The Charity Law & Practice Review

THE CHANGING FACE OF THE CHARITY TREASURER AND BOOKKEEPER: ASSESSING THE IMPACT OF THE CHARITIES ACT 1993

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Abstract

The Charities Act 1993 introduced a major new *statutory* regime for charity accounting. Most community-based voluntary organisations *are* charities, and so affected by the rules. It was clear from the outset that major consequences would emerge for treasurers and for bookkeepers/finance workers in smaller voluntary organisations (referred to collectively as the "finance role").

The present research represents the results of a four year study of this issue, drawing on qualitative work with over 300 organisations, and in depth work with 50 groups. Multiple methods of investigation were employed, largely based on naturally occurring data, and including significant use of action research, to give a rich model of the trends emerging. The focus is on charities with total income between £10,000 and £250,000.

The paper outlines the new legal requirements, and identifies seven major areas in which these have had significant impact on the finance role in smaller charities. From this impact, four patterns of response are identified, categorised as "withdrawal", "ignoring completely", "ignoring until year end", and "involvement", and the consequences of each pattern are considered.

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The research focuses on organisations in the latter group, where an individual in the finance role sought to engage to at least some extent with the requirements of the new regime, and consequences of that engagement are analysed. The consequences include some significant changes in the function and status of the finance role within the organisation.

Five major conclusions are drawn from the study. In general it is argued that the sector has coped well with a huge change in the statutory environment and that the quality of financial management has improved, but the level of compliance appears significantly different between registered and excepted charities. Some cultural changes in the finance role are reported, affecting not just voluntary organisations but also the accountancy profession. The emergence of the new role of independent examiner is also assessed.

1. Purpose and Approach of the Research

1.1 Purpose of the Study

The new accounting regime introduced in England and Wales under the Charities Act 1993[2] has created a new form of statutory regulation affecting much of the voluntary sector. Most voluntary organisations with non-trivial income *are* charities and so affected by the rules: the requirements apply both to registered charities and excepted charities (such as places of worship). In fact one of the new developments introduced by the Act is that it is now compulsory for all organisations with charitable objects to apply for registration as charities if their income exceeds £1000 per annum[3] apart from those categories that are specifically excepted or exempted.

So, apart from those voluntary organisations which exist purely for the benefit of their members (such as private sports clubs), or which have political (non-charitable) objects, almost all voluntary organisations in England and Wales are subject to the new regime.

Even in larger charities, with ready access to professional advisers and trained finance staff, the impact has been considerable. But it was clear from the outset, simply by reviewing the content of the legislation, that major consequences would

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2 *Charities Act 1993*, as amended by Orders and by the *Deregulation and Contracting Out Act 1994*. The accounting requirements are contained in Part VI of the Act and secondary legislation.

3 Charities Act 1993 s.3(2).

emerge for treasurers and for bookkeepers or finance staff in smaller voluntary organisations. In understanding the sector, it is important to assess what impact this new regime would have (positive and negative).

It was thus expected that the study would reveal much about: (a) how the sector responds to new regulation; and (b) the quality of financial management in the voluntary sector.

1.2 Terminology

The term "charity" in this paper refers to any organisation in England and Wales subject to the new rules: the organisations studied include registered charities and a number of churches, which are excepted charities (see above).

The term "treasurer" is used to refer to a *trustee* who takes particular responsibility for finance issues in the charity. In small charities, the treasurer may maintain all the day to day accounting records and produce the year end accounts, with no support at all from paid staff. In slightly larger organisations, the role of the treasurer may be more concerned with advising the trustees on financial policy, but with the actual bookkeeping delegated to a member of staff. Some treasurers in the study were drawn from a professional background such as accounting or banking, but many had learned the role informally.

The term "finance worker" is used to refer to a *member of staff* whose post includes responsibility for bookkeeping or financial management. In many cases, the finance worker was employed as an administrator with many duties other than finance; sometimes the finance worker was also the manager. Very few of the finance workers studied had any formal accounting training.

The term "finance role" is used to refer collectively to *all* those responsible on a day to day basis for financial issues in the charity: i.e. the treasurer *and/or* finance worker(s).

1.3 Research Methodology

The author was in the fortunate position of having convenient access to a great deal of practical data concerning the impact of the new regime on smaller charities, and the research approach was structured to take advantage of that.

A qualitative method was used, based (a) on naturally occurring data; (b) on a participant observation role through training events; and (c) an action research role by the author, arising out of consultancy work being undertaken in any case.[4] The aim was to gain maximum possible immersion into the issues that the new accounting regime was raising, specifically for smaller and locally-based voluntary organisations.

Six specific means of engagement were used to develop an understanding of these issues, over a four year period from 1995 to 1999. These are as follows.

(a) The author had some contact with the Home Office and the Charity Commission in 1994/95 as the regulations for the new regime were going through consultation: he attended a number of seminars at that time, and made submissions at the consultation stage. This served to provide an understanding of the central issues.

(b) A software package[5] was developed for use by small to medium charities to maintain accounts under the new rules: the impact which this software might or might not have would reveal a great deal about motivation of voluntary organisations to comply with the new regime. Equally, the queries, problems, and feedback from organisations seeking the use of such a package would indicate those aspects of the new regime that presented particular difficulties. By late 1998 several hundred users of this software were involved.

