

How are Charities going with the New Accounting Requirements?

And what do we want and expect of a regulator in the sector?

I was prompted to think about these questions by some recent media. The first was hearing on National radio DIA Charities Services, our New Zealand charities regulator, talking about the percentage of charities that have complied with the new accounting reporting requirements so far. The figure quoted was only 59% had complied. This is a low number. But then being reasonably well versed in this sector I was not at all surprised by this seemingly low statistic in this first year of mandatory adoption.

The same article quoted Sue Barker, a well respected Charities Law expert, stating that: *"the non-compliance was "alarming" and charities needed to take the requirement seriously.*

"It's a brave new world out there and charities need to step up."

"It's a governance issue. You have to meet these new requirements. Otherwise you actually are breaching the Charities Act and that could put your charitable registration at risk."

She said many charities, particularly the smaller ones, were overwhelmed and stressed by the changes.

"Charities are struggling to transition to the new regime... apparently when charities are seeking help from accountants, a lot of accountants aren't familiar with the new rules either."

All statements I also agree with. Albeit the statement that some small charities are "overwhelmed" by the changes does raise another issue which is their capacity and resourcing to handle change and a level of accountability suited to their level of operations.

The same Radio NZ article went on to quote Volunteering NZ stating that more needed to be done to support charities to adopt the new standards. With any change, more can always be done. However there has been considerable awareness raising and education efforts from some parties such as DIA Charities Services, the External Reporting Board and some others. I think there is also some responsibility to be laid at the door of the charities to seek to understand the changes. Sadly, just making education available does not mean that all who should will access it or learn from it. It is also not fair to lay the burden of education on just a couple of parties. This is something that many entities in the sector should be involved with. There is no doubt that more ongoing education is required. But I would make the point that this is a two way street.

I was then somewhat disappointed by the article then quoting a Labour minister basically blaming the Government for "dropping the ball" and not having done enough. The comments immediately read like political point scoring. Personally I find very few instances when "the blame game" helps improve matters. But hey we are in an election year so best we all buckle up and get prepared for lots more of these soundbites.

The next day I heard more media from an accounting provider saying the new standards are too hard for small charities and *"how this isn't fair"*.

Then I read Fundraising New Zealand's February 2017 editorial and lead article expressing strong disappointment in the regulator not being strict enough enforcing reporting dates. So what to make of all this?

Some Context

A member of the public without detail knowledge of the changes and the charities sector could quite rightly be thoroughly confused as to what is going on.

The first important piece of context is that this change in legislation requiring registered charities to comply with new accounting standards is the biggest change in financial reporting ever for New Zealand charities. I repeat the word "ever". It is also leading us to a much better place in terms of transparency and accountability for charities in New Zealand. But this will take a few years to actually achieve.

The next piece of context is that we have a wide spread of size and sophistication in our registered charities in New Zealand. This will obviously impact their ability to be aware of and cope with change. And of our 27,849 registered charities (the number on the date I tapped this article as it changes daily) over 95% are either small, or extremely small, in size.

However, the accounting standards that charities have to comply with have been designed with the size spread in mind. In fact, our accounting standard setter went to great pains to consider and accommodate this in designing both the framework for financial reporting as well as the detailed accounting standards that entities within are required to comply with. For this reason we have 4 tiers of accounting standards that need to be complied with and these are primarily designed to ensure an appropriate fit for the size and complexity of the charity.

Broadly I believe they do this well. For the very small charities (below annual operating expenditure of \$125,000) the requirements are akin to being not much more onerous than the ability to record transactions, balance a chequebook, and then present information in some standard categories. Now if that is too hard for some small charities then I seriously question whether they should have the benefits of tax exempt status. An exemption that is in effect funded by the tax paying public. I appreciate that my views will immediately raise the ire of some in the sector. But I stand by it and believe that some entities probably need to stand back and take a reality check. Interestingly, many small charities possibly don't actually need charitable status to do what they do. But if they do need it, or want it; then there has to be some compliance checks to ensure appropriate accountability to the general public. Just saying something is too hard is a cop out in my view.

