

Technical factsheet

Matters of material significance reportable to charity regulators

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This factsheet has been produced in partnership with Steve Collings FMAAT FCCA, director of Leavitt Walmsley Associates Ltd chartered certified accountants, lecturer and author of financial reporting publications. You can find the latest publications at stevecollings.co.uk.

INTRODUCTION

In November 2017, the Charity Commission issued updated guidance in the form of [*Matters of Material Significance reportable to UK charity regulators – A guide for auditors and independent examiners*](#).

The guidance applies to both independent examiners and auditors, who have a duty to report matters of material significance to the relevant charity regulator. There are three UK charity regulators:

- The Charity Commission for Northern Ireland
- The Office of the Scottish Charity Regulator
- The Charity Commission for England and Wales

The updated guidance applies for all audits or independent examination reports being issued, regardless of the accounting period being examined.

There is an important distinction between an independent examiner and an auditor. An independent examiner does not express an opinion on the financial statements as an auditor does. Instead, an independent examiner reviews the accounting records of the charity and compares the accounts presented with those records. Should the independent examiner discover differences between the accounting records and the financial statements, the report is qualified in respect of those differences.

An auditor, on the other hand, expresses an opinion as to whether the financial statements give a true and fair view of the state of the charity's affairs. The assurance provided by the auditor is of a high level but is not absolute due to the inherent limitations of an audit (for example, the use of sampling, reliance on tests of controls and use of estimates).

Auditors and independent examiners are only expected to report matters which they identify during the normal course of their work. This means that there is no additional requirement for auditors or independent examiners to carry out additional work aimed at identifying matters of material significance that are reportable. In all cases, professional judgement must be applied by the auditor or independent examiner when considering whether, or not, to make a report to a charity regulator.

It is important to emphasise that even if the charity trustees have reported a matter to the charity regulator, the auditor or independent examiner will have some additional information or perspective that the regulator needs in order to reach a fully informed assessment of the matter. Hence, the auditor or independent examiner is also expected to make a report to the charity regulator.

Material significance

Charity law refers to the term 'material significance' to determine which matters are to be reported to the charity regulators. In addition, the term 'must' means that the Charity Commission is referring to a specific legal or regulatory requirement, and auditors and independent examiners must report any matters of material significance that they encounter during their appointment.

Auditors and independent examiners will, of course, have come across the term 'material'. However, for the purposes of the Charity Commission, the term has a slightly different meaning to which auditors and independent examiners will be familiar with because it is wider than financial materiality.

Doubts concerning whether a matter is reportable

The general mantra of the Charity Commission is:

'When in doubt, report it.'

This is the default preference for auditors and independent examiners. Therefore, always err on the side of caution and if any doubts exist concerning a matter, simply report it to the Charity Commission to ensure that legislative requirements are discharged appropriately.

REPORTABLE MATTERS

There are nine reportable matters in the Charity Commission's list. The guidance states that a matter becomes reportable as soon as:

- the auditor or independent examiner becomes aware of it; or
- the auditor or independent examiner intends to offer a modified audit opinion, an audit opinion with an emphasis of matter or material uncertainty regarding going concern; or
- a qualified independent examination report identifies one or more concerns about the charity's accounts.

The list issued by the Charity Commission is **not** conclusive. In other words, auditors and independent examiners must apply professional judgement where other matters emerge.

The nine reportable matters of material significance are as follows:

1. Dishonesty and fraud
2. Internal controls and governance
3. Money laundering and criminal activity
4. Support of terrorism
5. Risk to charity's beneficiaries
6. Breaches of law or the charity's trusts
7. Breach of an order or direction made by a charity regulator
8. Modified audit opinion or qualified independent examiner's report
9. Conflicts of interest and related party transactions

Matter 1: dishonesty and fraud

During the course of an audit/independent examination, matters suggesting dishonesty or fraud involving a significant loss of, or of material risk to, charitable funds or assets

Inaccurate or misleading information presented to the auditor or independent examiner is indicative of dishonesty. The guidance states that duplicate invoices that appear to have been altered in their dates or value, or signatures on documents that do not tally with others submitted, are two basic examples that may give rise to concerns by auditors or independent examiners.

The [Fraud Act 2006](#) applies to England, Wales and Northern Ireland, but does not apply in Scotland. In Scotland, criminal fraud is mainly dealt with under common law and a number of statutory offences. The guidance states that in Scotland fraud is committed where someone achieves a practical result by the means of a false pretence.