(c) Training workshops were presented on the new regime[6] for treasurers and finance workers from approximately 160 organisations in the period 1995-1999. These were undertaken in small groups (usually no more than twelve

4 This work was undertaken through *The Kubernesis Partnership*, a small firm of charity consultants in which the author is a partner.

5 The package is the *Kubernesis Accounting System* (KAC), a nominal ledger system designed for fund accounting in small to medium charities. Earlier versions of this had existed prior to the new regime introduced by the Act, but in autumn 1995, KAC Version 3 was released, offering smaller charities the means to keep accounts distinguished by fund, and to produce a year end Statement of Financial Activities and Balance Sheet in the layout required under the new rules; it can also be used for multi-fund receipts and payments accounts. KAC Version 4 was released in autumn 1997, giving further facilities for medium-sized charities. The research draws on charities using KAC V3 and V4.

6 Some of the workshops were directly arranged by the Kubernesis Partnership but the majority were presented by the author under the auspices of other voluntary sector training providers. Hence a wide cross section of voluntary organisations were involved, with a wide range of existing accounting procedures.

persons at any one workshop, often less) with an emphasis on feedback and discussion of individual practice.

(d) Individual work was undertaken with approximately 25 organisations on defining charts of accounts for their specific implementation of the new regime (linked with (b)). Some further consultancy work on certain aspects of accounting procedures was undertaken with a further ten organisations.

(e) The author acted as Independent Examiner for twelve sets of charity accounts in the period 1997-99. The role of independent examiner is a crucial part of the new charity accounting regime. It is now a legal requirement for charities with an income over £250,000 to have a professional audit; but unincorporated charities below this can opt for an independent examination (IE). An IE does not generally require a professional accountant, but the IE requirements are laid down by law, and cover much more than "informal audits" which many voluntary groups had in the past. Conducting an IE gives a great deal of insight into a charity's approach to the finance role. Further insights were also obtained via informal feedback from other independent examiners, through a new Association of Charity Independent Examiners.[7]

(f) The author has worked closely with a small grant-making trust which asks all grant applicants (if their application is within the trust's criteria) to send in a copy of their accounts. As a result, over 150 sets of charity accounts were seen and studied to assess the level of understanding and implementation of the new accounting rules. These charities applying for grants demonstrated a huge range of accounting approaches, and are quite distinct to the organisations included in the other categories above.

Overall, this approach allowed use of *some* data from well over 300 charitable organisations, and detailed data (based on face to face work with treasurers and finance officers) from approximately 50 organisations. The charities studied had income ranging from £200.00 to £5M, though the vast majority were under £250,000.

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7 The *Association of Charity Independent Examiners* was formally launched in January 1999, and is now a registered charity in its own right. At the time of writing (November 1999) it has approximately 250 members. It is a voluntary body serving both accountants and non-accountants who act as independent examiners. The author has been appointed General Secretary to the Association.

The focus of the study is on charities with income between £10,000 and £250,000: sufficient to require that accounts have to be sent to the Charity Commission (if the organisation is a registered charity), but not large enough to require a professional audit.

The majority of the organisations studied were unincorporated, though there were some charitable companies (for which there are some differences in the accounting regime, as the organisation has to comply with company law as well as charity law). Since the charitable companies were only a small proportion, this paper is written in terms of the accounting principles applicable to unincorporated charities, unless mentioned otherwise.

Only one of the organisations studied had a trading subsidiary company: the issues of trading subsidiaries and consolidated accounts are considered beyond the scope of this paper, as they are rare in charities of this size.

2. Outline of the New Charity Accounting Regime

In England and Wales, unincorporated charities are now subject to four levels of regulation regarding their accounts and accounting procedures. In summary, this regime is as follows.

(a) The Charities Act 1993("the Act") requires charities to keep proper accounting records, produce published accounts, and have them audited or independently examined (according to income). The Act allows the published accounts to be on a receipts and payments basis up to £100,000 income; beyond this accruals accounts are required.

(b) The Charities (Accounts and Reports) Regulations 1995[8] ("the Regulations") set out exactly what has to appear in published accounts produced on the accruals basis, and also determine the duties of auditors and independent examiners.

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8 Charities (Accounts and Reports) Regulations 1995 SI 1995/2724.

(c) The Statement of Recommended Practice on Accounting by Charities[9] ("the SORP") is a statement of accounting practice which goes further than the regulations. The Charity Commission has stated that they expect the accounts of charities to comply with the SORP,[10] and moreover the Regulations require charities over £100,000 to state the accounting standards used and give details of any departures. Hence, the SORP is to all intents and purposes a mandatory part of the new regime. Various "Mini-SORPs"[11] simplify the full SORP for smaller charities.

(d) Directions and guidance by the Charity Commission also form part of the new statutory regime: for example the Commission was empowered under the Act to give directions on the steps that must be carried out by an independent examiner,[12] and these directions make clear, for example, that even the smallest charities must properly distinguish their restricted funds.

Because of the various thresholds in the Act, the requirements increase according to the total income of the charity: table I summarises these. At each level the *additional* requirements are stated but all the requirements of smaller charities also apply. (The table is only a summary of key principles.)

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9 Statement of Recommended Practice on Accounting by Charities (Charity Commission, October 1995. Published with approval by the Accounting Standards Board.)