For larger charities then they will have to comply with one of the 3 other mandatory accounting standard sets. If their annual operating expenditure is over \$2 million then those charities may notice quite a jump in complexity of the accounting standards they are now required by law to comply with. But then in my view the Government got it about right in setting \$2m as the threshold. (And they did so after significant consultation). If any entity is spending more than \$2m a year then I would expect that they need to have appropriate governance and accounting sophistication to adequately account for that. Add to that the fact that the entity is receiving a tax exemption from the rest of New Zealand just emphasises this further.

I think it important to remember that the fundamental point of these new accounting standards is to ensure appropriate comparable accounting is followed in the sector so that the results are understandable. Never before have we been able to compare "apples with apples" with charities financial reporting in New Zealand. Transparency and accountability are critical for the public's ongoing trust and confidence in the sector.

"All things are difficult before they become easy"

The above is a favourite saying. There is no denying that this is a significant change for the sector. With any significant change it will of course take time before the new becomes "business as usual". We are also all human and hence whether we admit it or not, we are all predisposed to react adversely to change.

Add to that the fact that the new relates to accounting standards. Even most accountants will readily acknowledge that not too many people get too motivated and excited about new accounting standards. So perhaps the motivations to get into this change are not as great as in some other areas?

Also this is not just new for charities. Accountants who may assist charities are also coping with significant change with new accounting standards, and not only for charities. To a much lesser extent lawyers also need to appreciate this change in charities financial reporting landscape as this is now required by law in New Zealand.

The expectation of the general public is that these professionals will be on top of any new change. And so they should, especially when they are charging for their services and holding themselves out as being

the experts. But the reality is that accounting and legal professionals also grapple with staying on top of all change. These things take time. My hope is that as "professionals" can get on top of these changes quite quickly for the benefit of the sector as a whole. Their professional bodies also have a role in ensuring sufficient ongoing education and assistance.

So what of our charities regulator?

Then we have our regulator. With the benefit of hindsight I would suggest they coped well with the huge challenge that was registering all charities in New Zealand. A task that involved assessing their charitable purposes and legal documents, and then the IT challenge of creating what is possibly one of the best information registers our Government currently has.

With a population of nearly 28,000 separate entities to regulate, and being part of a Government department there is also the NZ challenge of having limited resourcing.

And now they have a new challenge. Some would characterise this as being the policeman for the sector. It is a role that they must take. However I have been increasingly impressed by their willingness to firstly take an educative approach to the changes. Seeking to help a sector that is characterised by many small and resource poor entities. Trying to make them aware and provide resources to show them how, rather than instantly taking the big stick approach. Sadly that big stick approach is rather prevalent with other regulators.

So while some may say they need to be tougher, I think this is appropriate for a sector that is more than any other almost exclusively made up of entities that exist to do good.

But a regulator they are, and just because an entity is trying to do good won't be an excuse for them not doing their regulatory role. I fully expect that our regulator will have to wield their stick and possibly the sooner that some charities appreciate this reality the better. Some considerable slack is being cut to some charities at present but they should not be lulled into thinking this will last.

The regulator also has their own challenges. Not least; how to cost effectively cover the entire population of NZ charities is a very real and immediate challenge. I'm not sure that the same people that may complain about the regulator not taking a tougher view would be very happy with increased financial charges to cover the costs if the regulator were to be better resourced. An interesting conundrum in finding the right balance.

There is also the challenge of the tightrope to be walked of being seen to appropriately do their job when there is always a simplistic media risk of being called out for beating up some "poor charity". You can just see the sensationalist headlines now. Never mind the fact that the "poor charity" in question may be woefully non-compliant with its legislative financial reporting requirements.

Summary

The sector as a whole is dealing with a very big change. As with any change some are not as aware and up to speed as they should be.

However, it is not an insurmountable change by any means, and especially if all those who can assist do so, rather than just pointing fingers at others.

I also remain convinced it will be worth it. We will end up with much better transparency and accountability in our charities sector.

Like Rachel's advertisement used to say; *"It may not happen overnight, but it will happen!"*



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