Example

During the independent examination, an examiner discovers an invoice for £500 paid for by a charity which appears to be for private expenditure by a senior trustee. The senior trustee confirms that the payment should not have been made by the charity but has arisen because of a mix-up with the banking system.

In terms of materiality, the amount in question may be immaterial to the financial statements, but it may be material in nature because it indicates a breakdown of internal controls.

Even if a matter is 'potentially' fraudulent, it should be reported to the relevant charity regulator.

Matter 2: Internal controls and governance

During the course of an audit/independent examination, matters suggesting failure(s) of internal controls, including failure(s) in charity governance, that resulted in, or could give rise to, a significant loss or misappropriation of charitable funds, or which lead to material charitable funds being put at major risk

The charity must have systems and controls in place that aim to safeguard the charity's assets. While it is generally accepted that no internal control system is 100% effective against theft or misappropriation of assets, charities must have systems in place to protect assets. A weak internal control environment, or a lack of internal controls, places charitable funds at risk.

Example

A charity raises funds through a variety of activities, including attending supermarkets and other events using collection tins to raise funds. Cash is given to a member of the charity after the weekend but no record of this cash is maintained, nor are there any checks on the monies collected.

This weakness in the control environment places income completeness at particular risk. As there are no checks or controls in place over the cash collected, the scope for theft is much greater. The independent examiner should report such failings in the control environment.

In the example above, there were weaknesses in the control environment over the completeness of cash collected. Even in situations where there are authorisation procedures in place, if there are no procedures in place to guide staff, this in itself may warrant reporting.

The guidance also states that the scale of assets is important and involves the use of judgement based upon materiality for the auditor or independent examiner. The guidance goes on to state that if the risk of misapplied charitable funds is low, then raising the matter with the charity only may be more appropriate than raising it with the charity regulator.

Matter 3: Money laundering and criminal activity

During the course of an audit/independent examination, knowledge or suspicion that the charity or charitable funds, including the charity's bank account(s), have been used for money laundering, or such funds are the proceeds of serious organised crime, or that the charity is a conduit for criminal activity

The guidance recognises that this matter requires a more specific nature of suspicion arising from documents and information available to the auditor or independent examiner.

Example

A charity has paid out large amounts of round-sum amounts to a third party, which the accounts clerk has posted to 'legal and professional fees' in the accounting system. The independent examiner has not been able to obtain an adequate explanation for the amounts transferred.

This would be a trigger for the independent examiner to suspect money laundering and/or criminal activity is taking place. This would warrant a report to the charity regulator.

The purpose of money laundering is to conceal the proceeds of crime by processing money through an intermediary, or a series of intermediaries, so as to make the money appear to be legitimate. The guidance recognises that money can be in various forms, such as cash, money transfer, cheque, bitcoin and similar cryptocurrencies.

Example

A charity receives a donation of £20,000 from an individual, which is placed into the charity's bank account. On the same day, the sum is paid out to another party in exchange for an asset. The independent examiner has concluded that the donor of the cash is connected to the other party where the charity obtained the asset from.

In this example, it would not be unreasonable to be concerned about the fact that money laundering has been attempted.

There are nine indicators in the guidance (which are not exhaustive) of money laundering as follows:

- refusal by the trustees to explain an unusual transaction
- concerns about the honesty, integrity or identity of trustees
- large or regular donations that require the charity to transfer those funds to a nominated party inside or outside the UK, or to buy goods or services from the donor or a named third party
- loans from an unknown or unverified source, at a zero, low or commercial rate of interest, which the charity is asked to repay by cheque or bank transfer to the donor or a third party
- request by a donor to return funds by cheque or bank transfer because they were 'paid from the wrong account'
- 'loaning' of the charity's bank account to enable deposits or transactions by other third parties or individuals
- making money transfers inside or outside the UK on behalf of a third party in return for a fee
- illogical transactions or routine of funds through a series of bank accounts
- unusual investment or property transactions without a clear investment purpose or rationale.