10 Statement of Recommended Practice on Accounting by Charities p2.

11 *Accruals Accounting for the Smaller Charity* (October 1995); *Accounting for the Smaller Charity (on a receipts and payments basis)* (October 1995); *Charity Accounts: Charities under the £10,000 Threshold* (March 1996). (All published by the Charity Commission.)

12 General Directions of the Charity Commissioners under s.43(7)(b) of the Charities Act 1993 on the Carrying Out of an Independent Examination published in *The Carrying Out of an Independent Examination: Directions and Guidance Notes* (Charity Commission, March 1996).

Income of Charity	**Summary of minimum accounting requirements under the new regime** (unincorporated charities)
< £1,000	Must keep proper accounting records "sufficient to disclose the financial position of the charity at any time" kept for six years. Must produce published accounts at year end (can be on receipts and payments basis), available to members of public on request
£1,000 to £10,000	Organisation must become a registered charity, unless specifically exempt or excepted.
£10,000 to £100,000	Accounts must at least be subject to Independent Examination. Accounts must be sent to Charity Commission (registered charities).
£100,000 to £250,000	Accounts must be on accruals basis, complying fully with Regulations and SORP: hence presentation must use SOFA* and Balance Sheet and all required notes.
> £250,000	Accounts must be subject to professional Audit.

* SOFA = *Statement of Financial Activities* - the new primary financial statement in charity accounts, analysing income and expenditure into certain categories, and presented in multiple columns for unrestricted, restricted, and capital funds.

Table I *- Summary of Charity Accounting Requirements by Income*

The new regulations came into effect for accounting years starting on or after 1 March 1996,[13] and organisations are allowed up to ten months after year end to complete their published accounts[14] and send them to the Charity Commission. It follows that even with the latest possible accounting year, and the maximum possible delay in producing the accounts, all charities should have produced at least one set of accounts under the new rules by December 1998. Charities with earlier accounting years and less delay in producing their accounts, and those who have sought to apply the principles as soon as they were published, may well have completed up to three years under the new regime.

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13 Charities (Accounts and Reports) Regulations 1995 reg 1.

14 Charities Act 1993 s.44(3) & (4).

The table summarises the minimum requirements: some charities are subject to additional requirements imposed by funders or by umbrella bodies to which they belong: a major example is the *Church Accounting Regulations*[15] that apply to Church of England Parochial Church Councils.

3. Specific Impacts on Smaller Charities

Analysis of all the organisations included in the study led to the identification of many different consequences where the new regime had prompted some kind of changed practice.

The SORP and Regulations between them cover a huge range of issues, but not all were relevant to the charities in this study: for example, the requirement in the SORP to show investment assets at market value (which was seen by many accountants as a big change[16]) only affected a very few organisations, since many smaller charities have no long term investment assets at all.

However, from a large number of issues identified in relation to specific organisations, seven major themes were observed. These major areas of impact each involved large numbers of smaller charities having to make changes to their practices to comply with the new regime.

3.1 Proper Accounting Records At All Times

The need to keep proper accounting records able to reveal the financial position of the charity at any time means that many charities have had to adopt new approaches to keeping basic accounting records.

Some very small groups that formerly relied on "shoe box accounting" where no regular records were kept during the year have started to keep proper manual books. In slightly larger organisations, concern at books that were only comprehensible to the one person such as the treasurer, has created some impetus towards use of computer systems. Even where proper manual books or computer systems were used they were often only brought up to date many months in arrears: the new

15 Church Accounting Regulations 1997 GS 1255, General Synod of the Church of England. (In *The Charities Act 1993 and the PCC*, Church House Publishing, 1997).

16 For example *Charities Newsletter* No 11, September 1997, p.2 (Moores Rowland Chartered Accountants).

regime has caused trustees to put some pressure on those in the finance role to keep the accounts reasonably up to date, with regular reports to trustees.

3.2 Fund Accounting

The concept of keeping accounts in funds ("pots" of money or resources held for specific purposes) long predates the new accounting regime, as it is a basic matter of trust law. In some sectors such as churches and grant-making charities, fund accounting was well established prior to the new regime, but many service-providing charities had, in the past, simply produced a single income and expenditure account, with no effective means of tracking donations for specific purposes.

Other organisations had worked on the basis of opening new bank accounts for every new fund or project, but this then gave rise to the problem that sometimes the year end accounts only disclosed the main fund of the charity, not the various funds held for special purposes. In some cases, with commercial style accounting systems, the different funds were being managed effectively as separate companies, with no real understanding of the overall financial position of the whole charity.

Also, the multi-bank account approach becomes unwieldy with more than two or three funds: one charity in the study had sixteen general bank accounts (a current and deposit account for each of eight projects) and large numbers of transfers were being made between the accounts for recharges between funds that could have been handled purely as book entries. Prior to implementing the software used in this study, the charity's finance workers were actively hostile to the idea of any grants for new purposes, because they would simply have been unable to cope with the proliferating numbers of accounts.

Under the new regime, *all* funds must be brought together on the SOFA, or for a charity under £100,000 working on a receipts and payments basis, a separate receipts and payments account is needed for each fund,[17] with the assets of all funds brought together on a "Statement of Assets and Liabilities".[18]

To cope with fund accounting, there is no need for separate bank accounts, provided a charity either maintains manual books distinguishing all income and expenditure by fund, or uses a computer system that can do this. Pressures of this kind were a major rationale for switching to software systems such as the one used in this study.

