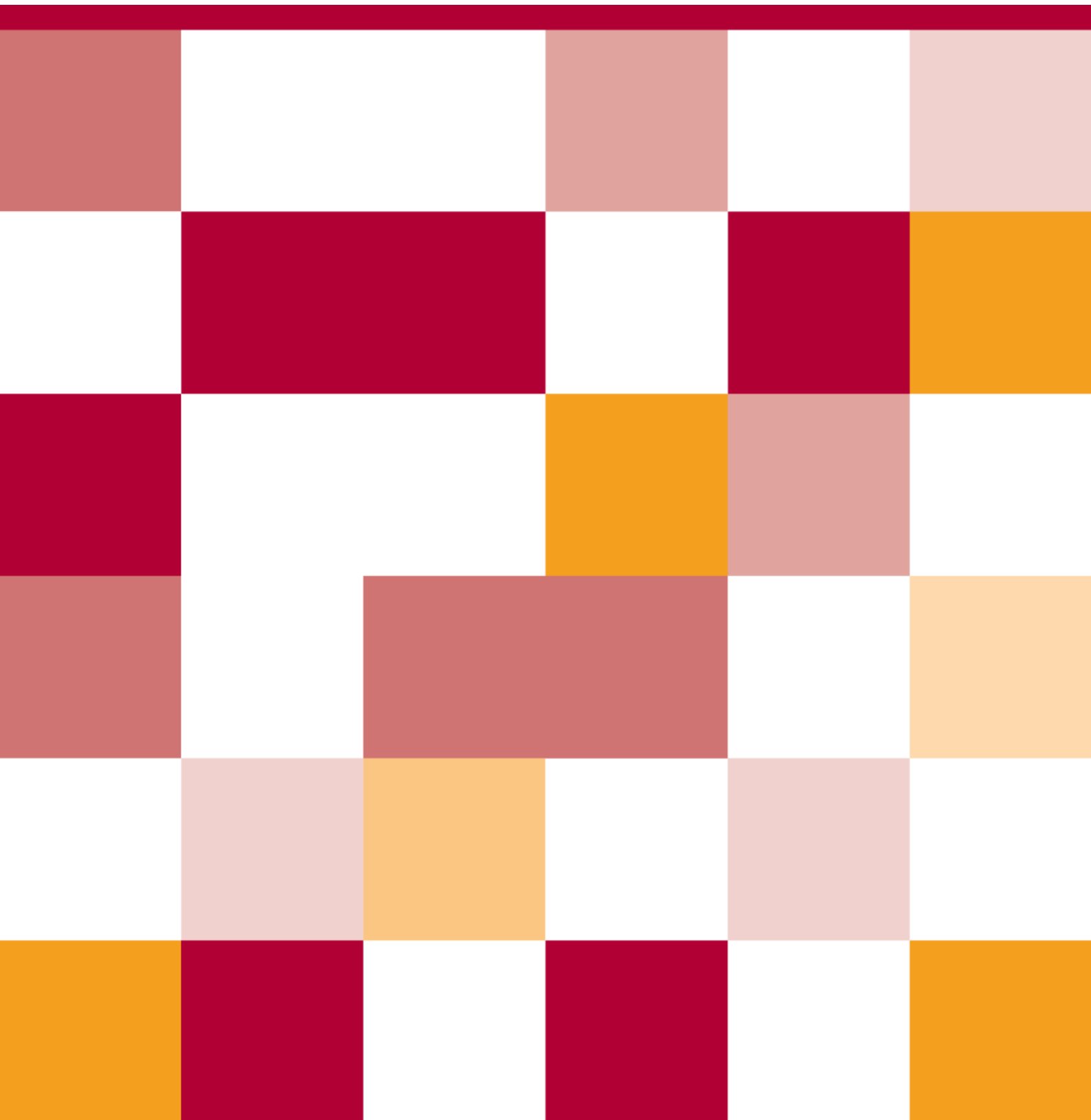




**Draft Charities (Accounts and Reports)
Regulations 2007: Consultation for Investment
Fund Charities
Draft Regulatory Impact Assessment**



Draft Charities (Accounts and Reports) Regulations 2007

PARTIAL REGULATORY IMPACT ASSESSMENT

for
Investment Fund Charities in England and Wales

June 2007

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1. Proposals

- 1.1 Regulations relating to the accounting and reporting requirements of Investment Fund Charities (including Common investment Funds (“CIFs”) and Common Deposit Funds (“CDFs”) which form part of the proposed Charities (Accounts and Reports) Regulations 2007 to be made under the Charities Act 1993 (“the 1993 Act”).
- 1.2 A separate consultation document and RIA have been prepared in relation to changes proposed in the Regulations affecting the accounting requirements of general charities (as opposed to investment fund charities). Copies of these two documents are available electronically at www.cabinetoffice.gov.uk/thirdsector.