Matter 4: Support of terrorism

During the course of an audit/independent examination, matters leading to the knowledge or suspicion that the charity, its trustees, employees or assets have been involved in or used to support terrorism or proscribed organisations in the UK or outside the UK, with the exception of matters related to a qualifying offence as defined by Section 3(7) of the Northern Ireland (Sentences) Act 1998

The guidance states that the emphasis here is twofold. Documents and information provided to the auditor and independent examiner would be that which would generate the suspicion; and the suspicion must relate to the support of terrorism or proscribed organisations.

If the concern of the auditor or independent examiner relates to the support of a particular organisation, a check on the [Gov.UK website](#) will confirm whether the organisation is a proscribed organisation.

Where the auditor or independent examiner discover evidence that suggests a trustee or any other person is using the charity's assets to support terrorist activity, this should be immediately reported to the relevant charity regulator as well as to the police.

Matter 5: Risk to charity's beneficiaries

During the course of an audit/independent examination, evidence suggesting that in the way the charity carries out its work relating to the care and welfare of beneficiaries, the charity's beneficiaries have been or were put at significant risk of abuse or mistreatment.

Auditors and independent examiners must notify the relevant charity regulator where charity beneficiaries have been put at significant risk of abuse or mistreatment.

Example

A charity works with young and vulnerable people and its aim is to enable them to have a better quality of life. The charity does not have a safeguarding policy in place, nor does it carry out any Disclosure and Barring Service (DBS) checks on its volunteers.

This issue should be reported to the relevant charity regulator.

The guidance recommends that auditors and independent examiners carrying out work for charities in England and Wales read the Charity Commission for England and Wales's *Safeguarding vulnerable groups and children*.

Matter 6: Breaches of law or the charity's trusts

During the course of an audit/independent examination, matters suggesting single or recurring breach(es) of either a legislative requirement or of the charity's trusts leading to material charitable funds being misapplied

Auditors and independent examiners should familiarise themselves with the charity's purposes and governing document. During the course of their work, they may discover breaches of legal or trust requirements, which should be raised with the charity and/or charity regulator. The auditor or independent examiner will consider the scale, nature and frequency of the breach when dealing with the relevant reporting aspects.

Example

During the year, a charity disposes of property contrary to the terms of the original trust.

This would be reportable to the charity and the charity regulator as it is a breach of the charity's trust.

Matter 7: Breach of an order or direction made by a charity regulator

During the course of an audit/independent examination, evidence suggesting a deliberate or significant breach of an order or direction made by a charity regulator under statutory powers including suspending a charity trustee, prohibiting a particular transaction or activity or granting consent on particular terms involving significant charitable assets or liabilities.

A breach of an order or direction made by a charity regulator is a serious matter and there is an expectation that the charity will bring any such issues to the attention of the auditor or independent examiner.

Ordinarily, when a charity regulator issues an order or direction to a charity, a public announcement is made and hence the auditor or independent examiner should be aware of such through their initial planning of the assignment.

Example

On 30 March 2018, a trustee was suspended pending an investigation into fraudulent expenses claims. Expenses claims continued to be submitted by the suspended trustee and honoured by the charity.

The trustee has been suspended and hence should not be carrying out any further work for the charity. The fact that they continue to be submitting expense claims (which are already the subject of a fraud investigation) is a breach of an order or direction and therefore is reportable.

Matter 8: Modified audit opinion or qualified independent examiner's report

On making a modified audit opinion, emphasis of matter, material uncertainty related to going concern, or issuing of a qualified independent examiner's report identifying matters of concern to which attention is drawn, notification of the nature of the modification/qualification/emphasis of matter or concern with supporting reasons including notification of the action taken, if any, by the trustees subsequent to that audit opinion, emphasis of matter or material uncertainty identified/independent examiner's report

An auditor expresses an opinion on the truth and fairness of the charity's financial statements. An independent examiner does not form an opinion on the financial statements, but instead expresses a conclusion as to whether anything has come to their attention which suggests the financial statements differ from the accounting records. Independent examiners also consider if there are any matters which require disclosure.

An auditor may sometimes judge a qualified opinion to be appropriate in the circumstances (for example, if they disagree with an accounting treatment, disclosure or non-disclosure of an issue as appropriate). While qualified opinions are the 'least' serious, they are expressed only as a last resort where a disagreement cannot be resolved. Disclaimers of opinion are the most serious and would be expressed when the auditor is unable to form

an opinion on the financial statements – for example, because the accounting records have been destroyed.