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17 Accounting for the Smaller Charity (receipts and payments basis) p.6 (Charity Commission, October 1995).

18 Charities Act 1993 s.42(3).

The demands of fund accounting have also led to trustees thinking much more about their responsibilities for *all* funds of the charity: the study revealed that in the past many trustees took no interest in projects which they saw as being the responsibility of others.

The need to bring together all funds of the charity has also created a new pressure on the overall treasurer of an organisation to incorporate funds held by subsidiary groups. This was particularly noticed with the churches, where the treasurer typically looked after two or three main church funds, but not the funds of youth groups, women's fellowships, parish magazines, etc. However, many service-providing charities were also found to have subsidiary money held for lunch clubs, bookstalls, etc.

In the past, many of these subsidiary groups were seen as handling their own funds with no interferences by the trustees or treasurer. In some cases the effect of the new regime is that subsidiary groups have been hived off, and required to constitute themselves as charities in their own right. But in most cases this was not a viable approach, and such subsidiary funds have had to be included in the main accounts of the charity. Examples were found where treasurers who were previously responsible for only one or two funds, found themselves having to produce accounts for a charity which in reality had fifteen or more funds.

3.3 More Elaborate End of Year Reporting

Although most of the groups studied had published some kind of year end accounts prior to the new regime, apart from the charitable companies such accounts had normally been very simple - often confined to a single page showing an income and expenditure account, possibly a balance sheet, the signature of the treasurer and possibly an honorary auditor, and often no annual report at all, other than perhaps some comments from key individuals.

However, the new regime introduced, for the first time, statutory provisions on the format of the annual report and accounts, which, for most of the organisations studied, were much more complex than they had been used to previously.

Under the Regulations and SORP, a charity using accruals accounting (compulsory over £100,000 but also chosen by many below that limit) has to provide a SOFA and Balance Sheet in a required layout, together with at least twenty issues that have to be disclosed by way of notes to the accounts, accompanied by a statutory annual report, and a proper independent examiner's or auditor's report. For even the simplest charity, it is hard to get this into less than around seven pages.

However, the principles of the SOFA caused less difficulty than expected, and most accounts containing a SOFA showed a reasonable attempt to fulfil the requirements. Detailed work with individuals established that the different columns of funds were easily understood (though some had difficulty with appreciating that several different restricted funds might be brought together in the one column). The analysis of income into donated income, investment income and trading income for charitable objects and for fundraising purposes was also readily appreciated and found to be helpful - although a different result was found on the random sets of accounts received by the small trust, there were many examples of SOFAs where the income categories bore little resemblance to those required by the Regulations.

Slightly more difficulty was found on the SOFA with allocating expenditure between expenditure on charitable objects, fundraising expenses, and management/ administration costs, which necessarily required judgment: for many in the finance role in small charities, the need to make assumptions and judgments in allocating expenditure was a wholly new concept. But whilst it was clear that very different criteria were used by different charities in making this allocation, all the SOFAs seen appeared to make a fair attempt at this. (The Regulations allow charities under £100,000 doing accruals accounting to dispense with this distinction,[19] but in the study no example was seen of a SOFA where this was done.)

Even with receipts and payments accounts, the need to show receipts and payments by fund plus a statement of assets and liabilities, once again accompanied by an annual report and an independent examination or audit report, means that few charities tackling the regime properly can rarely meet the requirements in less than four or five pages.

This result of these increased requirements meant that much more effort had to go into the process of producing year end accounts, and professional help was needed much more widely than in the past.

3.4 Accruals Accounting

For the larger charities in the study - those that were close to or over the £100,000 threshold - one of the biggest problems was the need to keep accounts on an accruals basis. This meant for the first time, distinguishing capital expenditure (so it could be capitalised as fixed assets and subsequently depreciated), and incorporating debtors and creditors (and in some cases accruals and prepayments) at year end.

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19 Charities (Accounts and Reports) Regulations 1995 Schedule I Part I item 5.

Apart from a few organisations where the treasurer was a professional accountant, almost all the charities in the study had kept accounts on a receipts and payments basis prior to the implementation of the new rules.

For those in the finance role with no formal accounting background, the principles of accruals accounting (although not specific to charities) were found to create much greater conceptual problems than the requirements of fund accounting.

Even once the principles were understood, there was considerable resistance from some to switching to accounting on an accruals basis, principally on the grounds that the trustees or funders would not then understand the accounts (or any interim management reports if the accruals basis was used in the normal records). The fact that fund balances would comprise fixed assets and debtors as well as cash at bank was seen as a major difficulty. Also, the process of incorporating *existing* fixed assets, at the start of the first year of accruals accounting, proved to be an extremely demanding task for many in the finance role.

Some organisations using professional accountants at year end worked by maintaining day to day books on a receipts and payments basis, leaving their accountants to deal with fixed assets, debtors and creditors purely in the year end accounts, but often this led to problems in relating the final accounts to the figures used in interim reports. Other treasurers and bookkeepers (generally those using the software mentioned) took on the task, with appropriate training, of keeping records on an accruals basis throughout.