2. Purpose and intended effect of measures

2.1 The Objective

- 2.1.1 The proposed requirements will amend the relevant parts of the Charities (Accounts and Reports) Regulations 2005 (“the 2005 Regulations”) to maintain the consistency of reporting requirements with the Investment Management Association's Statement of Recommended Accounting Practice for the Financial Statements of Authorised Funds (“the IMA SORP”) which was revised in December 2005.
- 2.1.2 In addition, the Charities Act 2006 (“the 2006 Act”) made a number of changes to Part 6 of the 1993 Act including inserting a new section 49A and Schedule 5A which creates a new provision for the preparation and scrutiny of group accounts. In a number of key areas matters are to be addressed in Regulations. The objective of the Regulations, so far as concerns group accounts, is to ensure a workable framework for the preparation of group accounts and the related annual report together with relevant provision for the scrutiny of such accounts. The Draft 2007 Regulations seek to achieve this objective as economically as possible in terms of the regulatory requirements introduced.

2.2 **Devolution**

- 2.2.1 The Regulations considered in assessment would only affect CIFs and CDFs (“investment fund charities”) in England and Wales.

3. The background

- 3.1.1 The 2005 Regulations included accounting provisions relating to CIFs which were consistent with the IMA SORP published in November 2003 and also set out information to be provided in the annual reports of such charities. The IMA SORP 2003 has been superseded and the Regulations require certain amendments to ensure consistency with the revised IMA SORP published in December 2005.
- 3.1.2 The IMA SORP sets out recommended accounting practice for authorised unit trusts and open-ended investment companies in the UK. The 2005 Regulations drew heavily on the recommendations contained in the IMA SORP 2003 recognising that the information needs of charities participating in investment fund charities were very similar to those of general investors in commercial collective investment schemes such as unit trusts and open-ended investment companies.
- 3.1.3 Whilst the accounting changes introduced by the IMA SORP 2005 are not great, it is important that the accounting regime for CIFs reflects changes in terminology, presentation and the disclosure of gains and losses from derivative transactions introduced by the new SORP.
- 3.1.4 The new Regulations relating to the preparation and scrutiny of group accounts are unlikely to affect any investment fund charities currently registered as none operate through a group structure with subsidiary undertakings. Nevertheless, there is no legal prohibition on them acquiring or forming subsidiary undertakings and therefore it is considered prudent for the proposed Regulations to set a framework for the preparation and scrutiny of such accounts and the related annual report. Prior to the introduction of these group accounts provisions into the 1993 Act, the preparation of group accounts was a practice recommended by the Charities SORP and applied to those charities where the combined income of the group exceeded the statutory charity audit threshold for individual accounts. The preparation of group accounts is now

general sector practice. However, until the 1993 Act was amended by the 2006 Act, no legal status was given to group accounts by charity law.

4. Risk assessment

- 4.1.1 If the 2005 Regulations are not amended for the changes introduced by the IMA SORP 2005 then the accounting framework provided by the Regulations would be inconsistent with recommended practice adopted by commercial collective investment schemes and in particular investment funds charities would continue to apply the valuation bases and disclosures provided by a superseded SORP. The policy objective of ensuring that the standard of financial reporting by investment fund charities is consistent with that of commercial collective investment schemes would be risked.
- 4.1.2 In the event of an investment fund charity undertaking investment or other activities through a subsidiary undertaking, a workable framework would not exist in law for the preparation and scrutiny of group accounts or for an annual report relating to such accounts. This would pose a risk to the relevance of investor information available and impede the implementation of the requirements introduced by the 2006 Act relating to parent charities and group accounts.

5. Options

5.1 Option 1: Rely on existing 2005 regulations

- 5.1.1 This option would result in the accounting methods and principles for valuing fund assets and liabilities requiring compliance with a superseded SORP. In addition the identification of gains and losses from derivative transactions would not be required. CIFs currently follow the recommendations of the IMA SORP and a failure to amend the 2005 Regulations would create a tension between legal requirements and accepted accounting practice.
- 5.1.2 Whilst the changes to the 2006 Act would still require the preparation and

scrutiny of group accounts where required, without Regulations a workable framework for their preparation and scrutiny would not exist in law.

5.2 **Option 2: Implement the proposed Regulations**

5.2.1 The changes to the 2005 Regulations will allow investment fund charities to prepare reports and accounts using methods and principles consistent with the IMA SORP 2005. This will ensure that the Regulations continue to reflect appropriate accounting standards and relevant annual reporting to meet the information needs of charity investors.

5.2.2 Whilst no investment fund charities current utilise subsidiary undertakings to undertake activities, a framework is put in place to deal with this eventuality and thereby ensuring the information needs of investing charities will continue to be met.

6. Charity sub-sectors affected

6.1.1 The proposed changes affect 42 CIFs. Currently there are two CDFs, however, these are unaffected by the changes unless they, at some future date, undertake activities through subsidiary undertakings which is considered unlikely.

6.1.2 Charities operating “pooling” arrangements for their investments would not be affected by the Draft 2007 Regulations applying to investment fund charities. A “pool charity” can be distinguished from other CIFs in that all charities eligible to participate must, at the time when any particular contribution is made to the pool, be administered by exactly the same body of trustees which the pooling scheme appoints as the charity trustees(s) of the “pool charity”. A small number of schemes, although made as pooling schemes, allow a somewhat wider participation by charity connected in some way and are required to follow the Regulations applying to investment fund charities to help ensure investor protection. The Draft 2007 Regulations do not change this position. .

