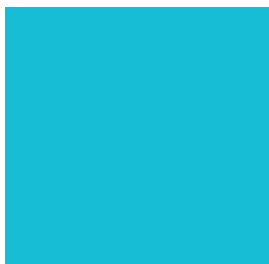
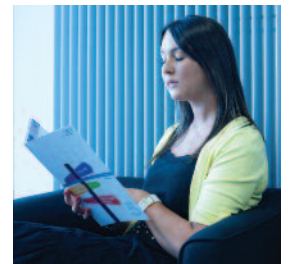


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OSCR Guidance for Charities  
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**acie**  
association  
of charity  
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examiners

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## 1. Introduction

In Scotland, more than two thirds of charities are ‘small’ – that is, they have an annual income of less than £25,000. OSCR recognises that it can sometimes be challenging for such charities to understand and comply with formal requirements and therefore publishes specific guidance to assist and support the small charity. This guidance booklet aims to be a comprehensive package, providing information and practical guidance on both the preparation of accounts and external scrutiny and is designed particularly for smaller charities although a number of best practice elements are also applicable to larger charities.

All Scottish charities are required to prepare annual accounts. These consist of numerical information and also a Trustees’ Annual Report which is narrative information providing details that cannot be expressed in financial terms. This is important for a full understanding of the charity, its purpose and the activities that it carries out in seeking to achieve this. It is often the case that readers of the accounts who are not familiar or confident with numerical data will find the Trustees’ Annual Report an invaluable source of information.

A charity’s accounts are a means of communication that the charity can use to its own advantage. Anyone who has ever given time or money to a charity will have an interest in understanding how the charity uses that money.

OSCR has already published specific guidance on how to prepare accounts – this can be found in two publications which are available from the OSCR website at **[www.oscr.org.uk](http://www.oscr.org.uk)**:

- Scottish Charity Accounts: A Guide to the 2006 Regulations
- Scottish Charity Accounts: OSCR Receipts and Payments Accounting Workpack

Under statutory requirements, the accounts of Scottish charities must also be externally scrutinised. That is, someone who is independent of the charity has reviewed the accounts and produced a report, attached to the accounts, that highlights any issues to the reader. As such, external scrutiny is an important component of the overall regulation of charities in Scotland, a scheme designed to ensure transparency and public accountability by charities.

This guidance booklet is about independent examination, which is one of the two forms of external scrutiny that may be carried out under the statutory provisions in Scotland, and is particularly appropriate for smaller charities. It aims to explain, in broad terms:

- how to understand what form of external scrutiny is applicable to different charities
- what independent examination involves
- what responsibilities and duties are attached to the role of the independent examiner.

## 2. How to use this guidance

This guidance has been developed specifically for use in relation to Scottish charities and is designed to be of use to the following groups:

- charity trustees
- individuals already acting as independent examiners
- individuals who have been approached to act as independent examiners
- third parties with an interest in charity accounts.

Charity trustees need to understand:

- when an independent examination is required
- what independent examination actually involves
- what an independent examiner's report means.

Third parties with an interest in charity accounts are likely to need to be aware of these key aspects as well, although they would be expected to take a slightly different interest from that of a person within a charity.

Individuals who are acting as independent examiners, or have been approached to do so, need to have a good understanding of:

- who can act as an independent examiner
- what independent examination actually involves – this will involve greater detail and depth of knowledge than required by charity trustees
- how to draft an independent examiner's report, what the report means and how to report on any other matters to OSCR.

This guidance document covers each of the key areas outlined above and also provides example reports for independent examiners to use in various situations. The document has been written with a view to enabling everyone to understand the requirements and best practice procedures.

In order to make this guidance document user friendly, there are specific sections of the document that are written with particular groups in mind, while others are more widely applicable.

Each section is clearly marked at the start with the relevant interest group. Where a section is marked as being particularly relevant for independent examiners, it should also be read by individuals who are approached to act in such a capacity to ensure they are fully aware of what independent examination entails. We would encourage users of the document to read the other sections where relevant. Independent examiners are strongly recommended to read all of this guidance.

The following terms, in particular, are used throughout this guidance:

The '2005 Act' means the Charities and Trustee Investment (Scotland) Act 2005.

The '2006 Regulations' means The Charities Accounts (Scotland) Regulations 2006 (as amended).

The 'SORP' means Accounting and Reporting by Charities: Statement of Recommended Practice 2005 (second edition).

There is a full glossary of terms used in this guidance booklet at Appendix 6.

Within the guidance, we have posed some 'milestone' questions for the reader. These are designed to help indicate where it is time to make a particular decision. We have provided some answers to these questions where this may be useful and in some cases we have provided some practical tips. Hopefully you will find these helpful as you progress through the guidance.

### 3. Types of external scrutiny

#### 3.1 What is independent examination? **For all interest groups**

Independent examination is one of the two forms of external scrutiny that may be carried out under the statutory provisions in Scotland. Broadly speaking, an independent examination involves reviewing the accounting records and the annual accounts of the charity and considering whether the annual accounts are a fair reflection of the underlying records. When carried out properly, an independent examination provides a degree of comfort that the figures in the accounts, including the Trustees' Annual Report, present an accurate picture of the financial activity of the charity during the accounting period.

Also involved in the process is consideration of any unusual items in the accounts that may require further discussion or explanation from the charity trustees. The independent examination seeks to ensure that the charity's accounts, including the Trustees' Annual Report, fulfil the requirements of the 2006 Regulations and adequately reflect the operations of the organisation for the period concerned.

#### 3.2 Independent examination versus audit **For all interest groups**

An independent examination is a form of external scrutiny which:

- offers an assurance that nothing has been found that needs to be brought to the attention of readers of the accounts
- is less rigorous than an audit
- is less costly than an audit.

The independent examiner's report is prepared on an 'exception' basis. This means that there is an assumption that the examiner is content with the accounting records and accounts unless they specifically state otherwise. The report is intended to be simpler than an audit and no opinion is expressed on the accounts.

In contrast, an auditor is required to build up a body of evidence and express an opinion on the accounts. The opinion given in an audit depends on the nature of the accounts that have been prepared.

- If receipts and payments accounts have been prepared, the opinion will state whether or not the accounts 'properly present' the receipts and payments for the charity for the financial year. In practice, OSCR expects very few charities preparing receipts and payments accounts to have an audit.
- If fully accrued accounts have been prepared, the opinion will state whether the accounts provide a 'true and fair view' of the financial affairs of the charity.

Historically, the term 'audit' has been used loosely to describe any external scrutiny of accounts, although since 1990 it has had a more specific meaning. Under the 2006 Regulations, if the term 'audit' is used in a charity's constitution or governing document, the charity must have its accounts audited by either:

- a registered auditor
- the Auditor General for Scotland
- an auditor appointed by the Accounts Commission for Scotland (responsible principally for public bodies).

Audits are more commonly required for larger charities, although smaller charities may also require an audit. It is possible that the governing document of the charity may contain specific terms requiring the accounts to be audited or referring to an 'auditor'. In such a situation, the charity is required to have its accounts audited as stated above. An independent examination would not be acceptable in such cases. In other situations, 'audit' may be instructed because that has been the custom in the past.

### **Milestone 1 –**

- **Does the governing document of the charity require an audit to be carried out rather than an independent examination?**

**OR**

- **Is it simply custom and practice for the charity to have its accounts audited?**

If the answer to either of these questions is yes, the charity trustees may wish to pause and consider their options:

- if the governing document contains a requirement for audit, the charity trustees may wish to consider changing the governing document
- where it has simply been custom and practice for the accounts to be audited, the charity trustees can adopt a different policy and elect instead for an independent examination
- in any event, it may be worthwhile for the charity trustees to contact funders to determine whether an audit is really required or whether independent examination is adequate. The charity trustees may wish to consider whether any trading issues or related parties necessitate an audit being carried out
- if the charity trustees *choose* to have the accounts audited, this may have a cost implication.

### 3.3 Changing the governing document **For charity trustees**

The governing document of a charity may take many forms including a 'Constitution', 'Memorandum and Articles of Association', 'Trust Deed' etc.

Where the governing document contains either:

- a requirement to prepare fully accrued accounts regardless of the level of income (non-company charities)
- a requirement for audit.

then the charity trustees may wish to consider whether these provisions are still necessary, or whether they might wish to change their governing document.

Charity trustees should note that changes can only be made where the governing document provides the necessary power for the charity trustees to make such a change. If there is no such power within the governing document, the charity trustees would have to use the charity reorganisation provisions within the 2005 Act. For further information on the reorganisation provisions and notification of changes to the governing document, please refer to OSCR's Charity Reorganisation Guidance and Consents and Notifications Guidance, as applicable. These may be downloaded from the OSCR website at **[www.oscr.org.uk](http://www.oscr.org.uk)**

## 4. Eligibility for independent examination **For all interest groups**

In Scotland, the formal requirements for accounts and external scrutiny are contained within the 2005 Act and the 2006 Regulations. The requirements differ depending on the constitutional form of the charity, the level of the charity's income and also any relevant provisions contained within the charity's governing document.

This section looks at the relevant factors and explains how to understand what the required form of external scrutiny is for a charity.

### 4.1 Form of accounts

Table 1 below sets out the formal requirements under the 2006 Regulations for the form of accounts to be prepared by Scottish charities.

**Table 1: Format of accounts**

| <b>Gross income</b>               | <b>Format of accounts<sup>(2)</sup></b>                                      |   |
|-----------------------------------|--|---|
| Less than £250,000 <sup>(1)</sup> | Non-company charities:<br>receipts and payments accounts<br>(See Appendix 2) | Charitable companies:<br>fully accrued accounts<br>(See Appendix 3) |
| £250,000 and over                 | Fully accrued accounts<br>(See Appendix 3)                                   |   |

(1) Less than £100,000 for periods commencing before 1 April 2011.

(2) Preparers of accounts also need to consider any relevant requirements of the charity's governing document in understanding the format of accounts to be prepared – there may be provision requiring accrued accounts to be prepared for example which would overrule the above threshold requirements.

#### *Receipts and payments accounts*

Non-company charities with gross income of less than £250,000 (£100,000 for accounting periods starting before 1 April 2011) will normally prepare a simple form of accounts called 'Receipts and Payments Accounts'. These are much easier to compile than fully accrued accounts as they simply provide basic information regarding the money that has come into and been paid out by the charity. Therefore, an individual does not need to be professionally qualified to undertake the role of independent examiner for these accounts.

However, where an audit of receipts and payments accounts is required as a result of a requirement in the governing document, a decision of the charity trustees or any other enactment, a qualified auditor will be required. (See section 3.3)

Trustees of charities that are eligible to prepare receipts and payments accounts may *choose* to prepare fully accrued accounts instead. However, they should be aware that such accounts will require to be examined by a qualified independent examiner, which may have a cost implication for the charity.

### *Fully accrued accounts*

Charitable companies are *always* required to prepare fully accrued accounts. They do not have the option of preparing receipts and payments accounts. This is as a result of company law requiring such bodies to prepare accounts that are ‘true and fair’.

Non-company charities with gross income of £250,000 ((£100,000 for accounting periods starting before 1 April 2011) or above must also prepare fully accrued accounts.

Where fully accrued accounts are prepared, they must be prepared under the methods and principles of the SORP. The external scrutiny of fully accrued accounts must be carried out by an individual who is professionally qualified to understand such accounts as they can be complex in comparison to receipts and payments accounts.