Certainly those organisations which, in the past, had produced their accounts internally, were often reluctant to engage professional accountants if it could be avoided, even when passing the £100,000 threshold. The wording of the SORP, being written largely for trained accountants, was often an area of difficulty for this group.

3.5 Publications of Detailed Notes and Disclosures

For a significant minority of the charities in the study, the need to include specific disclosures in the notes to the accounts was a major barrier to address in terms of the internal culture of the organisation.

Under the Regulations, charities using accruals accounts are required to include notes to the accounts disclosing any remuneration or transactions with trustees and connected persons.[20] The definition of connected persons goes as far as grandchildren and business partners of trustees. Although not mandatory with receipts and payments accounts, such disclosures are still recommended by the Charity Commission.[21]

For those charities where trustees have little close involvement this presented little problem, but for others, particularly charities in small communities, it was found that many of the staff, or contractors who undertook work for the charity, were closely related to trustees, and hence the full financial details of the relationship had to be published as notes to the accounts. A particular problem arose in some independent churches, where the minister was a trustee and also received a salary, the amount of which in some cases was regarded as highly confidential.

In some cases, the need to disclose information led to trustees wishing to withdraw from particular roles, either as trustees, or from providing goods or services to the charity.

Other disclosures were largely seen as simply creating additional work: for example the need to establish total amounts spent on trustees expenses was often difficult if expenses paid to trustees were amalgamated with other volunteer expenses. On the other hand, the requirement in the SORP to disclose all staff salaries over £40,000 was normally met with the verbal response "Chance would be a fine thing"!

3.6 Trustees As A Whole Much More Responsible for Accounts

One very substantial effect of the new regime, observed in charities of all sizes in the study, was an increased understanding of the role and responsibility of trustees as a whole in relation to the accounts.

This is partly linked to more extensive education in general on trustee responsibilities, but for several of the charities studied where detailed interaction took place, the approval of the annual accounts by the trustees became an important issue, as trustees began to grasp their responsibility for the whole financial management of the charity.

The impression gained was that in the past, most charity trustees had seen finance and the production of accounts as the responsibility purely of the treasurer and/or

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20 Charities (Accounts and Reports) Regulations 1995 Schedule I Part IV items 1(c) and (e).

21 Accounting for the Smaller Charity (receipts and payments basis) p.16 (Charity Commission, October 1995).

finance worker, in some cases with some input at year end from an accountant. In many cases, the first time most trustees saw the accounts was when they were presented to a members' AGM: prior to the new regime, very few organisations went through a formal process of trustees approving the accounts *before* they were circulated.

Other pressures on trustees to take a more active responsibility for accounts came from auditors and independent examiners insisting on appointment by the trustees as a whole, and possibly circulating management letters to the full body of trustees.

3.7 New Arrangements for Audit/Independent Examination

The new requirements under the Act for audit or independent examination of accounts was found to have created a completely new relationship between charities and their accountants or examiners.

Of the charities studied, past practice fell into three groups:

(a) A few had never bothered with any independent scrutiny of the accounts at all.

(b) Some had a tradition of appointing an ordinary member of the organisation, or a sympathetic neighbour as an informal auditor.

(c) Some tried to find a local accountant who would "do the accounts" for little or no charge - often this was based on a long-standing arrangement.

Such relationships were fairly distant, with usually only the treasurer or bookkeeper having any contact with the person concerned.

However, the new regime marked major changes in this respect. Charities who had previously had no scrutiny began looking for independent examiners. Those who had previously acted as informal auditors either withdrew when their new responsibilities became clear, or needed extensive training and support to become effective independent examiners. Professional accountants who had previously done a few charity accounts as a sideline came to realise that charities were a specialist area: as a result, the free charity audit by a professional firm has become relatively rare.

The result for many charities has been a big increase in the fees for scrutiny of their accounts (often accompanied by a need to engage professional help in preparing the accounts as well as for the independent examination or audit).

4. Responses of Treasurers/Finance Workers

The previous section has summarised seven main areas of impact, which most of the charities in the study needed to address *if they were to comply* properly with the new regime (many charities had further issues to consider, specific to their own work or procedures).

However, few organisations were willing to comply with everything required under the new rules, particularly at first, and an analysis was made of the broad behavioural responses that arose, as those in the finance role started to become aware of the new rules. These are categorised under four headings.

The responses described here are those of the key person in the finance role. In some cases this was the treasurer; but many of the organisations studied had only a very distant relationship between the finance worker and the treasurer, or even no treasurer at all, and in these cases the response of the finance worker forms the basis of the approach taken.

4.1 Withdrawal

For many long standing treasurers and bookkeepers, the response to the new regime was to withdraw from the role with the typical comment: "This is all too much - I'm stepping down as treasurer." Similarly, there were cases of bookkeepers taking retirement, or being transferred to non-finance roles.

In most cases, this response was only discovered through contact with the *new* person in the finance role, who reported the reaction of their predecessor, so it was difficult to discover precisely what had caused the withdrawal. However, increased regulation is a common issue prompting retirement in all fields of work.

4.2 Ignoring Completely

The second category of response was typified by the comment: "I'm convinced that what we've always done is fine." Treasurers and finance workers taking this approach took the view that their existing accounting and reporting procedures were perfectly adequate, and little or no adverse consequences would follow from continuing with this. Sometimes this was compounded by the charity's "informal auditor" taking a similar line.

