

## Financial Information Kit

The purpose of this kit is to provide basic information on keeping financial records to facilitate compliance by registered charities with the requirements of the Canada Revenue Agency.

Contents of this kit:

- FAQs: Financial Reporting and Registered Charities
  
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  - Setting Up a Chart of Accounts for a Small Organization
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  - Getting Ready for an External Audit – What Can You Prepare?
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- Additional Resources
  - We're Calling to Set Up a Time to do an Audit (*LawNow* Article Series)

This kit is available for free download at [www.charitycentral.ca/docs/financialkit-en.pdf](http://www.charitycentral.ca/docs/financialkit-en.pdf)

## Financial Reporting and Registered Charities

### Choosing a Professional Accountant

#### PA1

##### Once we're a registered charity, do we need a professional accountant?

No. It is not necessary to have a professional accountant.

Hiring a professional accountant is not related to your registered charity status with the Canada Revenue Agency (CRA). The CRA recommends that charities file audited financial statements if their gross income from all sources is more than \$250,000. You should evaluate the needs of your organization and the resources that you have available from within the organization. Someone in the organization needs to understand what is required in being a registered charity, including completion of the Registered Charity Information Return (T3010), and where to find the necessary information and resources.

The charity's treasurer should sign any financial statements that have not been professionally prepared.

#### PA2

##### What does a professional accountant do that our accounting clerk or volunteer bookkeeper can't?

While **bookkeeping** records your organization's transactions, **accounting** involves the whole process of recording, classifying, presenting, and interpreting the financial transactions. There is a big difference between accounting and bookkeeping.

Recording and preserving the transactions is **bookkeeping**. This function ensures that appropriate records and documentation exist for all financial transactions.

Presenting the financial transactions through financial statements and other required reports is an **accounting** function. These statements and reports show the results of operations and the financial condition of the organization.

The interpretation part of the accounting process involves analysis, explanation, and use of the information presented in financial reports. A professional accountant is trained and experienced in interpreting and reporting financial information from a perspective that an accounting clerk might not have.

You may be lucky enough to have a volunteer who is a professional accountant, but who may not have the time or the expertise in not-for-profit reporting to fill the role completely. If this is the case, you still need to examine your need for a professional accountant with the needed expertise.

## PA3

### What types of accountants are considered professional accountants in Canada?

In Canada, the provinces govern the accounting profession and the different services that each type of accountant may provide. All provinces recognize the three main accounting designations in Canada:

- CGA (Certified General Accountant)
- CA (Chartered Accountant)
- CMA (Certified Management Accountant).

## PA4

### What type of professional accountant do we need for what?

As mentioned in FAQ PA3, the provinces determine what services each designation can provide to the public. Services are usually categorized as

- **assurance services** that include audit and review services, and
- **non-assurance services**, which include compilations or notice-to-reader engagements (see FAQ FMR7) and tax filings that include Registered Charity Information Returns (T3010).

Once your organization decides what services you need, refer to the provincial website of each accounting body to determine which designation can best meet your needs. Most of these websites will also contain a referral list of accountants in your area that provide the services you're looking for.

The national websites for the accounting bodies are

- Certified General Accountants Association:  
[www.cga-canada.org](http://www.cga-canada.org)
- Institute of Chartered Accountants:  
[www.cica.ca](http://www.cica.ca)
- Society of Certified Management Accountants:  
[www.cma-canada.org](http://www.cma-canada.org)

Each of these websites has links to the provincial sites.

T3010 in English is available on CRA website at [www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html)

T3010 in French is available on CRA website at [www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-fra.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-fra.html)

## PA5

### What should we look for in choosing a professional accountant, whether volunteer or paid?

Your professional accountant should have experience working with charities and understand the compliance requirements of being a registered charity. Whether volunteer or paid for their services, your accountant should have the time to provide all the services you need.

Ideally, a prospective professional accountant should provide references from other charities for which he or she is providing services.

## PA6

### We're a new not-for-profit organization that recently received registered charity status. Should we get a professional accountant to set up our accounting records?

Accounting systems can be set up by anyone with experience in accounting or bookkeeping. A professional accountant can provide valuable advice if your charity has complex operations or a specific or unusual circumstance requiring professional expertise. In particular, anyone setting up your accounting records should know what's required to complete the T3010 (Registered Charity Information Return).