### *Further information*

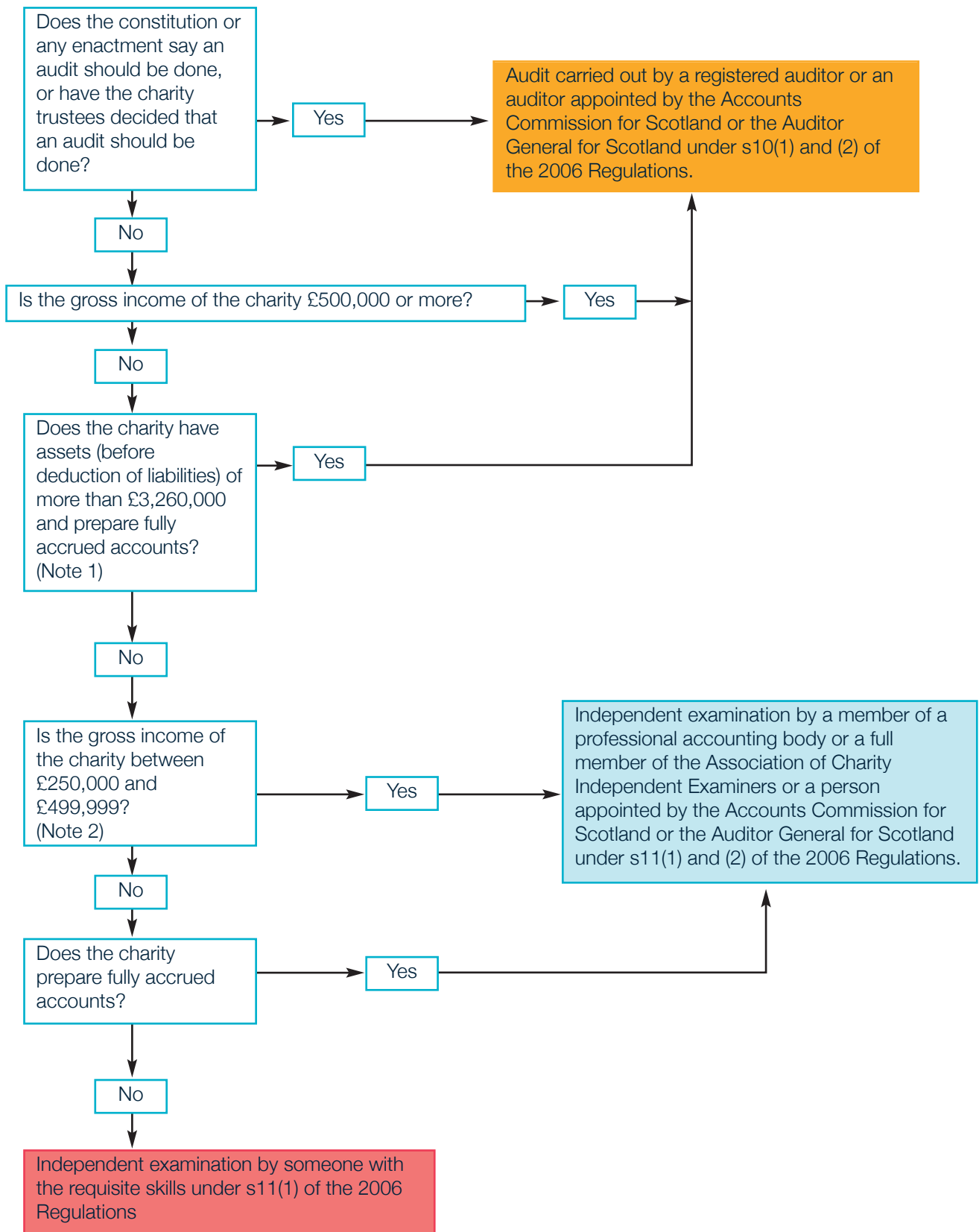
More detailed information on the preparation of accounts and the relevant requirements can be found within OSCR’s Accounts Guidance (Scottish Charity Accounts – an updated guide to the 2006 Regulations) which is available on the OSCR website. There is further information at Appendix 1 (summary of requirements), Appendix 2 (receipts and payments accounts) and Appendix 3 (fully accrued accounts) of this guidance.

## **4.2 External scrutiny criteria**

As a result of different forms of accounts being permitted under the 2006 Regulations, there are corresponding differences in the type of external scrutiny that is required.

Figures 1 and 2 provide a step by step guide to understanding the appropriate form of external scrutiny for Scottish charities. Note that there are different steps depending on whether the charity is a company or not.

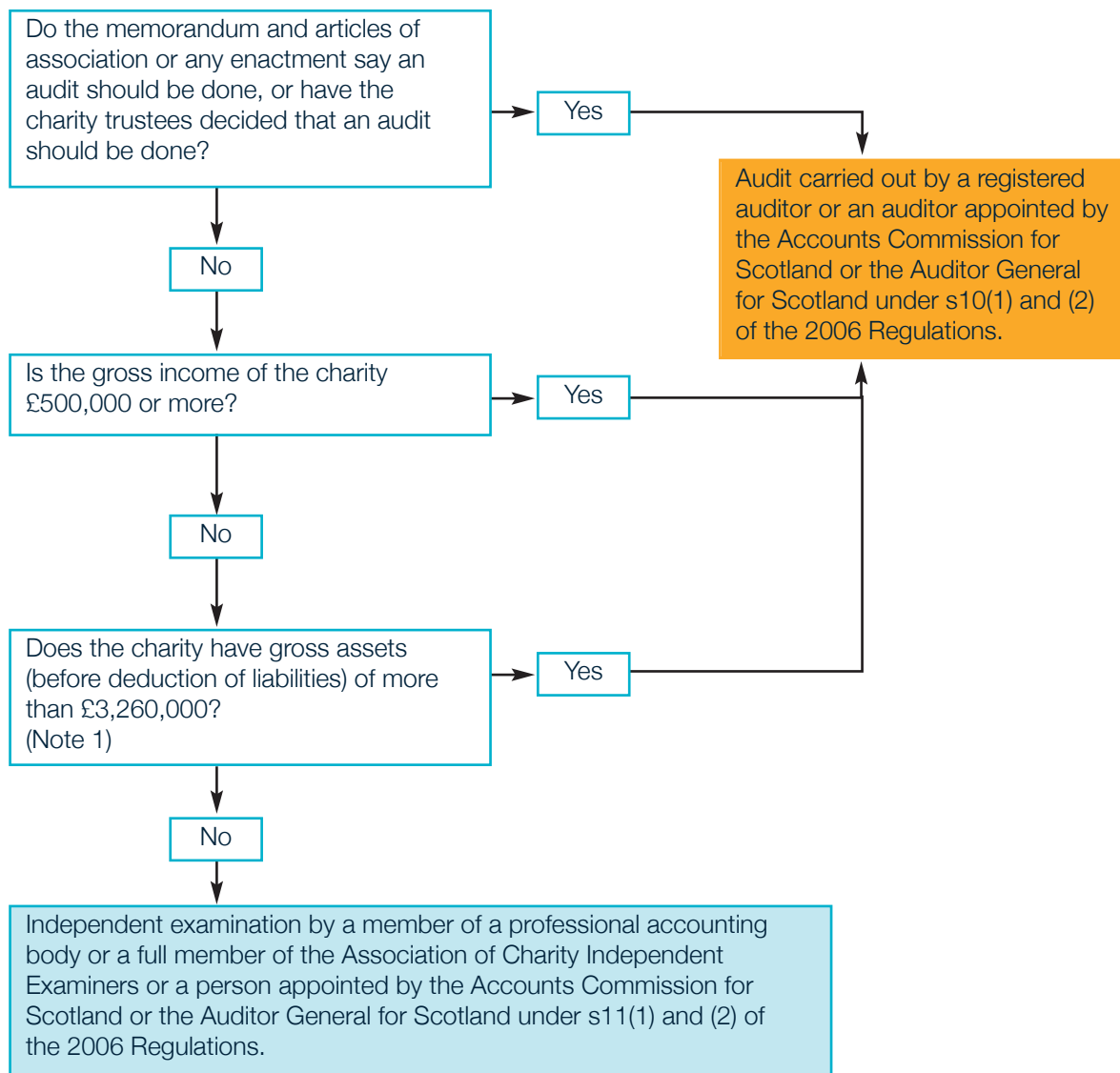
**Figure 1: External scrutiny for charities that are not companies**



Note 1: assets of more than £2,800,000 for periods starting before 1 April 2011.

Note 2: income between £100,000 and £499,999 for periods starting before 1 April 2011.

**Figure 2: External scrutiny for charitable companies – applicable for accounting periods starting on or after 1 April 2008\***



\*The above flowchart should only be used to understand the external scrutiny requirements for charitable companies preparing accounts for periods starting on or after 1 April 2008. For earlier accounting periods, reference should be made to the requirements under the Companies Act 1985 as outlined in OSCR's Accounts Guidance.

Note 1: £2,800,000 for periods commencing before 1 April 2011.

Figures 1 and 2 show that there are different forms of independent examination depending on the form of accounts being produced by a charity. In the next section we will look at these differences to provide a better understanding of the relevant underlying principles and how this affects the process of the independent examination.

## Milestone 2 –

### Is it clear whether receipts and payments accounts or fully accrued accounts should be prepared?

- If it is still unclear which type of accounts should be prepared, please refer to our accounting guidance.
- If receipts and payments accounts are to be prepared, you may wish to use our Receipts and Payments Workpack.
- The accounting guidance and Receipts and Payments Workpack can both be downloaded from the OSCR website at **[www.oscr.org.uk](http://www.oscr.org.uk)**
- If fully accrued accounts are to be prepared, the SORP is also available to download from the links page on our website at **[www.oscr.org.uk](http://www.oscr.org.uk)**

## 5. Who can act as an independent examiner?

### For charity trustees and independent examiners

Section 4 outlines the criteria for determining whether or not a charity is eligible to have its accounts independently examined. This section explains the different requirements for the individual acting as an examiner depending on the form of accounts being prepared by the charity.

Charity trustees should always bear in mind that they have an important responsibility when appointing an independent examiner.

- Where receipts and payments accounts are prepared, the examiner should be someone who they believe is able to carry out an independent examination in line with the relevant requirements. The trustees should satisfy themselves that the person appointed has the necessary skills to be able to carry out the engagement which may depend on the complexity of the charity's operations and its accounts.
- Where fully accrued accounts are prepared, the examiner should be someone who is professionally qualified to undertake the role.

### 5.1 Receipts and payments accounts

Receipts and payments accounts are a simple form of accounting that broadly consists of a summary of all monies received and paid by the charity during its financial year, along with a statement of balances at the year end.

Under the 2006 Regulations, receipts and payments accounts must consist of:

- a Trustees' Annual Report
- a Statement of Receipts and Payments
- a Statement of Balances as at the last day of the financial year
- notes to the accounts.

**Plus** a report from an independent examiner or auditor.

The independent examination of receipts and payments accounts must be carried out by someone independent of the management and administration of the charity and whom the charity trustees believe has the required skills and experience to carry out a competent examination of the accounts.

In deciding who might have the required skills, the charity trustees should take into consideration the degree of complexity of the accounts. The more complex the accounts are, the higher the level of experience and knowledge likely to be required by the independent examiner.

The types of people whom charity trustees could consider as having the required skills and experience might include:

- full or associate members of the Association of Charity Independent Examiners
- qualified accountants currently in employment
- retired accountants
- other people familiar with financial matters who can demonstrate familiarity with the current reporting requirements for Scottish charities.

## 5.2 Fully accrued accounts

Under the 2006 Regulations, fully accrued accounts must consist of:

- a Trustees' Annual Report
- a Statement of Financial Activities (SoFA)
- a Balance Sheet as at the last day of the financial year
- notes to the accounts.

**Plus** a report from an independent examiner or auditor.

For charities producing fully accrued accounts, the independent examination must be carried out by an individual who is appropriately qualified in matters of accounting and financial administration on the basis that the accounts to be examined are more complex.

The 2006 Regulations specify that the independent examiner **must** be one of the following individuals:

### **Either:**

- a member of one of the following professional bodies:
  - The Institute of Chartered Accountants of Scotland
  - The Institute of Chartered Accountants in England and Wales
  - The Institute of Chartered Accountants in Ireland
  - The Association of Chartered Certified Accountants
  - The Association of Authorised Public Accountants
  - The Association of Accounting Technicians
  - The Association of International Accountants
  - The Chartered Institute of Management Accountants
  - The Institute of Chartered Secretaries and Administrators
  - The Chartered Institute of Public Finance and Accountancy.

### **Or**

- a full member of the Association of Charity Independent Examiners

### **Or**

- a person appointed by the Accounts Commission for Scotland

### **Or**

- the Auditor General for Scotland.

### 5.3 Independence

It is critical that an independent examination is carried out by someone who is independent of the charity, and seen to be so. Independence is not possible if you are:

- one of the charity's trustees
- anyone else involved in the management, control or administration of the charity, which usually means being a senior employee of the charity. However, there are also occasions where a volunteer (other than a trustee) also has a key role and so would not be independent.