This view was particularly prevalent in organisations at the lower end of the income range, who were aware that the full regulations and SORP only applied to larger organisations, and who failed to appreciate that even receipts and payments accounts were affected by the new regime. Taking the accounts submitted to the small trust (section 1.3(f) above) many cases were found of organisations with income over £10,000 but under £100,000 where the accounts had nothing that could be said to constitute a Statement of Assets and Liabilities, and/or no independent examiner's report.

However, this view was also found in some charitable companies (even quite large ones in one or two cases, and sometimes supported by their accountants) who felt, provided they followed the Companies Act, that they were under no obligation to comply with the SORP.

4.3 Ignoring Until Year End

A third response by treasurers or finance workers was an acceptance of the issue, but leaving it entirely to someone else to deal with, as in the comment: "I'll keep the books as I've always done and let an accountant or someone sort it out at year end."

This strategy was certainly followed by many charities, and in a few cases, evidence was found where accountants were actively encouraging this. Provided proper accounting records were kept, there is nothing illegal about this approach, but it is difficult for the trustees to have effective financial control, and it can mean colossal work at year end.

4.4 Involvement

The fourth response was one of involvement, as indicated by the comment: "If this is something we have to do, I'd better find out more about it."

This does not necessarily mean the person in the finance role was an enthusiast for the new regime, but many people seemed to be saying that if the law or the Charity Commission now requires a new form of accounts, they were willing to do their best. Even when the key person in the finance role had little part in the preparation of the year end accounts, many were interested to understand the principles (often with the hope of reducing accountancy costs by doing more themselves).

4.5 Consequences of Each Pattern

As this was purely a qualitative study, no attempt has been made to assess the proportion of voluntary organisations in each category. Apart from the accounts sent into the small trust the sample of charities studied was far from random, and from looking purely at published accounts it is not easy to distinguish strategies 4.3 and 4.4, for example.

However, the consequences for organisations in relation to each of these patterns were studied, and can be categorised as follows.

The response of *withdrawal* has led to a shortage of treasurers for some organisations, leaving some charities in desperation regarding their financial management. A partial response has been a shift to more use of paid workers to handle accounts, but even in this respect there is a shortage of persons with proper bookkeeping skills *and* experience of charity accounting. There has also been more hands on involvement by accountants and other advisers, meaning greater costs for the organisations, at least in the short term.

In organisations where those in the finance role have *ignored* the rules, and sent accounts to the Charity Commission with no attempt at complying with the new regime, many are receiving Charity Commission letters requiring them to take action. The result is that the charity is forced to take action in the second year of the new regime, even if they ignored it initially. However, there remains a high level of non-compliance amongst excepted charities (e.g. churches) where there is no obligation to send accounts to the Charity Commission: in such cases the pressure to comply is very dependent on the diocese or similar umbrella body. In independent churches, the only pressure to comply comes from professional advisors, or from those within the organisation who have knowledge of the Act from other roles.

Charities which decide to *leave everything to an accountant at year end* have seen a huge rise in their audit/accountancy costs. Cases have been seen of charities where as much as 5% of income has been spent on accountancy, which may lead to questions from donors and funders. In some cases this has prompted a different strategy the following year.

Where treasurers or finance workers have been willing to take a step of *involvement* with the new regime, the research suggests that most are making progress. There is some increase in professional accountancy costs but much less than for those following a strategy of ignoring the issue. The study has focused on organisations in this category, and found that in general there is now good understanding of different restricted and unrestricted funds, for example, and many treasurers who had no previous knowledge of accruals accounting are coping well with concepts such as depreciation.

The production of a full set of accruals accounts complete with all required notes remains beyond the scope of most in the finance role, but as reported above, the crucial new report, the SOFA, has been well received and is even being used in some cases for receipts and payments accounts where multiple funds are involved.

In fact many trustees not specifically in a finance role are comfortable with looking at a SOFA on the grounds that it gives them a picture of the whole charity which in the past they found hard to obtain. The level of understanding of the SOFA was particularly strong in the charities mentioned in 1.3(b) and (d) where accounting records were linked automatically by software to the production of the SOFA and Balance Sheet, but training workshops mentioned in 1.3(c) with others from a wide range of charities found that most people in a finance role had little difficulty understanding the concepts of the SOFA.

4.6 Research Focus

The present research focused on the charities considered in section 4.4 where at least one person was making a serious attempt at understanding the new regime by taking part in workshops, using software to assist the task, or similar steps. Referring back to the research methodology in section 1.3, all those chosen for in categories 1.3(b) to (e) were to some extent taking an approach of involvement with the new regime. However, the assessment of a wide range of accounts submitted to a grant-making trust under 1.3(f) enabled this group to be compared with a wide range of other organisations.

5. Changes in the View of Voluntary Finance

The following changes in the organisations were observed or otherwise noted in relation to the impact of the new charity accounting regime, in charities where there was at least some degree of involvement with the new requirements.

5.1 Demand for Charity-specific Accounting Systems

Those seeking involvement in the new regime were seen to be quite willing to implement new accounting systems (manual or computerised). In some cases the solution was seen in improved manual systems, but only a few of those in the finance role wished to do full double entry manual bookkeeping (which is essential if fund accounts are to be kept without a separate bank account for each fund). Hence the distinct preference was for computerised systems.