7. Equality impact assessment

- 7.1 The proposed changes will not bring disproportionate benefits or costs to any particular groups. A review by the Charity Commission of the investment fund charities affected by the Draft 2007 Regulations did not identify any as being connected with BME organisations.

8. Sustainable development

- 8.1 Consideration has been given to whether these proposals will have costs or provide benefits to environmental protection, social values and progress, or the economy's long term growth and development. The proposals would not lead to any disproportionate adverse impact.

9. Cost calculations

9.1 Compliance Costs

- 9.1.1 The changes proposed are considered cost neutral.

9.2 Option 1: Retain the 2005 Regulations

- 9.2.1 The changes proposed are considered cost neutral.
- 9.2.2 Retaining the existing 2005 Regulation would give rise to no direct regulatory costs. However, in so far as CIFs are likely, in any case, to comply with the IMA SORP 2005, similar costs would be incurred in practice irrespective of the proposals and in the absence of regulation tensions could arise as the application of current recommended practice which would not be consistent with the regulatory requirements in place.
- 9.2.3 Whilst retaining the 2005 Regulations would give rise to no additional regulatory costs, in the event of a group structure being adopted by an investment fund charity, similar costs would arise where consolidation is required by the 2006

Act but implementation of these measures would be problematic in the absence of regulation.

9.3 **Option 2: Implement the proposed Regulations**

- 9.3.1 The key change proposed to the accounting requirements is for the methods and principles contained within the IMA SORP 2005 to be applied in valuing fund assets and liabilities. These methods and principles are broadly consistent with the superseded IMA SORP 2005 and therefore no significant compliance costs are anticipated as a result of this change.
- 9.3.2 The minor presentational changes to form and content of investment fund accounts, in respect of derivative securities, are unlikely to result in any significant increase in compliance costs as such disclosure rely on information that is likely to be readily available and already required by the IMA SORP 2005. Achieving compliance with the Draft 2007 Regulations is therefore unlikely to create any additional regulatory costs due to their consistency with the IMA SORP which fund managers are likely to have significant experience in applying.
- 9.3.3 The changes are unlikely to necessitate any training costs either for the auditors of such investment funds or those charged with their administration. No significant changes to record keeping or accounting procedures are anticipated.
- 9.3.4 At present no investment fund charity undertakes activities through subsidiary undertakings. The immediate regulatory cost of the Draft 2007 Regulations in relation to requirements placed on parent investment fund charities is therefore nil. Even, if at some future date, an investment fund charity adopted a group structure, the regulatory costs are still regarded as neutral. The Draft 2007 Regulations simply give a legal basis to generally accepted accounting practice. The Draft 2007 Regulations in providing a framework for the preparation and scrutiny of such accounts will assist preparers and auditors and also ensure relevant stakeholder information is provided through an expanded annual report.

9.4 **Other Costs**

9.4.1 There are no other costs anticipated.

9.4.2 A typical investment fund charity will see no significant increase in the cost of preparation or scrutiny of its accounts or in the preparation of its annual reports.

10. The Small Firms' Impact Test

10.1 As the proposals only impact on investment fund charities, they fall outside the scope of the Small Business Service.

11. Competition Assessment

11.1 The proposals impact equally on investment fund charities and are consistent with the accounting and reporting arrangements of the IMA SORP 2005 which applies to commercial collective investment schemes and therefore no competition concerns arise.

12. Enforcement and sanctions

12.1 The proposed regulations will, if necessary, be enforced under existing provisions of the Charities Act 1993 and will result in no additional enforcement costs.

13. Monitoring and review

13.1 The legislation will be monitored on an ongoing basis by the Charity Commission who receive annual reports and accounts from all investment fund charities with income of over £10,000 per annum. A full review of the Regulations will take place in 5 years or earlier if there are found to be causes for concern.

14. Consultation

14.1 Within government

14.1.1 The Cabinet Office has consulted with the Charity Commission on this matter. The Department for Trade and Industry, HM Treasury and The Financial Services Authority will all be included in the consultation exercise now being undertaken.

14.2 Public consultation

14.2.1 The Regulations will be exposed to public consultation for a period of at least 12 weeks from publication. The consultation will be addressed to those involved in the administration or audit of investment fund charities, key sector umbrella groups, professional accountancy bodies and a selection of charities that invest with these charities.

14.2.2 The consultation is due to close on 14 September 2007.

15. Summary and recommendation

15.1 Our clear preference is for option 2. This option best meets the objective of providing an accounting and reporting framework relevant to charities' reporting needs and creating appropriate accountability to a charity's stakeholders for the resources they control. The proposed Regulations are necessary to maintain a regulatory framework that is in line with current accounting and reporting practice.

16. Declaration

I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.

Signed.....

Date.....

- 16.1 This declaration is completed only as part of the full regulatory impact assessment, once consultation is completed, and the assessment updated.

17. Contact point

- 17.1 Enquiries regarding the contents of this partial Regulatory Impact Assessment should be made to:

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