Given that independent examination is about the charity's finances, there are certain people within a charity who are particularly likely to be asked *inappropriately* to take on the role of examiner. These include the charity's treasurer or book-keeper who keep the day to day records from which the formal accounts are prepared. This is because, if they carried out the independent examination, they would end up checking the integrity of their own work.

However, independence can also be compromised by being 'connected' to the charity. Such a connection can arise because of:

- a family relationship. For example, you may be the parent or child of a trustee or senior employee.
- a financial or commercial relationship. For example, you represent a body which funds the charity or the charity contracts with you to provide it with certain services other than independent examination.

Where the connection is financial or commercial:

- the connection is only relevant if it is significant to the charity's operations. For example, the person providing the window cleaning service at a charity shop is probably not connected in a significant way, whereas the landlord of the shop premises probably is.
- the connection is not only about any individual relationship, it is also about the organisation or business that you work for. In this case, if you work for a firm or body which has a significant contractual relationship with the charity (or, indeed, are a partner of such a body), it is likely that you will not be independent.

If there is a connection, it may be possible to put arrangements in place within an organisation or firm so that there is sufficient distance between those managing any contractual relationship and the person carrying out the independent examination. These are often referred to as 'Chinese Walls'. The arrangements need to be thought through and planned very carefully. They should not simply pay lip-service to the concept of independence and all parties should be satisfied that they address the issue adequately.

Particular groups who need to give this aspect of independence special consideration are those who act for the charity as accountants or financial advisors and/or who prepare the charity's formal accounts. Again, there is scope for arrangements to be put in place to safeguard independence, but these must be considered carefully in advance. To protect independence in such a case, the basic underlying principle is that any person involved in keeping the underlying accounting records for the charity i.e. providing bookkeeping services or involved in the administration of the charity should not be involved in providing independent examination services to the same charity.

See also the Glossary of terms – 'connected persons'

## 6. How to select and appoint an independent examiner

This section assumes that an audit is not required (refer to section 4.2 for the relevant criteria for determining what method of external scrutiny is required).

### 6.1 Selection of an independent examiner – formal requirements **For charity trustees**

The selection of a good independent examiner is important for a charity in fulfilling its regulatory requirements. However, the selection process is likely to be influenced by the individual charity's circumstances and operations. In this section, a number of different areas are outlined for consideration by charity trustees in selecting an examiner; the detail within each may differ between charities depending on individual circumstances. It is recommended that charity trustees consider the selection of an independent examiner at the earliest possible opportunity and do not leave such a decision until the time when the accounts are prepared.

In selecting an examiner, charity trustees should:

- determine the form of accounts to be prepared by the charity
  - Is the charity eligible to prepare receipts and payments accounts?
  - Are fully accrued accounts required?
- understand the required form of independent examination
  - Where receipts and payments accounts are prepared, the examiner needs to be a person with the required skills to carry out a competent examination
  - If fully accrued accounts are prepared, the examiner must be a professionally qualified person.
- determine what skills are needed
  - Charity trustees should always bear in mind that it is their responsibility to ensure that the accounts are prepared and externally scrutinised in line with the statutory requirements. Therefore, they should satisfy themselves that they understand these requirements and are aware of the skills that the examiner will need to carry out their duties. This may relate to the complexity of the charity's accounts or its operations. For example, if the charity engages in specialist activities, it may be advantageous for the examiner to have some relevant knowledge in that area so that they may understand the nature and type of transactions being entered into by the charity.
- consider independence requirements
  - As outlined in section 5.3, there are various aspects to consider in terms of independence of the examiner from the management and control of the administration of the charity – these should be carefully thought about by the charity trustees.

Charities may feel that they are unable to find someone willing to take on the role of independent examiner, particularly if they are seeking the service for free. However, it is important for charity trustees, and the general public, to understand the value of the work of the independent examiner and therefore to recognise that this may have a legitimate cost implication for the charity. The use of charitable funds for payment of reasonable independent examination fees is acceptable. This is an integral element of expenditure that is often necessary to ensure that the charity complies with the relevant legal requirements and is transparent and accountable to the public. Such costs would be categorised as ‘governance costs’ within the charity’s accounts.

Many charities also use their independent examiner to put their accounts in the statutory format in addition to carrying out the independent examination. However, charity trustees using OSCR’s Receipts & Payments Workpack may be able to prepare the accounts themselves, leaving the independent examiner to carry out only the external scrutiny. This could help to reduce costs, particularly for smaller charities.

## **6.2 Selection of an independent examiner – practical considerations**

### **For charity trustees**

As part of the selection process, the charity trustees may wish to use the following questions as a guide to assessing whether the person seeking appointment has the appropriate skills and abilities to carry out the relevant duties.

- Can we see a set of charity accounts that you have previously examined and were submitted to OSCR?
- How many Scottish charities do you act for?
- Are you familiar with OSCR’s Receipts and Payments Workpack? (receipts and payments accounts).
- Are you familiar with the Charities SORP 2005? (fully accrued accounts).
- Which professional body are you registered with and what level of membership do you hold? (qualified independent examiner).
- Have you checked with your professional body that you are eligible to carry out the examination? (qualified independent examiner).

## Milestone 3 –

### Who should be our independent examiner?

#### 6.3 Accepting appointment as an independent examiner **For independent examiners**

Where an individual is approached to act as an independent examiner, they should ensure that they have the necessary knowledge of the 2005 Act, the 2006 Regulations, the SORP (if appropriate) and the charity itself to be able to carry out the examination.

They should also ensure that they comply with any relevant requirements of, or guidance issued by, any professional bodies of which they are a member, before accepting such an engagement. Individuals who hold membership of one of the professional bodies listed in section 5.2 should ensure that the status/level of their membership permits them to act as independent examiner of the accounts for the charity concerned.

Where an individual is a member of more than one professional body, compliance with the relevant requirements and guidance issued by all of those bodies should be ensured. They must have regard to the rules of the stricter body and not undertake an independent examination outwith those limits.

Where an individual has been asked to take on the role of independent examiner and there has been a previous examiner, there should be some form of correspondence between the previous and new examiner to ensure a smooth handover between them. This also allows any issues that may have been a factor in the previous examiner ceasing to hold office to be brought to the new examiner's attention.

The new examiner may consider asking the following questions of the previous examiner.

Has the previous examiner stopped acting for this charity because:

- they have retired or changed their line of business?
- the circumstances have changed such that the examiner cannot continue in that role e.g. the charity's income has risen above a key threshold, or the individual wants to become more involved in the charity which would compromise their independence?
- the charity has decided to terminate the existing relationship – perhaps as a result of cost or dissatisfaction with the service provided?
- they have fallen out with the charity? For example, has their advice been ignored?
- there has been a mutual parting of the ways?

Before accepting appointment, the prospective independent examiner may wish to use the following questions as a guide to whether they feel they have the relevant skills and abilities to carry out the examination.

- Do I have sufficient knowledge of the charity itself and the charitable sector?
- Are the accounts likely to be simple or complex?
- Do I have the necessary skills to understand the level of complexity of the accounting records?
- Am I independent of the charity trustees and the management, control and administration of the charity?
- If this is my first appointment as an independent examiner, do I feel able to carry out the work?
- Does my governing body authorise me to carry out the work? (qualified independent examiner).
- Are there any issues raised by the previous examiner that need to be considered? (if applicable).

## **Milestone 4 –**

### **Should I accept appointment as an independent examiner?**

Before accepting appointment, individuals may wish to consider whether it may be appropriate for them to take out professional indemnity insurance (PII) to cover them in their capacity as an independent examiner. This is normal practice for professionals acting in such a capacity and therefore potential examiners may wish to consider whether this would also be appropriate for them.

OSCR's view is that it is difficult to foresee situations where it would be necessary for non-professional independent examiners to need professional indemnity insurance as it is hard to envisage where there may be third party exposure or significant risk arising from reliance placed on a set of receipts and payments accounts.

However, there are no set rules and, in highlighting this issue here, OSCR does so to bring the matter to the attention of the reader to enable an informed choice to be made.

## 6.4 Recording the appointment of an examiner

### For charity trustees and independent examiners

Once the charity trustees have chosen an independent examiner, there should be a formal record of the agreement between the charity trustees and the examiner to ensure that both parties understand the services to be provided and the extent of the duties and rights of both the charity trustees and the examiner.

One method of formalising the relationship between the charity trustees and the independent examiner is by way of an 'engagement letter'. This is most commonly used by independent examiners who are providing such services on a commercial basis – that is, they are charging a fee for such work – and will usually take the form of a formal letter issued by the independent examiner. Alternatively, a letter can be issued by the charity trustees.

An 'engagement letter' is usually written by the person who is being engaged to act as an independent examiner. This type of letter is addressed to the charity trustees and sets out the services that the independent examiner will provide, their fee and the duties that they have, as an examiner, under the relevant legislation. The letter should include details regarding the timetable for the independent examination and a schedule of the work to be carried out. The examiner will prepare and sign two copies of the letter and send them to the charity trustees for consideration and signing. Thereafter, one copy will be returned to the independent examiner and the other retained by the charity trustees for their own records.

It is recognised that where a person provides independent examination services to a charity for no charge, it is more likely that a simple letter of appointment or email exchange will be used. This is essentially a written communication that agrees the terms of appointment. Charity trustees are encouraged, as a matter of best practice, to actively consider the merits of formalising their relationship with the independent examiner by having a method of setting out the services that are expected via a letter of appointment. This will enable both parties to understand and appreciate the extent of the work and duties involved in the independent examination process.

For smaller charities, where the examiner is an unpaid volunteer for example, an email could be adequate if the charity trustees and independent examiner feel that this is appropriate.

To assist in the preparation of a letter of appointment, an example is provided at Appendix 5.

## 7. Preparation for an independent examination

In this section, the preparation involved prior to the independent examination taking place is explained.

### 7.1 Preparation by charity trustees **For charity trustees**

Responsibility for maintaining the accounting records and the preparation of accounts always remains with the charity trustees, even where the charity trustees actually employ someone else to carry this out.

In this section, we look at how the information that has been kept by the charity during the financial year should be prepared for presentation to the independent examiner and also how the charity trustees themselves should prepare for the process.

Part of the role of the independent examiner is to review the accounting records kept by the charity and compare them with the accounts prepared from those records. In preparation for the independent examination process, the charity trustees should make sure that:

- the accounting records provide a complete record of all transactions that the charity has entered into during the financial year and are fully up to date
- the accounting records are *sufficiently detailed* to show and explain the transactions (see Table 2 for further guidance on the phrases in italics). In particular, they must be able to:
  - show, *day to day*, the money received and spent by the charity
  - record the *assets and liabilities* of the charity
  - disclose the financial position of the charity *at any time*
  - produce a statement of account in line with the 2006 Regulations.
- the annual report and accounts are prepared for the examiner, unless the independent examiner is assisting in the preparation of the accounts. For further information see section 7.2
- they are prepared to answer any questions regarding the financial transactions that have taken place during the year or to provide any other information that the examiner may require (e.g. minutes of charity trustee meetings). The examiner is entitled to seek any information or further explanation for any matter which comes to their attention in the course of their work. If any information that the examiner requests is not made available, the examiner may make a statement within the report to that effect. It is important to note that the entitlement of the independent examiner to any information that they deem necessary for the fulfilment of their duties extends to information from not only present charity trustees and employees but also to individuals who previously held the role of charity trustee or employee of the charity.

For small charities with simple financial transactions, the accounting records should be kept in a manner that allows them to be summarised on a regular basis, perhaps every quarter. More complex charities should be able to pull their results together more frequently, such as monthly or even weekly. The quality of the books and records held will either help or hinder the charity trustees in their efforts to manage the financial affairs of the charity. If the books and records have been kept in an appropriate manner, then the preparation of the year end accounts should be much easier, quicker and possibly also less costly.