Many of those who chose the specific computer-based accounting system used in this study (see 1.3(b)) had been prompted by frustrations with inadequate manual systems or by existing software designed primarily for small businesses rather than charities. For these subjects, the direct link to the year end reports was a major attraction. However, the training workshops also identified others who were using non-charity-specific software, and keeping track of funds simply within a suitable nominal coding structure, but with rather more done at year end by an accountant

5.2 Training

Substantial demand for training on the principles of the new charity accounting regime was observed: some of the workshops offered were over-subscribed, notwithstanding much other training on the SORP offered by other trainers. It became clear that some organisations which, in the past, have allocated training funds purely in relation to the service provision side of their work, were willing to fund training for those in the finance role. An interesting development has been the number of accountants who, not being charity specialists, chose to attend courses offered primarily for charity treasurers and finance workers.

Nevertheless, it would appear that those who have sought training or bought books,[22] software, or other guidance on the new regime only represent a small minority of the total number of charities in the £10,000 to £250,000 income range. The accounts received by the grant-making trust (1.3(f)) showed only a small minority of charities under £100,000 making a serious attempt at complying with the new rules, and even with those in the £100,000 to £250,000 range, compliance was often superficial with many areas overlooked.

It is clear that a huge need for charity finance training still exists, with many people in charity finance roles not even aware of their need to gain an appreciation of the new regime.

5.3 Greater Use of Professional Help

The research found that even those charities seeking active involvement in the new regime are seeking much more outside help. As reported in section 3.7, relationships with auditors and independent examiners are now much closer than in the past. Accountants are being asked to help the charity with accounting procedures, rather than just getting involved at year end, and the process of accounts preparation at year end is a much more comprehensive activity.

However, there was evidence in some charities of concern at the costs of this additional expenditure on professional services. Also, several cases were found of

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22 For example: Sayer, Kate *A Practical Guide to Accounting by Charities* (Directory of Social Change, 1996).

charities whose accountants were not charity specialists, where the charity was effectively having to educate their accountant on the new requirements.

5.4 Semi-professionalisation of the Finance Role

One significant consequence of the new regime has been the "semi-professionalisation" of the charity finance role. In the past, it was assumed in many charities that anyone with a basic knowledge of figures could be a treasurer or bookkeeper; often the role of bookkeeper was the most junior post in an organisation.

This has changed significantly as charities have begun to appreciate the responsibilities of the finance role. Once trustees are asked to approve a full set of accounts prepared under the Act, there is greater recognition of the underlying financial procedures in the charity. In one example, trustees who only thought of their charity as an organisation of £30,000 income (because they were only concentrating on the main fund) realised that they were actually managing a £120,000 income, and were willing to promote finance workers accordingly.

Also, at year end, or through training sessions, the finance workers themselves now have much more contact with their accountants than in the past, and are beginning to communicate in a similar language.

Other changes noted towards semi-professionalisation of the role include:

- job advertisements for bookkeepers calling for specific charity/voluntary sector finance experience;

- organisations which previously expected a voluntary treasurer to handle all the bookkeeping are recognising the need to employ finance workers as the complexity of the task increases;

- administrators and bookkeepers being enrolled on formal accountancy training programmes such as NVQs in accountancy, or the Association of Accounting Technicians (AAT);

- job titles such as "finance officer", "finance manager" or "financial controller" are emerging, even in organisations with under £250,000 income, emphasising the significance of this function;

- the development of bodies such as the Association of Charity Independent Examiners (which is now awarding a professional qualification) to support independent examiners, and an Association of Church Accountants & Treasurers in the church sector;

- the growth of Community Accountancy Projects, i.e. voluntary sector projects seeking to provide financial support for other voluntary organisations;

- provision of University courses specifically aimed at charity finance staff.

Not all the changes can be attributed purely to the new accounting regime: some are a consequence of the increased statutory funds flowing into parts of the voluntary sector. But overall it is clear that, compared to the pre-1993 situation, there is now a much greater appreciation of the importance of the finance function by charity trustees, managers, and funders.

5.5 Better Overall Financial Management by Staff and Trustees

The requirements of the new regime necessarily require better understanding of the organisation's finances by those who have to make financial decisions within an organisation.

In part, the implementation of new systems and better trained individuals in the finance role has led to better management accounting information provided to senior staff and trustees. In those charities where there has been some degree of involvement, few trustees now would agree expenditure purely by considering the bank balance without taking account of restricted funds.

5.6 Changed Role of Charity Commission

The implementation of the new accounting regime has been accompanied by a radical change in the perceived role of the Charity Commission.

The Commission now communicates much more with charities, takes part in exhibitions and conferences, and produces a wide range of attractively presented publications.[23] At the same time, the Charities Act 1993 has given the Commission much greater powers to take action where trustees are failing to comply with the Act.[24]

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23 See for example: *Charity Commission News* Issue 10 Spring 1999.

24 Charities Act 1993, ss.6 to 43.

In this study, the general impression of the Commission, from those in the finance role seeking involvement with the new regime, was as a helpful body, existing to protect charities, but which nevertheless had to be obeyed. In fact, the perceived authority of the Charity Commission was often felt more strongly than the underlying legislation.