T3010 in English is available on CRA website at [www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html)

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## PA7

### How should the accounting records be set up so we can easily complete the Registered Charity Information Return (T3010)?

Your charity needs to consider all the users of your financial information and their requirements. One of the most important users of a charity's financial information is the Canada Revenue Agency (CRA). You need to understand the financial information required for the T3010:

- The balance sheet information for the T3010 is basically the same as in any set of financial statements.

The revenue and expense accounts on the T3010 are designed to provide the CRA with information they need to monitor charities. The CRA's categories may not provide information in the same way as you need for management purposes or to meet other user needs.

Your charity should design your accounting system so that you can easily transfer information to the T3010 return. Keep track of where the information originates in the accounting system so that you can report consistently to the CRA from one year to the next. This is particularly important when the person who is completing the return changes from year to year, as may be the case when a volunteer or an external accounting firm does the work.

For more information, see the Tipsheet #4 – Financial and Other Information Needed to Complete the Registered Charity Information Return (T3010)

T3010 in English is available on CRA website at [www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rtrn/flngb-eng.html)

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## Financial Management and Reporting

### FMR1

#### What's the difference between financial statements from our accounting system and "audited financial statements"?

Having "audited financial statements" usually means that a person independent of the organization's management has gathered evidence to support the financial information that management provided. This independent person or body adds a report to the information expressing whether the information has been fairly presented. (When accountants say the information is "fairly presented," they mean that it is complete and has been shared openly and honestly.)

You need to address the fact that audited financial statements are not always done by professional accountant. Those involved in not for profit organizations generally think of audited

financial statements as those audited by professional accountants. The bylaws of some organizations indicate that two members of the organization can also provide the audit services and report to the board.

When external professional accountants perform an audit and issue their audit opinion, they follow generally accepted auditing standards and report using generally accepted accounting principles. These are broad and specific rules adopted by the accounting profession as guidelines for measuring, recording, and reporting the financial transactions and activities of an organization. This provides consistency in reporting between organizations and within one organization from year to year.

In contrast, statements from a charity's accounting system do not provide the same assurance to financial statement users and very often do not match accounting standards.

## FMR2

### **What is meant by “good financial management”? Who is ultimately responsible for the financial management of a charity?**

Good financial management means your charity cares appropriately for the money entrusted to your organization in order to meet your community’s needs and your requirements as a registered charity. Good financial management includes planning ahead for your financial needs, establishing and monitoring financial policies, and establishing and monitoring internal controls appropriate for your organization.

The whole board is responsible for the financial management of the organization, not just the treasurer or the finance committee. The board should establish financial policies and monitor these policies to ensure they reflect the current desires or practices of the board and make changes as required. The board must also keep an eye on financial practices to ensure that the policies are being carried out as intended.

## FMR3

### **Are audited financial statements always done by professional accountants?**

No. The term “audited financial statement” does not always refer to financial statements that are audited by a professional accountant. The bylaws of some registered charities indicate that two members of the organization can also provide the audit services and report to the board and members.

## FMR4

### **Are registered charities required to submit audited financial statements to the Canada Revenue Agency with their annual T3010?**

No. Registered charities are required to provide a copy of their financial statements with their T3010, but the statements do not have to be audited. The CRA recommends that charities file audited financial statements if their gross income from all sources is more than \$250,000.

## FMR5

### **If the CRA doesn’t need audited financial statements, why do we have to have them?**

Audited financial statements assure the users of your financial information that the information is fairly presented. You may need the audit financial statements to meet legal requirements in your constitution and bylaws or to satisfy government regulations and the needs of the users. Users include funders, members, board, management, creditors, bankers, employees, donors, beneficiaries of services, and the community at large.

## FMR6

### **Is it a good practice to have our financial statements audited by a professional accountant?**

The requirement for an audit may be found in a charity’s bylaws or other legal documents or may be required by a funder or other financial statement user. An audit can often identify financial errors in information, but whether it is a good practice, necessary, or unnecessary is different for different types and sizes of organizations.