**Table 2: Explanation of terms used in describing the requirements for keeping accounting records**

|                               |   |
|-------------------------------|---|
| <b>Sufficiently detailed</b>  | This will depend on the size and complexity of the charity. The larger and more complex the charity, the more complex the accounting controls and records would need to be. |
| <b>Day to day</b>             | This includes assets and liabilities. Records must be written up as transactions occur.   |
| <b>Assets and liabilities</b> | Registers of equipment and investments, lists of money owed to and by the charity (if appropriate).   |
| <b>At any time</b>            | A third party with sufficient experience could draw up a set of accounts at any time in the year, not just at the year end.   |

## 7.2 Annual report and accounts

A key part of the preparation for the independent examination process will be the production of the annual accounts document for the charity. The content of this document is set out in the 2006 Regulations and comprises the following elements:

- a Trustees' Annual Report
- financial statements, including notes
- an external scrutiny report.

The content of each of these elements will depend on the form of accounts being prepared. For further information, refer to OSCR's Accounts Guidance or the summary information at Appendix 1. The form of accounts is also discussed in section 4.1 of this guidance.

For specific information relating to receipts and payments accounts, refer to Appendix 2.

For specific information relating to fully accrued accounts, refer to Appendix 3.

In many cases, it is recognised that the independent examiner may also undertake the task of preparing the accounts. Charity trustees should bear in mind however that the ultimate responsibility for the accounts of the charity lies with them, and while another individual or organisation might be engaged to undertake this task, the content, approval and filing of accounts with OSCR remains the responsibility of the charity trustees.

Where the task of preparing the accounts is delegated to an individual who is also acting as an independent examiner, it will still be necessary for the accounting records to be complete and up to date as outlined in section 7.1. This is so that the examiner can simply extract the relevant figures from the accounting records and put them into the required statutory format of the accounts. The examiner should not have to make any significant changes to the accounting records in order to obtain the figures required to prepare the accounts. The transactions should, as far as possible, be summarised into categories of income and expenditure and also assets and liabilities, where appropriate.

## 8. The work of the independent examiner **For independent examiners**

In order to assist those providing independent examination services, a number of 'best practice' steps have been identified for examiners to follow in undertaking their duties.

In summary, these steps are:

**Step 1: Preparation by the independent examiner**

**Step 2: Ensuring that the charity has prepared its accounts on the correct basis and that it is eligible for independent examination**

**Step 3: Keeping a record and planning the work required**

**Step 4: Accounting records and the comparison with the accounts**

**Step 5: Form and content of accounts**

**Step 6: Drawing conclusions and preparing a report**

Each step is explained in more detail as follows:

### **Step 1: Preparation by the independent examiner**

Independent examiners, in preparing for the review of the accounting records and annual accounts, should ensure that they have an understanding of the charity for which they are providing a service. This means that the examiner should be aware of, and understand, the objectives of the charity and the activities that it undertakes in order to further those objectives. This is necessary in order for the examiner to be satisfied that the spending of the charity is in line with the charitable purposes. Identification of any expenditure outwith the scope of the charity's purposes may constitute a matter that should be reported by the examiner to OSCR. This will be looked at in greater depth in section 9.

For those independent examiners charging a fee and therefore deemed to be providing 'accountancy services', there is also a need to comply with the Proceeds of Crime Act 2002 and Money Laundering Regulations – this includes the need to hold proof of identification and address for the principal office bearers and a proportion of the charity trustees.

As preparation for the examination, the independent examiner may wish to use the following questions as a guide to whether they are ready to carry out the examination.

- Am I familiar with the accounting and reporting requirements?
- Have I read the governing document of the charity?
- Is the charity eligible for an independent examination?
- If fully accrued accounts are being prepared, am I qualified to carry out the examination?
- What practical knowledge of the charity do I have?
- Have I seen the last set of accounts?
- Have I seen the minutes of the most recent meeting of the charity trustees?
- Have I seen the minutes of any other relevant meetings of the charity trustees, including the meeting where approval was given for my appointment?
- Have I checked the OSCR register entry for the charity?

## Milestone 5 –

### Have I carried out all the necessary preparatory work?

#### **Step 2: Ensuring that the charity has prepared its accounts on the correct basis and that it is eligible for independent examination**

This step involves looking at a number of criteria in order for the examiner to be satisfied that the accounts of the charity are prepared on the correct basis and that independent examination is the permitted form of external scrutiny for the charity. It is also important to check if the examination must be carried out by a qualified person or not.

Therefore, there are several key elements to consider:

- If the charity has prepared receipts and payments accounts, is it eligible to do so under the 2006 Regulations?
- Is the charity a company?
- Is the charity eligible for independent examination under the 2006 Regulations?

#### *Can the charity prepare receipts and payments accounts?*

As explained in section 4.1, the 2006 Regulations set out where a charity is eligible to prepare accounts on a receipts and payments basis. This is where the gross income of the charity is less than £250,000 (£100,000 for periods starting before 1 April 2011) and the charity is not a company.

In addition, the examiner should ensure that they are provided with a copy of the most up to date governing document for the charity as it is possible that the document will contain specific provisions about the format of the accounts to be prepared. For example, there may be reference to ‘true and fair’ accounts which would require the preparation of fully accrued accounts. Receipts and payments accounts do not fall within the definition of ‘true and fair’ in this context.

### *Is the charity a company?*

Where the charity is also a company, it is required to comply with not only charity law but also company law. This means that the charity must prepare fully accrued accounts on a 'true and fair' basis in accordance with both charity and company law. An independent examination must then be carried out by an appropriately qualified individual as explained in section 5.2.

### *Eligibility for independent examination*

As outlined at section 4.2, it is important to ensure that the charity is eligible to have an independent examination of its accounts as opposed to an audit. This not only involves looking at the gross income and gross asset levels of the charity but also at the constitution or governing document of the charity.

## **Milestone 6 –**

- **Are the charity's accounts prepared in the required form?**
- **Is the charity eligible for an independent examination?**

### **Step 3: Keeping a record and planning the work required**

This step involves thinking about what processes need to be carried out and how they will be recorded. Obtaining a good understanding of the charity, its charitable objectives or purposes and the activities that it carries out to further or achieve these purposes, forms an integral part of deciding on what processes are most appropriate. It is also important for an examiner to keep a written record of their work from the planning stage through to their report. Any evidence, analysis or explanations the examiner obtains should be kept as part of this recording of their examination.

The record of work done during the examination process is for the benefit of the examiner, not OSCR. The record should focus on key factors taking account of risk. A comprehensive manual is not required – a series of bullet points, for example, may be sufficient at the planning stage and tick boxes alongside this would provide a record of completion. Key factors could include staffing and cash handling arrangements. The more complex the charity, the more factors that will need to be considered.

During the planning stage the examiner should consider any issues surrounding their independence. Any issues and consequent safeguards introduced should be clearly documented within the working papers. Any items documented as a threat to independence and any safeguards implemented should also be communicated to the trustees of the charity.

Once the examiner has a clear understanding of what the charity does and why, they should then consider the format of the accounting records held by the charity and the form of accounts prepared. This will guide the examiner in deciding on the most appropriate process to apply to the examination. For example, the processes carried out when examining a set of

receipts and payments accounts are likely to be different to those carried out in the course of an independent examination of a set of fully accrued accounts. Similarly, the processes carried out when examining a very basic set of accounting records comprising a manual cash book, bank statements, receipts and invoices will be different to those carried out when examining a charity that uses a computerised accounting package to maintain its accounting records.

A practical example may be that when examining a set of basic, manual accounting records, an examiner is likely to carry out some work to ensure that the entries made in the cash book correspond to transactions listed on the bank statements and to an invoice or receipt. Where a charity is using a computerised package to maintain the accounting records, this may be done initially on a test basis, but is unlikely to be required after that.

### **Milestone 7 –**

- **Have I planned the work adequately?**
- **Do I know what processes are required?**
- **Do I have an adequate method of documenting my work?**

#### **Step 4: Accounting records and comparison with the accounts**

Under the 2006 Regulations, the independent examiner is required, in the report, to state whether any matter has come to their attention that gives them cause to believe that in any material respect the accounting records have not been kept in respect of the charity in accordance with the requirements of the 2005 Act and section 4 of the 2006 Regulations.

##### *Accounting records*

In order to be able to fulfil the obligations placed on the examiner by the 2006 Regulations, it is necessary for the examiner to review and consider the accounting records in some depth. The accounting records are required by the 2006 Regulations to be sufficient to show and explain the transactions of the charity and which:

- disclose the financial position of the charity at any time
- enable the charity trustees to ensure that the accounts are prepared in accordance with the 2006 Regulations.

The 2006 Regulations specify that the records shall contain:

- entries showing from day to day all sums of money received and spent by the charity and the source or application of those monies
- a record of the assets and liabilities of the charity.

Further guidance on what these requirements actually mean is provided in section 7.1.

In practice, for smaller charities the records will consist of:

- a basic cash book, either paper or electronic, written up on a regular basis. Records should be written up, where possible, as transactions occur.
- a record of assets and liabilities which might include a fixed asset register. This would detail equipment held with corresponding purchase cost and current value.
- a list of debtors and creditors – those people or organisations that owe money to the charity or are owed money by the charity – and the amounts due.

The independent examiner, in the report, is required to state whether any matter has come to their attention that gives them cause to believe that in any **material** respect accounting records have not been kept in accordance with the relevant requirements.

*What does 'material' mean?*

'Material' in this context means that the examiner is required to consider whether the overall format and content of the accounting records appears to be in line with the requirements outlined above. The objective is not to identify every single unintentional error or missing receipt. On a practical level, if the examiner were to stand back and look at the accounts, does the omission or inclusion of an error alter the overall picture that the accounts portray. If so, the item or issue is considered to be material.

If the examiner comes across a mistake, a decision has to be made as to whether the sum involved is large enough to warrant comment in the context of their duties. The key question is, does the omission or inclusion of an error alter the overall picture that the accounts portray?

In determining whether an amount is material, judgements will have to be made. Examiners familiar with materiality from a commercial point of view should note that materiality thresholds tend to be lower for charities because of the implicit trust placed on charities due to the nature of their income.

For further clarification, please refer to the Glossary of terms definition of 'material'.

*Comparing the accounting records with the annual accounts*

After examining the accounting records, the examiner should then consider those records in comparison with the annual accounts. The accounts must fairly reflect the underlying records and this is what the examiner should consider. For charities that have more than one type of fund for example (i.e. unrestricted, restricted and endowment funds), it is important to ensure that the transactions that relate to each fund are easily identifiable from the accounting records in order that they can be easily related to the appropriate columns within the accounts.

The examiner should compare the accounts of the charity with the charity's accounting records in sufficient detail to provide a reasonable basis on which to decide whether the accounts are in accordance with the accounting records.

The examiner needs to carry out sufficient procedures to be satisfied as to whether or not the regulatory requirements have been met in terms of the substance of the accounting records. This does not mean, however, that the examiner has to individually check every receipt or invoice to a corresponding bank deposit or cash withdrawal for example.

There is no requirement to trace back to source documentation (such as paid invoices, remittance advices, letters from funders etc.) and verify accounting records unless concerns arise during the examination that cannot be explained.

Examples of procedures that may be carried out would be:

- reviewing bank statements, cash books or other accounting records for large or unusual items or transfers
- checking for completeness (control accounts, bank reconciliations)
- checking from books and records to the accounts (paying-in books to banking to accounting entries to accounts)
- checking back from accounts to accounting records if anything looks unusual.

### Milestone 8 –

- **Are the accounting records sufficient in terms of the formal regulatory requirements? (Refer back to section 7.1 for further clarification if required.)**
- **Do the accounts fairly reflect the accounting records?**
- **Are there any material items to consider that are not adequately represented in the accounts?**

### Step 5: Form and content of accounts

#### *Statutory requirements*

Under the 2006 Regulations, an independent examiner must consider whether the form and content of the accounts is in line with the statutory requirements. If they consider that the accounts do not comply in any material respect, they must state this in their report.

In practical terms, the actual work to be carried out will differ depending on whether the accounts are prepared on a receipts and payments basis or a fully accrued basis.

- For receipts and payments accounts, the examiner will need to consider section 9 and Schedules 2 and 3 of the 2006 Regulations. Independent examiners may find the Schedules to the 2006 Regulations useful as a checklist. The 2006 Regulations are available to download from the OSCR website.
- For fully accrued accounts, the examiner will need to consider section 8 of the 2006 Regulations and the SORP.

Please refer to Appendices 2 and 3 for further information regarding accounting requirements.

