring additional reporting to enable more effective regulatory action and the potential reporting burden.

In developing the proposed list of matters, the UK charity regulators have considered what matters the auditor or independent examiner will come across during their assignment and the existing reporting duties and disclosure requirements. Our assumption is that requiring the separate reporting of matters that the auditor/ independent examiner would normally come across in any event means that any reporting burden is kept to a minimum.

Section 7

Consultation

7.1 All three charity regulators are interested in your views. In summary we are seeking your views on:

- whether the matters outlined are the correct matters which should be reported to us,
- the descriptions of the matters – are they clear and helpful?
- whether there are any other matters which should be included, or indeed any matters which should be removed, and if so, why?

In addition, each of the UK charity regulators is considering issuing more general guidance for auditors and independent examiners when reporting a matter of material significance to the charity regulator. This guidance would be intended to help both auditors and independent examiners better understand their duties with regard to the UK charity regulators.

Section 8

Consultation questions

8.1 We welcome comments on any aspect of the Invitation to Comment, in particular

Q.1 The list of material matters of significance which must be reported was developed to aid auditors and independent examiners in understanding their duties under the legislation. Do you agree that it is useful to have a list of matters which must be reported? If not, what means do you suggest of helping auditors and independent examiners meet their statutory duty to report?

Q.2 Do you agree that the descriptions of the matters to be reported are clear and helpful? If not please advise where further clarity is required.

Q.3 The terminology in Matters 1 and 2 has been amended to agree to that used in the Statement of Recommended Practice for Charities (SORP), do you agree that this is helpful for consistency? If not please advise what terminology you would recommend and why?

- Q.4** Matter 3 has been expanded to specifically include the charity's bank account in the areas where funds could be used for money laundering. This is based upon our experiences where the charity's bank account has been used to move money. Do you agree that the expanded definition is helpful? If not please advise what alternative definition you would use.
- Q.5** Matter 4 is now applicable to Northern Ireland and has been expanded to exclude the need to report any matters that were related to a qualifying offence as defined by Section 3(7) of the Northern Ireland (Sentences) Act 1998. Do you agree that the matter should be expanded in this way? Do you consider that the proposed wording is appropriate? If not please explain your answer and advise what alternative wording you would use.
- Q.6** Matter 8 from the previous list of matters to be reported has been removed. This is due to the fact that this led to auditors and independent examiners advising the Regulator where they had simply ceased to hold office. Where ceasing to hold office occurs due to a reportable matter this should be covered by an alternative matter. Do you agree that this matter should be removed? If not please advise why it should be retained?
- Q.7** Matter 9 has been introduced to ensure that auditors and independent examiners report to the charity regulator as soon as they issue a modified audit opinion (including any emphasis of matter) or qualify their independent examiner's report and notify the regulator . Separate notification enables the matter to be considered for regulatory action and avoids any delay arising from awaiting the filing of the charity's accounts. This will be useful to the regulators as there have been a number of instances where matters have not been reported separately but simply included when the auditor's or examiner's report is qualified. Do you agree that the inclusion of this within the matters of material significance will assist auditors and independent examiners? Please give your reasons for this response.
- Q.8** Auditors regularly offer guidance and areas for improvement to their clients. We recognise the important role this plays in ensuring charities meet their regulatory requirements. Where charities fail to act upon the recommendations made by their advisors this may be an indication of governance concerns and should be reported to the regulator. Do you agree that this matter should be included as a reportable matter? If not please provide your reasons for this.

Q.9 It is important for public trust in charities to ensure that all relationships are properly managed in accordance with charity law and where required disclosed in order to maintain public trust and confidence. Matter 11 highlights the need for auditors and independent examiners to report to us where they believe that relationships are not managed well or are not correctly highlighted to users of the accounts. Do you agree that this should be included as a matter of material significance? If not, please provide your reasons why.

Q.10 While the reporting requirements have not changed significantly we have increased the areas identified as matters of material significance to provide clarification for those with reporting responsibilities. Do you agree that this aids clarification and is not a significant increase in regulatory burden? If not please provide your reasons for this.

Q.11 In addition to the matters identified as reportable, we have received feedback that some further guidance around reporting requirements, including more practical examples of reporting matters of material significance would be useful. Do you agree that further guidance in this area is required and if so should this be provided by the regulators and/ or included in auditing standards?

8.2 In your response, please say what kind of organisation you are involved with or responding on behalf of, and what your role is as this will help us to understand the context of your comments.

8.3 Your comments will help shape the final list of matters of material significance to be reported. They may also be used to consider further guidance requirements in this area.

Section 9

How to respond to the consultation

9.1 The consultation will run for just over 3 months with a closing date of 11 September 2016.

9.2 There are two ways to respond to this consultation:

E mail:

Submit your response to matters@oscr.org.uk

Post

Send a written response to:

Claire Morrison
OSCR
2nd Floor, Quadrant House,
9 Riverside Drive,
Dundee DD1 4NY

If you have any questions about the consultation, please e mail them to matters@oscr.org.uk

Section 10

Data Protection

10.1 All information contained in the consultation responses (including personal information) may be published or disclosed in accordance with the access to information regime. This is primarily set out in the Freedom of Information Act 2000 (FOIA), Freedom of Information Act (Scotland) 2002, Data Protection Act 1998 and Environmental Information Regulations 2004.

10.2 We can only treat information in your consultation response as confidential if that's consistent with the law. There is a statutory Code of Practice under the FOIA and under the FOISA which public authorities must comply with. This sets out how confidential information must be dealt with. We can't give assurances that all information will be kept confidential, but we will take into account any representations that you make.

10.3 If you object to any information in your consultation response (including your personal details) being published, please say so. Please explain why you think the information should be confidential. This will help us to decide whether there are grounds for not publishing it.