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New Zealand Accounting Standards Board

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Tena koutou katoa

## **Simple Format Reporting Standards – Post-implementation Review**

I am pleased to provide a submission to the New Zealand Accounting Standards Board (“the NZASB”) on the Post Implementation Review of the Simple Format Reporting Standards. Charities Services’ functions under the Charities Act 2005 include supporting registered charities in meeting their obligations to prepare financial statements that comply with these standards.

Our vision is that our work contributes to a well-governed, transparent, and thriving charitable sector with strong public support. We strongly support any changes to the Simple Format Reporting Standards that make it easier for charities to comply, and that promote public trust and confidence in the charitable sector. Now that the not-for-profit financial reporting standards have been in place for five years, we support this review as an opportunity to assess whether the Simple Format Reporting Standards are functioning well for charities and the public. It also represents timely consideration of the process by which the financial reporting standards are set to ensure they remain relevant and appropriate for registered charities.

The feedback we have provided in the enclosed submission reflects the work that we do as a regulator, the key themes of low compliance with the standards, and the feedback we have received from the sector.

Since the introduction of the reporting standards, we have assessed a sample of Performance Reports and Financial Statements for compliance. Through this work, we have seen a low and declining rate of compliance with Tier 4 charities over the past three years. This has influenced our submission. When we have engaged with these charities, the feedback is often that they find the reporting standards too difficult.

We support the calls from the majority of submitters who commented on this issue in response to the Discussion Document on the modernisation of the Charities Act. More than two thirds of submitters that commented on this issue favoured reducing reporting requirements for smaller Tier 4 charities. Many submitters noted that the reporting requirements did not reflect the realities of governing a small entity, with limited resources and part-time volunteers.

Nga mihi,

**Stephen Reilly**

General Manager – Charities Services Ngā Ratonga Kaupapa Atawhai  
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### ***Our Operational Context***

1. Under the Charities Act 2005, Charities Services has several functions. This includes educating and supporting registered charities to meet their obligations under the Act, monitoring registered charities, responding to complaints about charities, inquiring into possible breaches of the Act or possible serious wrongdoing, promoting research into charities, and developing forms to support this work.
2. In performing our functions, we take a modern, responsive, risk-based approach. We target our resources to the areas that potentially have the biggest impact on promoting public trust and confidence in the charitable sector, and the effective use of charitable resources. Transparent and accurate reporting supports us carry out our functions and supports our vision of a well-governed, transparent, and thriving charitable sector with strong public support.
3. The financial information that is reported in charities' annual financial statements and performance reports is available on the publicly accessible charities register. The full statements/performance reports can be downloaded from the individual charity's listing on the register. Researchers and others interested in the sector can also search for information at the sector-wide level through the advanced search function. For the financial information to be searchable in this way, it must be included in our annual return form. Therefore, we align the information we collect through the annual return forms with the minimum reporting categories required to be reported by the standards.

### ***General Comments***

4. Transparent and accurate reporting supports us to carry out our functions and supports public trust and confidence in the sector. We have heard comments that more reporting, and more detailed reporting, contributes to higher levels of trust and confidence. This is not what our research suggests. Our research shows that the key drivers of public trust and confidence include charities spending their money wisely and effectively, ensuring that the majority of donations get to the end cause, and letting the public know how they raise funds, use their resources, and the positive difference they make. We support annual reporting requirements that enable charities to easily do this.
5. We consider that the ability for small reporting charities (under \$125,000 operating payments) to use a cash-based reporting approach is essential to encouraging reporting in the charitable sector. Through our engagement with the sector, it is apparent that when a level of accounting knowledge is required to understand and use the standards it may discourage reporting as often small charities do not have the capability to engage someone who has this knowledge. Charities Services supports simplicity in the reporting standards for charities that are considered small and believe that the effort involved in reporting should be reflective of the size of the charity.
6. We have noticed a low and declining rate of compliance of charities reporting under Tier 4. Declining compliance rates have occurred despite our continued efforts to educate and inform the sector about the reporting standards through a range of mechanisms, including newsletters, webinars, resources, and support for individual charities (through email, telephone, online clinics and face-to-face meetings).
7. Within the submissions on the discussion document for the Modernisation of the Charities Act, some submissions identified reasons why compliance with the standards may be difficult, stating that small charities; *"Have insufficient resources (time and money) to meet requirements; lack suitably experienced and qualified personnel or volunteers; have high personnel turnover; find the*



*reporting forms unnecessarily complicated; and have insufficient support materials to assist them.”*

8. We consider the use of accrual reporting for Tier 3 charities is appropriate due to the options it provides charities as well as enabling some comparability when shifting to a higher reporting Tier.
9. In our view, the terminology used in the standards, guidance and templates is too complicated for most preparers and users of the Performance Reports. This is more prevalent in Tier 4 reporting charities. We have provided examples below.
10. We understand that often the standards are only read by accountants, reviewers or auditors. While we request that changes are made to simplify the standard where possible, there is the need to focus on simplifying the Guidance and Templates. We find that many preparers of Performance Reports for charities have not read the standards but are more willing to use the guidance we provide them due to the plain language we use.