### *Any other information necessary*

In considering the form and content of the accounts document and the accounting records, it is important for examiners to ask themselves if any other information should be disclosed within their report to enable a reader of the accounts to have a reasonable understanding of the accounts. This may involve consideration of any significant or unusual transactions or activities that the charity has entered into during the period and whether these are adequately reflected in the accounts.

### *Trustees' Annual Report*

The accounts document for any Scottish charity must include a Trustees' Annual Report under the 2006 Regulations. The Trustees' Annual Report is an opportunity for the charity trustees to provide further supplementary information regarding their activities and achievements for the period. The report is particularly useful for readers who are not familiar with accounts but are still interested in understanding what the charity has achieved.

The content of the Trustees' Annual Report is specified in legislation. For receipts and payments accounts, the content is detailed within Schedule 2 of the 2006 Regulations. Charity trustees may wish to use schedule 2 as a checklist when preparing their report. Alternatively, the Receipts and Payments Workpack contains pro forma sheets for preparation of the report.

For fully accrued accounts, the content is detailed within the SORP. Charities preparing fully accrued accounts that are not subject to statutory audit (refer to figures 1 and 2 within section 4.2) should be aware that there are concessions available within the SORP which allow charity trustees to prepare a simplified Trustees' Annual Report. Please refer to Appendix 5 of the SORP for further clarification.

An independent examiner, in carrying out their work, is required to consider whether any of the information contained within the accounts is inconsistent in any material respect with the Trustees' Annual Report. In many cases, this may simply involve a review of any financial amounts stated within the Trustees' Annual Report and a comparison of this information with the financial statements. For example, the charity trustees may provide a brief financial overview of the charity for the year within their report which may include specifying the surplus or deficit for the year; an independent examiner would then check the stated surplus or deficit against the statement of receipts and payments or the statement of financial activities (fully accrued accounts) as appropriate. In other cases, it may be a slightly longer process, but this will depend on the extent of the information provided within the Trustees' Annual Report and the complexity of the financial statements.

## **Milestone 9 –**

- **Do the accounts, including the Trustees' Annual Report, include all the information required under the 2006 Regulations?**
- **Are the accounts in the statutory format?**

## Step 6: Drawing conclusions and preparing a report

Once the independent examiner has completed the necessary processes and procedures, they will need to reflect on all the evidence gathered and to consider any implications for their report.

At this stage, the examiner may have noted matters that necessitate some further discussion with the charity trustees. This may be to provide the charity trustees with an opportunity to amend the accounts before the examiner drafts his report which may, in turn, avoid a situation where an examiner may have to 'qualify' the report or make reference to any adverse findings from the examination.

The 2006 Regulations specify the content of the independent examiner's report to the charity trustees. It must include the following:

- the name and address of the independent examiner and the name of the charity concerned
- the signature of the independent examiner and details of any relevant professional qualifications or professional body of which the examiner is a member
- the date of the report and financial year in respect of which the accounts to which it relates have been prepared. The date of signing must be the same, or after, the date of signing of the Trustees' Annual Report and the financial statements by the charity trustees
- a statement that it is a report in respect of an examination carried out under section 44 (1)(c) of the 2005 Act
- a statement as to whether or not any matter has come to the attention of the examiner in connection with the examination which gives them reasonable cause to believe that in any material respect:
  - accounting records have not been kept in respect of the charity in accordance with section 44(1)(a) of the 2005 Act and section 4 of the 2006 Regulations
  - the accounts do not accord with those records
  - in the case of an examination of receipts and payments accounts, the receipts and payments account and statement of balances do not comply with section 9 of the 2006 Regulations
  - in the case of an examination of fully accrued accounts, the accounts do not comply with section 8 of the 2006 Regulations.
- a statement whether or not any matter has come to the independent examiner's attention in connection with the examination to which, in the independent examiner's opinion, attention should be drawn in the report in order to enable a proper understanding of the accounts to be reached

- a statement as to any of the following matters that have become apparent to the examiner during the course of the examination:
  - there has been any material expenditure or action which appears not to be in accordance with the purposes of the charity
  - any information or explanation to which they are entitled under section 13 of the 2006 Regulations has not been afforded to them
  - whether any information contained in the accounts is inconsistent in any material respect with any report of the charity trustees prepared under section 44(1)(b) of the 2005 Act in respect of the financial year in question.

The final step in the independent examination process is for the examiner to stand back and be objective about the accounts and the work done to date. They must consider whether any issues have been identified and whether the accounts actually make sense in light of what they know about the charity and by comparing the financial information with the Trustees' Annual Report.

They must ensure that they have identified all the unusual items or disclosures in the accounts. The examiner may need to seek explanations from the charity trustees for any issues that have not been resolved. The examiner should ensure that their own record of preparation, work done, explanations received and checks made is complete.

The examiner needs to:

- consider if the accounts look as they would expect from all the information they have gathered – do they make sense?
- check any large or unusual items that appear in the accounts or the accounting records.

The examiner will need to draw on their experience and exercise judgement as to what is 'unusual' for each charity.

Where no material issues have been identified and the examiner is satisfied with the results of the processes they have carried out, the reporting will be quite simple as there are no particular matters for the examiner to highlight to the reader of the accounts.

However, where issues have been noted with the format or content of the accounts or the accounting records etc, then it will be necessary for the examiner to consider the implications for their report. This means that the examiner will need to weigh up the issues identified and to assess whether or not these indicate that in any material respect the accounting records **have not been** maintained in line with statutory requirements, the accounts **do not agree** to those records or there are any other issues in relation to matters on which they are required to report. The examiner, as much as possible, needs to stand back and consider whether the accounts fairly and adequately represent what has happened in the charity in the financial period under review.

It is recognised that the drafting of the report in line with the regulatory requirements can sometimes be difficult for an examiner. In order to assist examiners, several example reports have been provided in Appendix 2 of this guidance, covering a variety of different situations.

In most cases, the preparation of the independent examiner's report for inclusion in the accounts document will be the culmination of the examiner's work. However, in the next section, the continuing reporting duties of the independent examiner to OSCR are explained.

It is worth noting here that it is the responsibility of the charity trustees to submit the accounts to OSCR along with the Annual Return Form.

### **Milestone 10**

- **Have I considered the findings of my work?**
- **Are there any implications for my report?**
- **Have I prepared my report in line with the requirements of the 2006 Regulations?**

## 9. Whistleblowing – continuing reporting duties for independent examiners **For independent examiners**

Independent examiners (and auditors) are also required to report certain matters to OSCR as part of their statutory reporting duties. This duty is distinct from the requirement for the independent examiner's report which is attached to the accounts document as described in Step 5. It is important to note that the independent examiner's report is only submitted to OSCR with the annual accounts. It is the charity trustees' duty to ensure that this is done. However, relevant matters as discussed below should be reported to OSCR by the independent examiner as soon as they become apparent. This requirement allows information to be provided to OSCR to assist in the fulfilment of its regulatory purposes.

The provisions within section 46 of the 2005 Act fall into two strands:

- matters that must be reported on the basis that the independent examiner has reasonable cause to believe that the matter is likely to be of material significance for the purposes of OSCR exercising its functions under sections 28 (inquiries about charities etc.), 30 (removal from the Register of a charity which no longer meets charity test) or 31 (powers of OSCR following inquiries) of the 2005 Act – often referred to as the 'statutory' reporting duty
- matters that the independent examiner may report as they have reasonable cause to believe they are relevant for OSCR in exercising any of its functions but are not captured by the mandatory reporting duty – often referred to as the 'discretionary' reporting duty.

### *The statutory reporting duty*

The reporting of a matter of material significance is a separate report from the independent examiner's report on the accounts. The 2005 Act requires the report to be made immediately the matter comes to the independent examiner's attention and it is recommended that the report should be made in writing although there is no legal obligation to do so.

It is not part of the reporting duty to require independent examiners to perform any additional scrutiny work as a result of the statutory duty nor are they required specifically to seek out reportable matters. Examiners should however include procedures within their planning processes to ensure that they have sufficient understanding to enable them to identify situations which may give reasonable cause to believe that a matter should be reported to OSCR.

In order to recognise whether a situation is likely to be of material significance to OSCR's functions, an understanding is needed of those matters which, either due to their nature or potential financial impact, are likely to require evaluation and, where appropriate, investigation by OSCR.

OSCR will always consider the following to be of material significance, and hence reportable:

- matters suggesting dishonesty or fraud involving a significant loss of, or a major risk to, charitable funds or assets
- 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
- 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
- matters leading to the 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
- 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
- significant or recurring breach(es) of either a legislative requirement or of the charity's trust
- 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
- the notification, on ceasing to hold office or resigning from office, of those matters reported to the charity's trustees which fall into one or more of the headings listed above.

These matters are considered central to the integrity of a charity and as such will require evaluation and where appropriate investigation by the regulator. OSCR considers all such reports to have a very high intelligence value and takes a risk based and proportionate approach to inquiry work when deciding whether to open an inquiry.

It should also be noted that where the matter relates to terrorism, then the matter must also be reported to the police. Should the matter involve money laundering, independent examiners who are charging a fee for their service should also report the matter to the Serious Organised Crime Agency under the requirements of the Money Laundering Regulations. If the report concerns the abuse of vulnerable beneficiaries, a report should also be made to the Police and/or Social Services.

Other matters considered material may change from time to time; currently they are reflected in OSCR's monitoring programme priorities.

Where independent examiners make a report, they may not have complete information about the issue(s) but should be prepared to provide as much relevant information as possible about the matter(s) they are reporting. Reference may also be made as to whether or not the trustees are aware of the issue and/or what action has been taken in response.

### *The discretionary reporting duty*

Independent examiners also have a broad discretionary right to report those matters that they believe may be relevant to the work of OSCR but that do not fall under the statutory reporting duty.

OSCR considers such reports to have considerable intelligence value and welcomes these submissions. Given the broad discretion permitted, it is not possible to list all instances for reporting. However, the examiner may usefully review the following matters:

- those which were not considered material relating to statutory duties
- where trustees are requested to provide additional information as part of OSCR's monitoring regime.

OSCR monitors larger charities using the annual Supplementary Monitoring Return which is designed to consider specific areas of interest, including:

- payments to charity trustees
- relationships with connected trading companies
- for charities with income of over £250,000 (£100,000 for accounting periods starting before 1 April 2011), comparison of some income/cost relationships.

Pre-populated Annual Return including the Supplementary Monitoring Return are sent out to charities automatically if the gross income for the previous year is £25,000 or over.

A specimen copy of the Supplementary Monitoring Return is available to download from our website.

Matters falling within this discretionary category are likely to be indicative of significant risks to charitable funds or their proper application and would therefore normally be relevant to the work of OSCR. Where such a matter arises, the independent examiner may discuss the matter with the trustees to identify whether it remains a matter of concern and whether the trustees have taken or are taking action which can reasonably be expected to remedy or mitigate the effect in the current or future years.

The range of matters to be included in this section is very wide and while the following examples can provide a guide, they are in no way exhaustive. The type of matters that may require reporting to OSCR could include:

- the cumulative impact on a charity of ignoring professional recommendations
- unexplained large discretionary redundancy payments above the statutory minimum
- smaller administrative or financial issues
- expenditure outwith the scope of the charity's purposes.

Although the independent examiner enjoys a discretion as to whether to make a report of a matter relevant to the work of OSCR, it is recommended that the examiner documents any relevant matters identified in the course of the independent examination and also the basis of any decision not to report a matter falling within this discretionary category.

### **Milestone 11 –**

- **Are there any matters that I must report to OSCR?**
- **Are there any matters that I think may be of interest or use to OSCR?**
- **Have I made the required/appropriate reports to OSCR?**

## 10. Cross border charities

### **For charity trustees and independent examiners of cross border charities only**

Charities that are registered both with OSCR and the Charity Commission for England and Wales are referred to as 'cross border charities' and are regulated by both bodies. Under OSCR's cross border monitoring regime, the Charity Commission is considered to be the 'lead regulator' for enquiry purposes.

As there are differences in the accounting regimes in place within Scotland and England and Wales, it is important that cross border charities are familiar with both and understand that they are required to comply with the more stringent requirements, regardless of the jurisdiction in which these arise.