However, for the excepted charities in the study, there was much less knowledge of the role of the Charity Commission, and in a minority of cases, even a sense of "Why bother with the new regime, if no one is going to force us?".

6. Findings

In summary, the following findings emerge from this study.

6.1 The Sector Has Coped Well

In general, little evidence has been seen of major protest towards the new regime. On the limited data available, it seemed that most charities who ignored the regime at first, were making serious attempts to comply by the second or third year.

Some evidence was found of people in finance roles who felt the new regime was excessive, but in most cases where there was a measure of involvement in the new requirements, there was an acceptance that the new regime would lead to more meaningful financial reporting.

The biggest concern was not about the regime as a whole, nor the presentation of the accounts in the new format with SOFA, notes, etc, but on the need for accruals accounting, with the fundamental confusion of fund balances not diminishing immediately by the cost of fixed assets purchased, and the problems of including income which was due but not yet physically received. Although depreciation of fixed assets over an appropriate timescale is crucial for the accounts of a charity to give a true and fair view,[25] many treasurers and finance workers found this concept hard, and even harder to explain to others. However, even this was generally accepted with good grace as being a requirement of the new regime.

Some evidence was discovered of smaller organisations that could not cope with the new rules and lost their treasurers without finding a replacement, with the outcome

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25 Accounting for depreciation - SSAP 12 (last revised October 1992) in *Accounting Standards* (Accounting Standards Board).

being a merger with a larger charity. However, this may well have been desirable in any case.

6.2 The Level of Policing Makes A Difference

Better compliance with the new regime was observed from *registered charities* (under scrutiny of Charity Commission) than by *excepted charities*.

The only substantial group of excepted charities in the study were churches (a range of denominations), and the impression was that they were much less willing to devote resources to the finance role, and to complying with the new regime, than were the registered charities. Although most of the denominational offices have produced guidance on the new accounting requirements, the guidance has not always been received by church treasurers, or they have failed to appreciate its significance. The exception to this was a few large churches, with incomes approaching the £250,000 level, where compliance was generally very good.

Nevertheless, the impact of the Charities Act does appear to have led to an increased awareness by churches that they are charities.

6.3 Accountancy Language Does Not Translate Well to Non-Accountant Treasurers/Bookkeepers

Most of the organisations studied needed a great deal of support in decoding or translating the SORP and Regulations into their own terms. It appears that those responsible for drafting the SORP were almost entirely professional accountants, who saw themselves as writing mainly for their fellow practitioners.

Although the mini-SORPS are some help, many organisations with income just over £100,000 really needed the person in the finance role to have a grasp of the full SORP, and this was daunting for those without a formal accountancy training. To give up on the SORP and leave everything to a professional accountant at year end is not an effective strategy for financial management of the charity, nor does it enable the trustees to make an informed decision when it comes to approving the accounts.

6.4 Quality of Financial Management Appears Improved

However, the net result of the regime appears to be a much higher level of understanding of financial management in the sector. There is greater understanding by trustees and staff of project funds, levels of reserves, proportion of expenditure on management and administration, etc.

6.5 Accountancy Profession Greatly Affected

Although the study did not set out to look at the accountancy profession, it became clear that the relationship between a local charity and its accountants (if any) had a big effect.

One result of the new regime is that firms of accountants are effectively divided into charity specialists and others who decline all charity work. (In addition, there are still significant numbers of professional accountants completely unaware of the whole regime.) In general, however, this means the tradition of accountants acting free of charge or for nominal fees for local charities is ending. The care needed with charity accounts, means that they can no longer be handled as a sideline.

Smaller charities are thus spending substantially more with firms of accountants than in the past, and a number which, in the past, produced accounts entirely under their treasurer and a voluntary informal auditor have turned to professional help as a result of the new regime. On the other hand, the non-professional accountants who are willing to take seriously the duties of independent examiner are finding ample demand for their services.

One consequence has been the growth of Community Accountancy Projects - i.e. voluntary organisations providing an accountancy service to other voluntary organisations, generally on a highly subsidised basis by means of grant aid. The fact that such projects have attracted resources indicates that voluntary sector funders see good accountancy in the sector as worthy of support.

7. Conclusion

The new accounting regime of the Charities Act 1993 represents the most dramatic development in regulation of the entire voluntary sector for over a generation.

This study has focused on smaller charities, defined as those with income in the £10,000 to £250,000 range, which would not in general require a professional audit. It is seen that in all cases the impact of the new rules has demanded substantial changes in financial reporting, and hence in the underlying accounting procedures.

The nature of this study prohibits any quantitative conclusions, and all tendencies reported apply purely to the specific charities studied, which are in no sense a random sample. But by focusing on those organisations where someone in a finance role has been willing to engage with the new requirements, the results are extremely positive. There has been a dramatic change in the understanding of charity finance, not only by treasurers and bookkeepers, but also by trustees as a whole.

There remains a long way to go, and the broader sample of accounts sent in to a small trust show that many charities are still at an early stage in complying, especially those with under £100,000 income, and especially with charities excepted from registration. However, no evidence was found of any major revolt against the new rules, and it seems that with a little more time and more actively promoted education and training, the new accounting regime will soon be seen as normative.