## FMR7

### What is a “letter of engagement” with a professional accountant?

An engagement letter is a formal contract with a professional accountant for services. This letter outlines the terms of the arrangement with the accountant and the type of report that will be provided. Read the engagement letter carefully; once signed, it becomes a legal contract. If there are any questions regarding the content of the letter, discuss these items with the accountant before signing.

## FMR8

### What are the different types of services that a professional accountant can provide?

You may engage an accountant for three types of financial statement services available to charities:

- compilations (or notice-to-reader engagements)
- review engagements
- audit engagements

A **compilation engagement** is appropriate for many small private organizations. The goal of a compilation is to prepare financial statements or other necessary financial information for your charity, based on data and information that you provide. Because you have provided all the information, the accountant does not give any assurance about the reliability or accuracy of the financial information being prepared.

Financial statements prepared under a compilation engagement are considered “compiled statements”.

A **review engagement** is seen as a limited-assurance engagement. What this means is that an independent accountant is expected to determine whether the financial information presented by

the charity is plausible or believable, but does not actually express an opinion on the fairness or validity of the financial statements. Unlike a compilation, which provides no assurance to the financial statement users, a review engagement is designed to offer a moderate assurance that the information is reliable. For some registered charities, a review engagement may be appropriate to satisfy the needs of the financial statement users. You need to determine whether your financial statement users will be satisfied with a review engagement or whether your bylaws permit a review engagement instead of an audit.

Financial statements prepared under a review engagement are considered “reviewed statements”.

An **audit engagement** is designed to provide the highest level of assurance for financial statement users. Audit procedures are designed specifically to allow the auditor to develop and express an independent opinion on the overall fairness of the financial statements. The auditor is also examining the financial statements to verify that they have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP).

Financial statements prepared under an audit engagement are the only ones that can be considered “audited financial statements”. The more assurance that the accountant provides to financial statement users, the more time the accountant will require on the engagement and therefore, the higher the fee. So you see, a compilation engagement that does not provide any assurance has fees that are much less than a review, which provides some assurance. An audit provides the most assurance so the fees are highest for an audit. An audit also provides a letter to management with recommendations for improvements to internal controls and other areas of interest to management.



## FMR9

### How is cost determined in having our financial statements audited?

In general, audit fees are based on a combination of the time needed to complete an audit and the level of staff required for that specific engagement. Audit fees can be charged based on a set fee quote agreed to before work begins or the fees may be based on the number of hours required to complete the work. Though time and expertise are the most significant factors determining audit fees, organizational characteristics, such as complexity and size, will have an impact.

## FMR10

### What work does our charity need to do in an audit of our financial statements?

In order for the audit to progress smoothly and efficiently, you must play an active role in the audit process.

- The auditor will provide your organization with a list of documents and working papers needed for the audit to proceed. You'll need to prepare these and provide them to the auditor on time.

Both your management and accounting staff should be aware of the audit and be available during the fieldwork portion of the audit in order to answer questions. If key personnel will not be available, you should let the auditor know as soon as possible, so that the audit plan can accommodate this.

- Management is responsible for informing the auditor of your expected timeline for the completion of the audit, particularly of any strict deadlines and the reasons for them.
- You are also responsible for continuing to maintain accounting records throughout the audit period, and making these documents available to the auditor upon request.

- Management should carefully read all letters from the auditor and ask immediately about any items that are unclear or incorrect.
- When you receive the audited financial statement drafts, management and other key parties need to take the time to review the statements and contact the auditor with any questions, comments, or concerns. Management must also review all audit adjusting entries and approve them before the final financial statements are issued. If your organization and the auditor are able to work together effectively and have an open line of communication, the audit can proceed as planned and all deadlines can be met.
- The board of directors has legal and fiduciary duties that include oversight of financial reporting. On a day-to-day basis, the board relies on staff or volunteers to provide them with the financial information needed to make effective decisions. Although others provide the board with the financial information, ultimately the board of directors is responsible for reporting to members and funders. For this reason, the board is asked to read, understand, and approve the final draft of the financial statements before the auditor releases the audit report.
- Depending on your organization, you may or may not have a finance or audit committee. If there is a committee, it usually plays an oversight role and is responsible for monitoring both management and the external auditor during the audit process. The committee is responsible for checking the selection of and compliance with accounting policies and practices within the organization. If an audit committee has been formed, it is primarily responsible for monitoring the appointment of an external auditor. The committee is also responsible for reviewing the organization's internal control systems to make sure that they are operating effectively. Without either of these committees, the board of directors usually assumes these responsibilities.