In practical terms, this means that, for periods starting before 1 April 2011, cross border charities must prepare fully accrued accounts where the income of the charity is £100,000 or more, despite the fact that the relevant threshold for the preparation of fully accrued accounts is £250,000 under the relevant regulations in England and Wales. Since 1 April 2011, the thresholds in Scotland have been increased to £250,000 and are therefore in line with the current regulations in England and Wales.

In addition, there are formal requirements for the content of receipts and payments accounts under the regulatory regime in Scotland and cross border charities preparing receipts and payments accounts are required to comply with these requirements. OSCR has a receipts and payments workpack that smaller charities can use to prepare their receipts and payments accounts and the Charity Commission will accept accounts prepared in accordance with the Scottish requirements, including those prepared using the workpack.

For English and Welsh charities that are subject to the independent examination regime, the Directions issued by the Charity Commission must also be followed and the independent examiner must, in his report, confirm that this is the case.

There is no comparable regime in Scotland and therefore the six steps to be undertaken in the independent examination process within this guidance booklet are what OSCR considers to be best practice in this area.

Cross border charities that are subject to independent examination must ensure that this is carried out in accordance with the Charity Commission Directions. However, in Scotland, there is also a requirement for an independent examiner to always consider the information contained within the Trustees' Annual Report in order to identify any inconsistency with the financial statements; this is different from the position in England and Wales where this is only required in relation to accrued accounts. OSCR will consider that where the Charity Commission Directions have been followed and supplemented by a review of the Trustees' Annual Report to identify any inconsistency, that the steps undertaken are appropriate and in line with the relevant requirements under the 2006 Regulations.

OSCR recommends that cross border charities refer to the Charity Commission's independent examination guidance: Independent Examination of Charity Accounts – Examiner's Guide (CC32) for details of the Directions and for example independent examiner's reports that are appropriate for cross border charities.

A specific example independent examiner's report is provided for reference at Appendix 4 – example 4.5.

It is also important to note that there is a difference in the filing deadline within the two jurisdictions – in Scotland, the appropriate Return forms and accounts must be filed with OSCR within 9 months of the charity's year end date. In England and Wales, the deadline is currently 10 months after the end of the financial year.

## Appendix 1: Summary of accounting requirements for Scottish charities

Table 3 provides a brief summary of the statutory requirements for the format and external scrutiny of accounts. Note however that where there is a constitutional requirement for audit within a charity's governing document or any applicable enactment that sets out this requirement, this takes precedence over the income and asset thresholds outlined below.

**Table 3: the statutory financial thresholds for the format and external scrutiny of accounts – accounting periods beginning on or after 1 April 2008**

| Gross income                              | Format of accounts   |   | External scrutiny of accounts** <sup>(2)</sup>                                   |   |
|---|--|---|--|---|
| <b>Less than £250,000<sup>(1)</sup></b>   | Non-company charities: receipts and payments accounts (See Appendix 2) | Charitable companies: fully accrued accounts (See Appendix 3) | Non-company charities: independent examination by a person with requisite skills | Charitable companies: independent examination by a qualified person |
| <b>£250,000<sup>(1)</sup> to £499,999</b> | Fully accrued accounts (See Appendix 3)                                |   | Independent examination by a qualified person                                    |   |
| <b>£500,000 and over</b>                  |  |   | Audit  |   |

(1) less than £100,000 and between £100,000 and £499,000 for periods starting before 1 April 2011.

(2) Note that gross assets of the charity must also be considered when determining the method of external scrutiny that the charity requires – where the assets are at least £3.26 million (£2.8 million for accounting periods starting before 1 April 2011) and fully accrued accounts are prepared, an audit is required under the 2006 Regulations.

Details of the format and external scrutiny of accounts are provided in OSCR's Accounts Guidance which is available from the website. For ease of reference, a summary of the main points has been provided in Appendices 1 and 2.

## Appendix 2: Receipts and payments accounts

The 2006 Regulations specify the form and content of receipts and payments accounts and this provides good structure for charity trustees to follow in preparing the charity's accounts. OSCR has produced a workpack for charities preparing receipts and payments accounts to use; it provides templates for completion in both hard copy and electronic formats and may be downloaded from the OSCR website.

The 2006 Regulations state that receipts and payments accounts must comprise:

- a Trustees' Annual Report
- a Statement of Receipts and Payments
- a Statement of Balances as at the last day of the financial year
- notes to the accounts.

Furthermore, the content of each of these elements is specified as being:

### Trustees' Annual Report

A charity's financial statements alone do not provide all the information a reader would need to gain a full picture of the charity; therefore, the charity trustees must prepare a report that includes the following elements:

- the name of the charity as it appears on the Scottish Charity Register and any other name by which the charity is known.
- the charity's Scottish Charity Number. This begins SC followed by 6 digits, the first being 0 (zero).
- the address of the principal office of the charity. Where the charity does not have an office, the annual report must give the name and address of one of the charity trustees.\*
- the names of all the charity trustees on the date the annual report was approved by the charity trustees unless:
  - there are more than 50 charity trustees, in which case the names of 50 charity trustees will be sufficient
  - the charity is entitled to exclude the names of the charity trustees because OSCR is satisfied that to include this information would jeopardise the safety or security of people or premises.
- the name of anyone who has been a charity trustee during the financial year covered by the accounts of which the Trustees' Annual Report forms part.\*
- the particulars of the constitution or governing document of the charity that contains the purposes and regulates the administration of the charity. This would include:
  - how the charity is constituted (e.g. unincorporated association, trust etc)
  - the organisational structure of the charity (e.g. a membership which elects a management committee or self appointing trustees)
  - the relationship of the charity to any other body (e.g. affiliation with an umbrella group).

- the purposes of the charity as set out in the constitution or governing document of the charity.
- a description of how charity trustees are recruited and appointed, including the name of any external body entitled to appoint charity trustees.
- a summary of the main activities of the charity and achievements in the financial year.
- a description of the policy the charity trustees have adopted to determine the level of reserves to be held by the charity. This should include:
  - the level of reserves held
  - why they are held
  - the amount and purpose of any designated fund, and the likely timing of any expenditure that has been set aside for the future.
- if the charity has a fund that is in deficit, an explanation of how it came about and what steps are being taken to rectify it.
- an analysis of donated facilities and services, if any, that the charity received during the financial year.

\*unless the charity is entitled to exclude the names or addresses because OSCR is satisfied that to include this information would jeopardise the safety or security of people or premises.

The Trustees' Annual Report must be approved by all of the charity's trustees and then signed by one trustee on behalf of all of them. The date of approval must be stated.

### Statement of Receipts and Payments

The Statement of Receipts and Payments provides an analysis of the incoming and outgoing cash and bank transactions for the year. The analysis must show the following categories separately along with corresponding figures for the previous financial year:

Receipts:

- donations
- legacies
- grants
- receipts from fundraising activities
- gross trading receipts
- income from investments other than land and buildings
- rents from land and buildings
- gross receipts from other charitable activities.

In addition, OSCR recommends that:

- proceeds from the sale of fixed assets
  - proceeds from the sale of investments
- should be shown separately from the above receipts.

Payments:

- expenses for fundraising activities
- gross trading payments
- investment management costs
- payments relating directly to charitable activities, detailing material items
- grants and donations relating directly to charitable activities
- governance costs relating to:
  - audit or independent examination
  - preparation of annual accounts
  - legal costs associated with constitutional matters or trustee advice.

In addition, OSCR recommends that:

- purchases of fixed assets
  - purchases of investments
- should be shown separately from the above receipts.

The Statement of Receipts and Payments must distinguish between unrestricted and restricted funds, as well as any expendable and permanent endowment funds. This is usually achieved by giving each fund a separate column in the accounts. Where a charity has more than one fund in any of these categories it can present the total funds held in each. The notes to the accounts must then explain in sufficient detail the content of the unrestricted, restricted and endowment funds so that the reader gains a full understanding of the accounts.

Any transfers from a restricted, unrestricted, expendable endowment or permanent endowment fund into another fund must be shown separately.

### Statement of balances

The Statement of Balances must reconcile the cash and bank balances at the beginning of the financial year and the surplus or deficit shown in the Statement of Receipts and Payments with the cash and bank balances at the end of the financial year.

As with the Statement of Receipts and Payments, the Statement of Balances must distinguish between restricted and unrestricted funds, as well as any expendable or permanent endowment funds held by the charity.

In addition, the Statement of Balances must also:

- summarise the investments held by the charity at their market valuation at the year end
- summarise the other assets held by the charity, including gifted assets, either at the valuation if available or at cost. Where the charity trustees consider the valuation to be lower than the cost, use the valuation
- include a total estimate of the liabilities of the charity at the financial year end. Contingent liabilities must be shown separately
- show corresponding figures for the previous financial year.

The Statement of Balances must be signed by a charity trustee on behalf of all the charity trustees and specify the date on which the statement of account was approved by the charity trustees.

### Notes to the accounts

Notes are an important part of the accounts. They expand on or explain the information contained in the Statement of Receipts and Payments and Statement of Balances, and will help a reader understand the accounts.

The notes to the accounts must contain the following information, unless it has been provided in the Trustees' Annual Report:

- the nature and purpose of the different funds held by the charity, including any restrictions on their use
- the number and amount of any grants paid out by the charity, the type of activity or project supported by those grants, and whether they were paid out to an individual or an organisation
- the amount of remuneration paid to a charity trustee or person connected to a charity trustee (a connected person). Any remuneration must be in accordance with section 67 of the Act and the note must specify the authority under which the remuneration was paid. If no remuneration was paid to a charity trustee or anyone connected to a charity trustee this must be stated
- the total amount and nature of expenses, if any, paid to charity trustees and the number of charity trustees receiving expenses. If no expenses were paid to charity trustees this must be stated
- the nature of any transactions between the charity and any charity trustee or person connected to a charity trustee. This may include, for example, a charity trustee purchasing an asset from the charity or a charity paying a firm for services such as professional advice where a charity trustee has a substantial interest in the firm. This note must include:
  - the nature of the relationship
  - the nature and amount of the transaction
  - any outstanding balances at the financial year end
  - any further information required to reasonably assist the reader to understand the statement of accounts.

### Appendix 3: Fully accrued accounts

Under the 2006 Regulations, the statement of account for fully accrued accounts must consist of:

- **a Trustees' Annual Report** from the charity trustees of the activities of the charity. The content of the annual report is detailed in the SORP. The annual report is a crucial component of the statement of account and its preparation should actively involve the charity trustees. It provides information that is not contained in the financial statements that will enable a reader to understand how the numerical information relates to the organisational structure and activities of the charity
- **a Statement of Financial Activities** of the charity that gives a true and fair view of the incoming resources of the charity and their application during the financial year
- **a Balance Sheet** that gives a true and fair view of the state of the financial affairs of the charity at the end of the financial year
- **a Cash Flow Statement** (applicable to large audited charities)
- **notes to the accounts** that explain the accounting policies adopted and explain or expand on the information contained within the main accounting statement. See the SORP for further information.

The Balance Sheet and Trustees' Annual Report must be signed by one of the charity trustees on behalf of all the charity's trustees. Both documents must also specify the date on which the statement of account of which they form part was approved by the charity trustees.

The trustees' or directors' report of a charitable company is often signed by the company secretary. Where the company secretary is not also a charity trustee, the report must be signed by a charity trustee.

The statement of account must be prepared in accordance with the methods and principles set out in the SORP.

Additional information must be provided in the notes to the accounts where the Statement of Financial Activities (SoFA) and Balance Sheet are insufficient on their own to provide a true and fair view.

If compliance with the 2006 Regulations for the preparation of accounts would not be consistent with giving a true and fair view, the trustees should depart from the 2006 Regulations to the extent necessary to give a true and fair view. The reasons for any departures from the 2006 Regulations should be given in the accounts.

To allow comparisons to be made, any figures in the Statement of Financial Activities or Balance Sheet must include the corresponding amount for the previous financial year or period. Where the corresponding amount referred to has a different definition, it must be adjusted to allow a comparison to be made.

Where there is no figure to be shown in the statement of account but there was a corresponding amount in the previous year, then the previous year's figure must be shown.