***What parts of standards, guidance or templates have been working well? Are there any that have been particularly useful?***

11. Compliant Performance Reports contain information that assists us to perform our functions as the regulator of registered charities in New Zealand. We use the Performance Reports as a starting point for assessing complaints or other compliance concerns raised about individual charities. Some of the key ways that the current standards assist this follows:
  - a. the Statement of Cash Flows (Tier 3) and Statement of Receipts and Payments (Tier 4) can help us identify unusual cash flows.
  - b. a lot of concerns and risks that we identify through our complaints and investigations work relate to related party transactions, major costs incurred by the charity, or large liabilities held for undisclosed reasons. The note disclosures in the Performance Reports help us assess these risks, and we therefore we support keeping the disclosures relating to these key points.
12. We support the reporting of non-financial information as it provides charities of all sizes a simple way to report an overview of their charity and the positive difference they make through the services they deliver. This provides readers of all backgrounds the ability to understand the charity, even if they cannot interpret financial statements.
13. We have had feedback from some governance teams of charities who also support the reporting of both financial and non-financial information annually, as they feel that they gain trust and confidence in how they are running the charity.
14. Charities Services’ staff that regularly use the information in the Performance Reports have provided the following feedback about the Tier 3 and Tier 4 standards:
  - a. Significantly more information is available from these statements than special purpose reporting, without the information being overly complex and extensive, such as reports provided under PBE Tier 1 or Tier 2.
  - b. A better understanding of the charity is gained without having to ask for further information. Compliant Performance Reports provide a holistic view of the entity, especially with the Statement of Service Performance.
  - c. The Simple Format Reporting (SFR) accounts are generally quick and easy to review, and it is easier to identify anomalies as we have a base level of expectation from the accounts.



15. The similarities in the structure and requirements between the two standards allows for a simpler transition from Tier 4 to Tier 3 reporting when charities grow and creates a minimum level of transparency in the charitable sector. In addition:
- a. The similarities between the two standards allows us to support charities in both tiers by using the same or similar resources.
  - b. We have also been able to support charities through the transition from Tier 4 to Tier 3 reporting due to the same minimum categories being used, and similar structured templates.
  - c. Having these similarities allows us to provide a consistent and comparable set of data from our public Charities Register database when reporting internally and externally.

***Are there any specific issues that you have encountered in applying the standards?***

16. While we do not apply the standards, we do review Performance Reports and Financial Statements prepared by charities and engage regularly with charities about the use of the standards. Our feedback below is based on this experience.
17. For the year ended 30 June 2018, 72% of Tier 4 charities were making some attempt to use the appropriate reporting standards. This dropped to 65% in 2019 and 59% in 2020, based on the compliance assessments we have done. We have also performed follow up compliance, to assess charities where we have let them know of their compliance issues in the past, to see if there has been some improvement. Almost 50% of Performance Reports that were assessed for Tier 4 charities were still not compliant even after being informed of their errors in the past.
18. There may be a range of reasons why charities aren't using the Tier 4 standards. From our engagement with charities, many find the standards and templates to be too complex for their operations. While not all the requirements in the standards will apply, those involved in preparing the accounts will need to make an assessment about each category and requirement to determine this. These assessments can be difficult, especially given the language used in the standards (which is reflected in the templates and guidance) may not be familiar to non-accountants. This lack of knowledge around terminology often results in many queries, or requests for advice in reporting. For example:
- a. Cash is referenced throughout the Tier 4 standard. While the term "Cash" is used to distinguish this standard from the accrual standard, many charities do not receive or pay cash in their ordinary course of business so can be confused about whether this cash standard applies to them.
  - b. Often, we have questions about the term "Receipts" as people associate this with the physical receipt they get in exchange for a payment they have made for a good or service, and not the receiving of cash or other funds. It's not often a term people necessarily associate with money that comes in to the charity. When combined with the title "Operating" often this confuses the term further. A suggestion would be to replace this with a term that is more direct and plain language, such as "Money Received" or "Incoming funds". The distinction between operating receipts and capital receipts adds further complexity to the term receipts.
  - c. We have had charities ask what is meant by a "Capital Receipt" or "Capital Payment" as the word capital is confusing to them. To provide clarification, we often must provide further examples of the type of transactions that would be described as capital. We understand the need to clarify payments between Operating and Capital, as this distinguishes between Financial Performance Payments and those that would generally



be reported in a Statement of Financial Position. We suggest using simplified versions of the terminology from the Statement of Cash Flows in Tier 3 or relating the cash transactions to the Statement of Resources and Commitments. Examples could be:

- i. Money received from a resource ("e.g. sale of building")
  - ii. Money paid for a resource ("e.g. purchase of building")
  - iii. Money received from a commitment ("e.g. loan drawdown")
  - iv. Money paid to a commitment ("e.g. loan repayment")
- d. We have heard concerns with splitting payments receipts between "Member and Non-Member", as many small charities are only concerned with whether what they are receiving in total is covering their costs. Separating money that comes from members and non-members creates additional complexity for those preparing the reports. We question whether this is a worthwhile distinction, particularly where members also pay for goods or services delivered by the charity (perhaps at a reduced member rate). This can distort the overall picture of how much money the charity receives in return for providing goods and services, as this would be captured in the "other receipts from members" category.
- e. The term "Reserves" is often mistaken for a 'reserving of cash' and recorded incorrectly in the Accumulated Funds. We find when engaging with charities, there is the lack of understanding that the recording of reserves in the accounting practice is more restrictive than the plain language 'reserves of cash'. A suggestion would be to simplify the term to "resources specifically held". Within the submissions for the Modernisation of the Charities Act, some submissions covered the obligations on reporting accumulated funds and supporting greater transparency on the accumulated of funds, such as further disclosure of their approach to the accumulation of funds.
- f. The use of the terms "Outputs" and "Outcomes" in the Statement of Service Performance causes confusion, and the quality of information reported under these headings is extremely varied. As the regulator, we find this information very useful to know however due to the confusion, often this is not reported correctly, accurately or completely. Often charities will interpret this as a need to separately record their expenditure. We suggest that simplifying this to be more direct in the content it is requesting, such as "Goods or Services Delivered".
- g. The term "Performance" is used throughout the two standards, but this covers multiple facets, which results in this having multiple meanings. Such as the report being called a Performance Report, while having separate statement of Statement of Service Performance and Statement of Financial Performance

***Are there any specific issues that you have encountered in applying the guidance, or templates?***

19. In our view, the templates that are currently available have several limitations.
- a. Charities have told us that once they have understood the templates, they find it useful to roll forward. However, it often takes on average two points of contact with the charity to explain the template and then provide further comments/ guidance where errors have been made, to reach the point of compliant accounts.



- b. The feedback we have received notes that the format can be confusing on what is required to be filled out, or the number of pages required results in missing information or entirely missed pages. This makes it difficult for preparers to keep the Performance Reports internally consistent.
  - c. For small charities where only a small number of fields apply, the templates are often submitted in full but with lots of blank sections. The resulting report is lengthy and may be difficult for a reader to easily digest and understand holistically.
  - d. Charities Services occasionally come across very small charities who have little to no financial activity, and the reporting requirements seem burdensome and have no benefit to them. A simplified version of the template that allows charities who have no financial transactions to report their non-financial information and a simplified financial information page would go some way to address this issue.
  - e. The templates reflect the complexity in the standard, and this feedback indicates the template may need to be simplified, or the required information made more obvious to the user.
20. We also see the need for further examples in the guidance, and diversity within those examples to reflect the needs of our diverse charitable sector. We have, for example, received feedback about the limitations of the standards for charities that have a Kaupapa Māori focus.
  - a. Preparers of Performance Reports have asked for the ability to report using bilingual headings. We suggest providing Māori headings for all key Statements.
  - b. The terminology of “significant” can be confused with “taonga”. The standards should address how to record items that don’t belong to the charity in a legal sense, but the charity has a custodian or kaitiaki relationship and looks after and cares for it for current and future generations. We suggest that the reporting standards provide examples and terminology options that encompass these different types of assets.
  - c. Another example is that “koha” can have a range of cultural meanings and recording different types of koha can be difficult under the current standards. In the Tier 3 and Tier 4 standard Koha is combined with donations, however the context in the way koha is given and what is given can vary widely in different situations. We suggest providing worked examples in the standard of different koha and how this can be recorded.
  - d. A more technical issue that has been raised with us is about applying the related party disclosure requirements in Iwi or Iwi related charities. Many involved in these charities whakapapa or connect to each other on several levels.
21. A translation issue has also been identified in interpreting terminology into other Pacific languages such as Samoan or Tongan. Providing simpler terminology in English would aid in the translation to more languages used by charities.
22. Charities Services work with a range of researchers who use the register to collate and analyse information at the sector-wide level. From our discussions with these researchers, we are aware that there are limitations which have resulted from the minimum categories of information that must be reported under the standards. Concerns have been expressed about the inability to find out how much money has been collectively donated to charities by members of the public (as these are now combined with other fundraising efforts), granted by the government, bequeathed by individuals, and how much is spent on salary and wage costs.
23. As the minimum categories currently stand, many charities find that their transactions do not fit well within the categories. This results in many transactions being included in the ‘Other’ section of the Statement of Receipts and Payments and/or the Statement of Financial Performance.



*Do you have any other comments you would like to raise about the standards, guidance, or templates?*

24. We appreciate the opportunity for Charities Services to be working with the XRB on engagement with the charitable sector, and the opportunity to address some of the issues that the charities in New Zealand face when it comes to reporting.