All modified auditor's opinions are required to be disclosed to the charity regulator, together with a sufficient level of detail to explain the nature of the matter and, where applicable, any action that has been taken by the trustees in respect of the modification.

Where an independent examiner qualifies their examiner's report, they, too, must report details of their qualified examination report to the charity regulator.

It should be noted that where the regulations have not been updated and an auditor or examiner concludes that they need to refer to a new SORP in their auditor's opinion or independent examiner's report because it is different to the one referred to in the regulations, such a reference is **not considered to be a matter of material significance to the charity regulator**.

Matter 9: Conflicts of interest and related party transactions

During the course of an audit/independent examination, evidence suggesting that conflicts of interest have not been managed by the trustees in accordance with guidance issued by the charity regulator and/or related party transactions have not been fully disclosed in all respects required by the applicable statement of recommended practice (SORP)

Conflicts of interest must be managed carefully by charities and each of the UK charity regulators has issued guidance on how to deal with such matters.

Example

Dominic is the brother-in-law of Joanne; both are trustees of the same charity. Dominic is responsible for the setting of trustees' remuneration, including Joanne's.

This is a conflict of interest because Dominic is related to Joanne and hence should not be involved in the setting of her trustee's remuneration. This is clearly a mismanagement of the conflict of interest and would be reportable.

Related party transactions often arise in a charity and, again, care must be taken to ensure that such transactions are managed appropriately. While charities are encouraged to obtain value for money, this should not compromise quality, and at the same time a fair and transparent tendering process should be in place at the charity for ongoing supplies of goods and/or services.

Where transactions with related parties have not been disclosed; or related parties themselves have been discovered by the auditor or independent examiner and transactions have taken place with those previously undiscovered related parties, this is an indicator that the related party relationship has been mismanaged and hence will be reportable.

REPORTING TO THE REGULATORS

Matters of material significance must be reported to the relevant charity regulator by the auditor or independent examiner. Such matters must be reported immediately when they become aware of the matter of material significance and, in England and Wales, such matters are required to be reported in writing (although in Scotland there is no requirement for written reports to be made).

Matters of material significance must be reported to the regulator with whom the charity is registered. Charities that are registered in Northern Ireland have their registration numbers prefixed with 'NIC', whereas charities registered in Scotland have their registration numbers prefixed with 'SC'.

Reporting matters of material significance: England and Wales

At present, reports must be sent by email to:

Whistleblowing@charitycommission.gsi.gov.uk

The email subject line should state 'Matter(s) of material significance reported'. The report must contain the following information:

- the examiner's name and contact address, telephone number and/or email address
- The charity's name and registration number (if applicable)
- a statement that the report is made in accordance with section 156 of the [Charities Act 2011](#).
- under which of the nine headings of reportable matters the report is made
- a description of the matter giving rise to the concern and the information available on the matter reported, together with an estimate of the financial implications
- in the event that the trustees are attempting to deal with the situation, a brief description of the steps being taken by the trustees of which the examiner is aware
- where the report concerns terrorist, money laundering or other criminal activity, confirmation as to whether the the National Crime Agency and/or police have been notified as appropriate
- where the report concerns the abuse of vulnerable beneficiaries, confirmation as to whether the police and/or social services have been informed.

Reporting matters of material significance: Scotland

In Scotland, all reports of matters of material significance are to be sent in writing to the following email address:

Section46@oscr.org.uk

The subject line should state 'Reporting matters of material significance'. The report should identify:

- the party reporting and the charity
- an explanation of the issue of concern
- identification of any supporting evidence regarding the matter under report
- a method of contact to follow up on the information

Reporting matters of material significance: Northern Ireland

In Northern Ireland, all matters of material significance should be sent in writing to the following email address:

concernsaboutcharities@charitycommissionni.org.uk

The subject line should state 'Reporting matters of material significance'. The report should identify:

- the party reporting and the charity
- an explanation of the issue of concern
- identification of any supporting evidence regarding the matter under report
- a method of contact to follow up on the information

Failure to report

Auditors and independent examiners who fail to report matters of material significance to the relevant charity regulator are breaking the law. The charity regulators will take very seriously any discovery that an auditor or independent examiner has failed in their legal obligation to report relevant matters. The charity regulators reserve the right to take any further action.

Auditors and independent examiners who are members of ACCA (including audit firms) may also be subject to disciplinary action by ACCA if they fail to report matters of material significance in contravention of legislation.

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