The Statement of Financial Activities must distinguish between unrestricted, restricted and endowment funds. However, where a charity has more than one fund in any of these categories it can present the total funds held in each. The notes to the accounts must then explain in sufficient detail the content of the unrestricted, restricted and endowment funds so that the reader gains a full understanding of the accounts.

Charities preparing fully accrued accounts should also be aware of the concessions that are available within the SORP for those charities that are below the statutory audit thresholds. Some particular accounting disclosures may not be relevant for the users of accounts prepared by smaller charities. Similarly, the level of detail provided in the Trustees' Annual Report is likely to be dependent on the structure, size and complexity of the charity and be proportionate to the needs of the users of the report. The concessions are detailed in Appendix 5 of the SORP.

## **Appendix 4: Example independent examiner's reports**

As the content of an Independent Examiner's Report is specified by the 2006 Regulations, it is important that the examiner uses the correct form of words in fulfilling his duty to provide such a report.

On the basis that there may be different situations encountered by independent examiners, several different reports have been provided for guidance here. These are briefly described below along with an explanation of the circumstances to which each one would be applicable:

- Example 4.1: Unqualified report for a non-company charity preparing receipts and payments accounts
- Example 4.2: Unqualified report for a non-company charity preparing fully accrued accounts
- Example 4.3: Unqualified report for a charitable company
- Example 4.4: Qualified report for a charity preparing receipts and payments accounts with a matter to be reported
- Example 4.5: Qualified report for a cross border non-company charity preparing fully accrued accounts with a matter to be reported

## **Example 4.1: Examiner's unqualified report for a non-company charity preparing receipts and payments accounts**

### **Independent Examiner's Report to the Trustees of 'ABC' Trust**

I report on the accounts of the charity for the year ended xx xxxx 20xx which are set out on pages xx to xx.

#### **Respective responsibilities of trustees and examiner**

The charity's trustees are responsible for the preparation of the accounts in accordance with the terms of the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006. The charity trustees consider that the audit requirement of Regulation 10(1) (d) of the 2006 Accounts Regulations does not apply. It is my responsibility to examine the accounts as required under section 44(1) (c) of the Act and to state whether particular matters have come to my attention.

#### **Basis of independent examiner's statement**

My examination is carried out in accordance with Regulation 11 of the 2006 Accounts Regulations. An examination includes a review of the accounting records kept by the charity and a comparison of the accounts presented with those records. It also includes consideration of any unusual items or disclosures in the accounts, and seeks explanations from the trustees concerning any such matters. The procedures undertaken do not provide all the evidence that would be required in an audit, and consequently I do not express an audit opinion on the view given by the accounts.

#### **Independent examiner's statement**

In the course of my examination, no matter has come to my attention [other than disclosed below\*]

1. which gives me reasonable cause to believe that in any material respect the requirements:

- to keep accounting records in accordance with Section 44(1) (a) of the 2005 Act and Regulation 4 of the 2006 Accounts Regulations
- to prepare accounts which accord with the accounting records and comply with Regulation 9 of the 2006 Accounts Regulations

have not been met, or

2. to which, in my opinion, attention should be drawn in order to enable a proper understanding of the accounts to be reached.

Name:

Relevant Professional qualification/professional body:

Address:

Date:

\* Please delete the words in brackets if they do not apply. If the words do apply set out those matters which have come to your attention.

## Example 4.2 Examiner's unqualified report for a non-company charity preparing fully accrued accounts

### Independent Examiner's Report to the Trustees of 'ABC' Trust

I report on the accounts of the charity for the year ended xx xxxx 20xx which are set out on pages xx to xx.

### Respective responsibilities of trustees and examiner

The charity's trustees are responsible for the preparation of the accounts in accordance with the terms of the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006. The charity trustees consider that the audit requirement of Regulation 10(1) (a) to (c) of the 2006 Accounts Regulations does not apply. It is my responsibility to examine the accounts as required under section 44(1) (c) of the Act and to state whether particular matters have come to my attention.

### Basis of independent examiner's statement

My examination is carried out in accordance with Regulation 11 of the 2006 Accounts Regulations. An examination includes a review of the accounting records kept by the charity and a comparison of the accounts presented with those records. It also includes consideration of any unusual items or disclosures in the accounts, and seeks explanations from the trustees concerning any such matters. The procedures undertaken do not provide all the evidence that would be required in an audit, and consequently I do not express an audit opinion on the view given by the accounts.

### Independent examiner's statement

In the course of my examination, no matter has come to my attention [other than disclosed below\*]

1. which gives me reasonable cause to believe that in any material respect the requirements:

- to keep accounting records in accordance with Section 44(1) (a) of the 2005 Act and Regulation 4 of the 2006 Accounts Regulations
- to prepare accounts which accord with the accounting records and comply with Regulation 8 of the 2006 Accounts Regulations

have not been met, or

2. to which, in my opinion, attention should be drawn in order to enable a proper understanding of the accounts to be reached.

Name:

Relevant Professional qualification/professional body:

Address:

Date:

\* Please delete the words in brackets if they do not apply. If the words do apply set out those matters which have come to your attention.

### Example 4.3 Examiner's unqualified report for a charitable company

#### Independent Examiner's Report to the Trustees of 'ABC' Company

I report on the accounts of the charity for the year ended xx xxxx 20xx which are set out on pages xx to xx.

#### Respective responsibilities of trustees and examiner

The charity's trustees (who are also the directors of the company for the purposes of company law) are responsible for the preparation of the accounts in accordance with the terms of the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006. The charity trustees consider that the audit requirement of Regulation 10(1) (a) to (c) of the 2006 Accounts Regulations does not apply. It is my responsibility to examine the accounts as required under section 44(1) (c) of the Act and to state whether particular matters have come to my attention.

#### Basis of independent examiner's statement

My examination is carried out in accordance with Regulation 11 of the 2006 Accounts Regulations. An examination includes a review of the accounting records kept by the charity and a comparison of the accounts presented with those records. It also includes consideration of any unusual items or disclosures in the accounts, and seeks explanations from the trustees concerning any such matters. The procedures undertaken do not provide all the evidence that would be required in an audit, and consequently I do not express an audit opinion on the view given by the accounts.

#### Independent examiner's statement

In the course of my examination, no matter has come to my attention [other than disclosed below\*]

1. which gives me reasonable cause to believe that in any material respect the requirements:

- to keep accounting records in accordance with Section 44(1) (a) of the 2005 Act and Regulation 4 of the 2006 Accounts Regulations
- to prepare accounts which accord with the accounting records and comply with Regulation 8 of the 2006 Accounts Regulations

have not been met, or

2. to which, in my opinion, attention should be drawn in order to enable a proper understanding of the accounts to be reached.

Name:

Relevant Professional qualification/professional body:

Address:

Date:

\* Please delete the words in brackets if they do not apply. If the words do apply set out those matters which have come to your attention.

## **Example 4.4 Examiner's qualified report for a charity preparing receipts and payments accounts with a matter to be reported**

### **Independent Examiner's Report to the Trustees of 'ABC' Trust**

I report on the accounts of the charity for the year ended xx xxxx 20xx which are set out on pages xx to xx.

#### **Respective responsibilities of trustees and examiner**

The charity's trustees are responsible for the preparation of the accounts in accordance with the terms of the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006. The charity trustees consider that the audit requirement of Regulation 10(1) (d) of the 2006 Accounts Regulations does not apply. It is my responsibility to examine the accounts as required under section 44(1) (c) of the Act and to state whether particular matters have come to my attention.

#### **Basis of independent examiner's statement**

My examination is carried out in accordance with Regulation 11 of the 2006 Accounts Regulations. An examination includes a review of the accounting records kept by the charity and a comparison of the accounts presented with those records. It also includes consideration of any unusual items or disclosures in the accounts, and seeks explanations from the trustees concerning any such matters. The procedures undertaken do not provide all the evidence that would be required in an audit, and consequently I do not express an audit opinion on the view given by the accounts.

#### **Independent examiner's qualified statement**

In the course of my examination, no matter has come to my attention other than that disclosed below.

1. which gives me reasonable cause to believe that in any material respect the requirements:
  - to keep accounting records in accordance with Section 44(1) (a) of the 2005 Act and Regulation 4 of the 2006 Accounts Regulations
  - to prepare accounts which accord with the accounting records and comply with Regulation 9 of the 2006 Accounts Regulationshave not been met, or
2. to which, in my opinion, attention should be drawn in order to enable a proper understanding of the accounts to be reached.

The matter that has come to my attention is that, in the course of my examination of the accounting records of the charity, it was noted that some transactions relating to the restricted funds of the charity were not separately identifiable. This has led to the accounts only showing some of the income and expenditure that relates to these funds within the correct column. The charity trustees are aware of the importance of maintaining full records of such transactions going forward.

Name:

Relevant Professional qualification/professional body:

Address:

Date:

## **Example 4.5: Examiner's qualified report for a cross border non-company charity preparing fully accrued accounts with a matter to be reported**

### **Independent Examiner's Report to the Trustees of 'ABC' Trust**

I report on the accounts of the charity for the year ended xx xxxx 20xx which are set out on pages xx to xx.

#### **Respective responsibilities of trustees and examiner**

The charity's trustees are responsible for the preparation of the accounts in accordance with the terms of the Charities and Trustee Investment (Scotland) Act 2005, the Charities Accounts (Scotland) Regulations 2006 and the Charities Act 1993. The charity trustees consider that the audit requirements of Regulation 10(1) (a) to (c) of the Charities Accounts (Scotland) Regulations 2006 and section 43(2) of the Charities Act 1993 do not apply. The charity is preparing accrued accounts and I am qualified to undertake the examination by being a qualified member of [named body].

It is my responsibility to:

- examine the accounts under section 44(1) (c) of the Charities and Trustee Investment (Scotland) Act 2005 and section 43 of the Charities Act 1993
- to follow the procedures laid down in the general Directions given by the Charity Commission under section 43(7)(b) of the Charities Act 1993
- to state whether particular matters have come to my attention.

#### **Basis of independent examiner's statement**

My examination is carried out in accordance with Regulation 11 of the Charities Accounts (Scotland) Regulations 2006 (the 2006 Accounts Regulations) and the general Directions given by the Charity Commission. An examination includes a review of the accounting records kept by the charity and a comparison of the accounts presented with those records. It also includes consideration of any unusual items or disclosures in the accounts, and seeks explanations from the trustees concerning any such matters. The procedures undertaken do not provide all the evidence that would be required in an audit, and consequently I do not express an audit opinion on the view given by the accounts.

## **Independent examiner's statement**

In the course of my examination, no matter has come to my attention other than that disclosed below.

1. which gives me reasonable cause to believe that in any material respect the requirements:

- to keep accounting records in accordance with Section 44(1) (a) of the 2005 Act, Regulation 4 of the 2006 Accounts Regulations and section 41 of the Charities Act 1993
- to prepare accounts which accord with the accounting records and comply with Regulation 8 of the 2006 Accounts Regulations and the requirements of the Charities Act 1993

have not been met, or

2. to which, in my opinion, attention should be drawn in order to enable a proper understanding of the accounts to be reached.

The matter that has come to my attention is that the format of the accounts does not comply with the 2005 Charities SORP on the basis that a profit and loss account has been included and not a Statement of Financial Activities. As such, there is no distinction between the unrestricted and expendable endowment funds held by the charity on the face of the primary financial statements. There is however a breakdown of what is contained within these funds at the year end date within the notes to the accounts.

Name:

Relevant Professional qualification/professional body:

Address:

Date:

## **Appendix 5: Example letter of appointment**

The following example may be used to agree the terms between the charity trustees and an independent examiner, particularly where the role is undertaken by an unpaid volunteer.

Where additional services are also provided – for example, the preparation of the charity’s accounts – an additional agreement would also be recommended.

The Trustees

XYZ Charity

Date

Dear Sirs,

### **Charity Name**

The aim of this letter is to set out the basis on which I act as Independent Examiner for the charity.

### **Roles**

As Trustees, you are responsible for maintaining proper accounting records and preparing the financial statements. You are also responsible for making available to me all of the charities accounting records and related papers as required.

As Independent Examiner, I have a responsibility to report whether the accounts are drawn up in a manner consistent with the founding documentation of the charity and The Charities Accounts (Scotland) Regulations 2006. The responsibilities for any other services provided will be agreed in advance through a further Letter of Appointment.