## FMR11

### What work does the auditor do?

- The auditor gathers information from the client to assess whether the financial information provided is correct. Once the risk is assessed, the auditor plans how to gather evidence to support the financial statements.
- The auditor ensures that the financial statements follow generally accepted accounting principles and adds a report that provides assurance to the financial statement users.
- The auditor will provide a report to management recommending any needed improvements in internal controls and other financial recording and reporting areas.

## FMR12

### Does an audit help the charity in completing their annual Registered Charity Information Return?

No. Not necessarily. An audit is carried out to meet requirements as outlined in **FAQ FMR4**. As audited financial statements are required by users other than the Canada Revenue Agency, the information is often presented differently from what is required on the Registered Charity Information Return. An audit may identify errors in a charity's accounting records that may have an impact on the accuracy of information provided on the return.

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## Choosing a Professional Accountant

Your decision as a charity to engage a professional accountant should include a process that:

- recognizes your charity's legal and contractual reporting needs
- identifies accounting and other reporting needs of the users of your financial information
- acknowledges the human resources (roles) that are available within the organization and identifies the gaps to meet the needs
- understands the financial resources required for the various professional accounting services available
- provides for selection of an auditor

### Legal and contractual reporting

A charity should review its legal and contractual reporting requirements at least once a year to ensure its requirements are being met. Legislation sets out whether or not an audit is required on an annual basis.

#### Reporting to Government

One of your charity's most important legal reporting requirements is the completion of the Registered Charity Information Return (T3010). Other legal requirements are identified in your incorporating documents and depend on the legislation under which you obtained incorporation, such as Alberta's *Societies Act*. This may differ from province to province. Other provincial legislation may also affect your reporting requirements, for example, certain fundraising activities (for example, the *Fundraising Act*).

#### Funders and Others

Contractual agreements with funders may specify reporting requirements. These funders may be government, foundations, and donors or may

relate to gaming and other activities. Your charity may have other contractual agreements with banks, landlords and in lease arrangements. Some of these contractual agreements include a requirement for the charity to provide audited financial information.

### Needs of your charity's financial information users

In addition to legislative bodies, funders, banks and landlords, and other users have an interest in your financial information. Some of these users are internal to the charity; others are external.

#### Internal Users

Internal users may include the board and management of the organization, your staff, and suppliers of goods and services. The board and management need information to help them in good financial decision-making and management of the charity's resources. Staff members are also interested in good financial management as it relates to their role in the organization and to their financial well being in working for the organization.

Suppliers of goods and services may ask for financial information for assurance that they will be paid.

### External Users

Other interested users may be external to the charity. These may include potential donors, sponsors and the community at large. Your financial information will help them to evaluate whether they can trust the charity to provide the services that they are looking to fund.

## Human resources – Financial roles and functions within your organization

Your treasurer, finance committee, accountant, or bookkeeper may be called upon to play a role in providing financial information. It is important to evaluate the roles of your human resources to discover what accounting and bookkeeping needs are or are not being met effectively. Accounting systems can be set up by anyone with experience in accounting or bookkeeping.

**Bookkeeping** is the recording and preservation of transactions. Bookkeeping includes the recording of the transactions to ensure that appropriate records and documentation exist for all financial transactions.

**Accounting** is a process that records, classifies, presents and interprets the financial transactions of an organization. Your organization's financial transactions are presented through financial statements and other required reports. These statements and reports show the results of operations and the financial condition of the organization. The interpretation part of the accounting process involves the analysis, explanation and use of the information as presented in the financial reports.

**TIP:** If you hire an outside accountant, you should designate someone in your organization as the key contact for the accountant. That individual should have a good understanding of the requirements of being a registered charity, including the completion of the Registered Charity Information Return, and must know where to find the required information and resources.

## Financial Resources Required

Accounting and financial reporting services are usually considered administrative expenses and most charities have limited budgets for these services. Your charity should allocate resources in this area in order to provide effective financial management.