### **Timetable**

As we discussed, the following is a proposed timetable:

Books received from trustees:                      date

Expected completion of examination:            date

Date of Trustees' Finance Meeting:            date

Date of Annual General Meeting:                date

### **Fees**

My work is undertaken on a voluntary basis and no fee shall be raised to the charity for my examination.

### **Or**

My fee for the independent examination will be £X and is due on completion of the examination.

### **Proceeds of Crime Act 2002 and Serious Organised Crime and Police Act 2005**

Under certain circumstances, the above legislation may require me to make a money laundering disclosure in relation to information obtained during my examination.

In addition, in some cases I have a statutory duty to report matters to the Office of the Scottish Charity Regulator (OSCR).

I should be grateful if you could confirm in writing your agreement to the terms of this letter by signing below. Once agreed this letter will remain effective from date of signature until it is replaced. You or I may agree to vary or terminate this appointment at any time, which must be given in writing.

Yours faithfully,

## **Appendix 6: Glossary of terms**

### **Accrued accounts**

Fully accrued accounts allocate the costs or income of a particular activity according to when the liability is incurred or when there is entitlement or certainty about income. This is not necessarily the date on which money is received or paid out.

### **Accounting and Reporting by Charities: Statement of Recommended Practice (SORP)**

In March 2005 the Charity Commission for England and Wales issued Accounting and Reporting by Charities: Statement of Recommended Practice (the 2005 Charities SORP). The SORP aims to improve the quality of financial reporting by charities. The second edition of the 2005 Charities SORP was published in May 2008 and may be downloaded from the OSCR website.

### **Assets**

Assets are property, goods, money, investments, rights to receive money in the future and logos, names, data and other intellectual property belonging to the charity.

### **Audit**

An audit is an examination of an organisation's accounts carried out by someone eligible to act as an auditor in terms of section 1212 of the Companies Act 2006. Where the audit is being carried out on accrued accounts it will be carried out following the International Standards on Auditing. The opinion on accrued accounts will state whether the accounts give a true and fair view of the financial affairs of the organisation. A true and fair view cannot be given on receipts and payments accounts and the auditors' opinion will state whether the statement of accounts properly presents the receipts and payments and its statement of balances.

### **Close relative**

Close relatives are children, parents, grandchildren, grandparents, brothers or sisters, and any spouse of these. See also 'connected person'.

### **Constitutional form**

Every charity is constituted in some way – companies are constituted by a Memorandum and Articles of Association for example and Trusts by a Trust Deed.

### **Constitutional requirement**

A provision within the constitution or governing document of the charity that, for example, requires an audit to be carried out in relation to the annual accounts or makes a reference to the appointment of an 'auditor'.

### **Contingent liabilities**

Contingent liabilities are liabilities that may arise from past events but whether they will, or how much they may be, is not yet certain.

### **Connected person**

A connected person is a person connected to a charity trustee by virtue of being:

- a close relative
- a spouse, civil partner or person with whom the charity trustee is living in an equivalent relationship
- any institution, corporate body or Scottish partnership where the charity trustee, or person connected to the trustee, has a controlling or substantial interest.

### **Designated fund**

A designated fund is that part of the charity's unrestricted funds that the charity trustees have decided to earmark, or designate, for a particular purpose.

### **Donated facilities and services**

Donated facilities and services are gifts to the charity of facilities, services of volunteers or beneficial loan arrangements.

### **Enactment**

An enactment includes Acts of both the Scottish and Westminster Parliaments and any subordinate legislation. Examples would be the Companies Act 2006, or the Charities and Trustee Investment (Scotland) Act 2005.

### **Endowment funds**

An endowment is a capital fund which is held for the benefit of the charity. The objective is to provide the charity with an income from the capital fund. There are two forms of endowment:

- a permanent endowment is one where the charity trustees must permanently maintain the whole of the fund. The charity trustees will not have the power to spend the capital as income
- an expendable endowment is one where the charity trustees have the option, under certain circumstances, to spend the capital.

Normally the governing document of the charity or the directions of the donor of the endowment will specify how the income from the endowment can be used and therefore whether the income should be included in the accounts as restricted or unrestricted.

### **Fully accrued accounts**

See 'Accrued accounts'

## **Gross income**

A charity's gross income is the total income of the charity for that particular year excluding any monies that are placed into an endowment fund (i.e. the initial set up of such a fund or any subsequent injection of new capital). Transactions that change the composition of the assets of an endowment fund are not included within gross income. Any income that has been collected specifically for and passed onto a third party (e.g. that part of a membership fee that is passed onto a parent body, or a collection held for another charity) should be excluded. However, the transferred amount should be recorded by way of a note to the accounts.

## **Independence**

Where a person is not involved in, and has no control over, the management and administration of a charity. Any 'connected person' cannot be independent.

## **Independent examination**

Independent examination is a less onerous form of external scrutiny than an audit and is usually available, under the 2006 Regulations, for charities with a gross income under £500,000. An independent examiner reviews the accounting records kept by the charity and compares them with the accounts prepared from those records. The examiner then writes a report which provides the information required by the Regulations and provides an assurance of whether or not anything has been found that needs to be brought to the attention of readers of the accounts.

## **Independent examiner**

An independent person whom the charity trustees reasonably believe to have the requisite ability and practical experience to carry out a competent examination of the accounts or, where accruals accounts are prepared, a professionally qualified person recognised by charity law.

## **Liability/Liabilities**

A liability is an obligation to transfer to another body some economic benefit usually, but not always, a sum of money.

## **Materiality**

There is no formal definition of what is 'material' but the concept may be more meaningfully explained by way of an example.

Consider the sum of £100.

- If the total income of the charity is £500, then £100 is material. However, if total income is £100,000 then £100 is probably not material.
- If the £100 in question indicates criminal activity, then it is probably always material. If it is included or omitted from the accounts due to a genuine mistake, it is not so likely to be material.
- Where it is more difficult to assess materiality from income, say £2,000 income where the £100 represents 5% of the income, the examiner should consider the nature of the mistake and the nature and context of the charity itself. For example, a loss of £100 in a charity working with young people on low incomes which offers advice on personal budgeting would probably be material. This is because the reputation of the charity could be damaged if the loss were made public. However, if the charity was a small arts charity putting on a couple of performances or exhibitions a year, the potential damage to its reputation may make the £100 error not material.
- Examiners need to be mindful of the cumulative impact of errors. One error of £100 may not be material, but three or four similar errors may indicate issues that require to be resolved.

## **Receipts and payments accounts**

Receipts and payments accounts are a simple form of accounting that consist of a summary of all monies received and paid via the bank and in cash by the charity during its financial year, along with a statement of balances.

## **Registered auditor**

A registered auditor is someone eligible to act as an auditor in terms of section 1212 of the Companies Act 2006.

## **Reserves**

General reserves are unrestricted funds held by a charity and are freely available to spend on any of the charity's purposes. This would exclude endowment and restricted funds.

## **Restricted fund**

Restricted funds are funds that can only be used for the particular purposes specified by the donor. For example, if a local authority provides a grant to a local charity to refurbish the community hall, the grant is a restricted fund that can only be used for the purpose it was given, in this case refurbishing the hall. Another example would be if a charity carries out an appeal for a particular purpose. The money raised by the appeal would be a restricted fund and should only be used for the purpose of the appeal. Income from assets held in a restricted fund (e.g. interest) will be subject to the same restriction as the original fund unless the terms of the original restriction say otherwise.

## **SORP**

See 'Accounting and Reporting by Charities'

## **True and fair**

Accounts that are prepared on a fully accrued basis in accordance with UK Generally Accepted Accounting Practice are considered to provide a 'true and fair' view as they include all assets and liabilities of the organisation at the period end date.

## **Unrestricted fund**

Unrestricted funds are funds that the charity trustees are able to use for any of the charity's purposes. Donations that are not given for a specific purpose would be an unrestricted fund (e.g. membership fees). Income from these funds is also unrestricted and can be used for any of the charity's purposes at the discretion of the charity trustees. Charity trustees may decide to earmark part of a charity's unrestricted funds for a particular purpose, e.g. major repair works. These sums are designated for that purpose and should be accounted for as part of the charity's unrestricted funds.

## **Appendix 7: Sources of advice and support**

### **App 7.1 Sources of advice**

**Office of the Scottish Charity Regulator (OSCR).** OSCR is the Regulator for charities in Scotland and provides information and guidance on charity law and regulation in Scotland. Contact: OSCR, Quadrant House, 9 Riverside Drive, Dundee DD1 4NY or 01382 220446 or visit [www.oscr.org.uk](http://www.oscr.org.uk).

**The Charity Commission.** The Charity Commission is the Regulator for charities in England and Wales and provides information and advice on matters affecting charities in England and Wales. Contact: Charity Commission Direct on 0845 3000218 or [www.charity-commission.gov.uk](http://www.charity-commission.gov.uk).

**Companies House.** The Registrar of Companies in Scotland offers a wide range of services and guidance booklets. Contact: Companies House, 37 Castle Terrace, Edinburgh EH1 2EB or 0870 33 33 636 or [www.companieshouse.org.uk](http://www.companieshouse.org.uk).

**Scottish Council of Voluntary Organisations (SCVO).** SCVO is the national body representing the voluntary sector and provides advice, information, support and assistance to charities. Contact: SCVO, Mansfield Traquair Centre, 15 Mansfield Place, Edinburgh EH3 6BB or the information service on 0800 169 0022 or [www.scvo.org.uk](http://www.scvo.org.uk)

**Third Sector Interface.** Every local authority area has a Third Sector Interface that provides advice, information and assistance to charities. Their contact details can be found in the phone book, libraries or on the Voluntary Action Scotland website at [www.voluntaryactionscotland.org.uk](http://www.voluntaryactionscotland.org.uk).

## **App 7.2 Professional bodies**

The Institute of Chartered Accountants of Scotland. Contact: **[www.icas.org.uk](http://www.icas.org.uk)**

The Institute of Chartered Accountants in England and Wales. Contact: **[www.icaew.co.uk](http://www.icaew.co.uk)**

The Institute of Chartered Accountants in Ireland. Contact: **[www.icaei.ie](http://www.icaei.ie)**

The Association of Chartered Certified Accountants. Contact: **[www.accaglobal.com](http://www.accaglobal.com)**

The Association of Authorised Public Accountants. Contact: **[www.accaglobal.com](http://www.accaglobal.com)**

The Association of Accounting Technicians. Contact: **[www.aat.co.uk](http://www.aat.co.uk)**

The Association of International Accountants. Contact: **[www.aia.org.uk](http://www.aia.org.uk)**

The Chartered Institute of Management Accountants. Contact: **[www.cimaglobal.com](http://www.cimaglobal.com)**

The Institute of Chartered Secretaries and Administrators. Contact: **[www.icsa.org.uk](http://www.icsa.org.uk)**

The Chartered Institute of Public Finance and Accountancy. Contact: **[www.cipfa.org.uk](http://www.cipfa.org.uk)**

The Association of Charity Independent Examiners (ACIE). Contact: **[www.acie.org.uk](http://www.acie.org.uk)**

The Accounts Commission for Scotland. Contact: **[www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)**

The Auditor General for Scotland. Contact: **[www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)**

### **App 7.3 Publications**

**Accounting and Reporting by Charities: Statement of Recommended Practice, (revised 2005).** From the Charity Commission. Contact: [www.charity-commission.gov.uk](http://www.charity-commission.gov.uk) or CCH on 0870 777 2906. Copies can also be downloaded from the OSCR website at [www.oscr.org.uk](http://www.oscr.org.uk)

**Scottish Charity Accounts: A Guide to the 2006 Regulations.** Copies can be downloaded from the OSCR website at [www.oscr.org.uk](http://www.oscr.org.uk)

**Scottish Charity Accounts: OSCR Receipts and Payments Accounting Workpack.** Copies can be downloaded from the OSCR website at [www.oscr.org.uk](http://www.oscr.org.uk)

**Charity Reorganisation guidance.** Copies can be downloaded from the OSCR website at [www.oscr.org.uk](http://www.oscr.org.uk)

**Consents and Notifications guidance.** Copies can be downloaded from the OSCR website at [www.oscr.org.uk](http://www.oscr.org.uk)



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