### Professional accounting services available

- **Consulting Services**  
A professional accountant can provide valuable advice if the charity has complex operations or a particular or unusual circumstance that would require professional expertise. A professional accountant is trained and experienced in interpreting and reporting financial information from a more experienced perspective, compared to a volunteer or an accounting clerk.

Professional accountants providing this type of consulting service may do so through a professional accounting firm or as part of their consulting practice. You must be clear about the services you want provided. With a clear understanding of what the professional accountant can provide, the related costs, whether on an hourly or a project basis, need to be detailed in a contract for service.

- Assurance Services

In Canada, your charity requires accountants when you need your financial statements professional audited or reviewed. These assurance services provide an opinion from a professional accountant to financial statement users about the fairness of the information presented.

Assurance services provided by professional accountants include audit and review services; non-assurance services include compilations or notice-to-reader engagements, consultations, and tax filings, including Registered Charity Information Returns.

Refer to FMR8 in the FAQs section of this package for descriptions of the types of assurance services.

If your charity needs assurance services, visit the provincial website of any one of the three accounting bodies to determine which designation can best meet your needs in your province. Most of these websites also contain a referral list of accountants in your area that provide the services you are looking for.

In Canada, the provinces govern the accounting profession. All provinces recognize the three main accounting designations in Canada: CGA (Certified General Accountant), CA (Chartered Accountant), and CMA (Certified Management Accountant).

For more information, contact:

- Certified General Accountants Association of Canada: [www.cga-canada.org](http://www.cga-canada.org)
- Institute of Chartered Accountants of Canada: [www.cica.ca](http://www.cica.ca)
- Society of Certified Management Accountants of Canada: [www.cma-canada.org](http://www.cma-canada.org)

You can link to your provincial websites from each of these national sites.

## Process for selecting an auditor or accountant

Your board should determine who will guide the process for selecting the auditor or accountant. The process may be guided by the whole board, an executive committee, finance committee or audit committee. The “who” may depend on the expertise or time available to participate.

### Example: Selecting an external auditor

The Finance Committee:

1. Recommends the appointment of external auditors to the Board and develop a list of potential auditors.
2. Develops a request for audit proposals that includes, but need not be limited to:
  - An outline of the work to be done
  - Partner and staff to be involved
  - Time frames for performing the workExpected remuneration
  - Travel costs
  - Miscellaneous expenditures, if known
  - Possible independence issuesThe proposals should also address relevant experience with similar organizations and provide client references.
3. Evaluates all proposals, makes a short list, and completes reference checks on the short list.
4. Determines if they wish to interview potential auditors as part of their recommendation process.
5. Makes their recommendation to the board.

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## Setting Up a Chart of Accounts for a Small Organization

### What is a chart of accounts?

A chart of accounts is an index of how we categorize financial information. A chart of accounts is usually divided into groupings of financial information. The groupings are those that appear on a set of financial statements.

A chart of accounts can be developed by account name only or by account name plus a numbering system that identifies each account. If you are planning to use an accounting software program, you will find that a general chart of accounts can be selected and then customized for your organization.

### What do we need to consider in developing our chart of accounts?

Each organization will have a different set of accounts based on the financial activities of their organization. You will need to look at your own organization and understand what accounts you will need to provide information to your financial statement users.

It is usually easier to start with a basic chart of accounts and add other accounts as you need them. The more accounts you set up, the more complicated your accounting becomes and, sometimes, the more errors that might occur.

You should consider the items on a Balance Sheet (also called a Statement of Financial Position) first. A Balance Sheet is organized in two sections: (1) assets, and (2) liabilities and equity.

Your next consideration is how many revenue accounts you need to provide the information expected by the users of your financial statements. Then, consider what expense accounts would provide the best information. The revenue and expense accounts are organized into an income statement (also called a Statement of Operations or Statement of Profit and Loss).

You will need to decide if you are going to record your accounting transactions on a **cash** or **accrual** basis. A **cash** basis means that you will record your revenue as you receive it and your expenses when you pay the bills. An **accrual** basis means that you will record your revenue in the time period it was earned and your expenses in the time period to which they relate. Under an accrual basis you will record accounts receivable when someone owes you money and accounts payable when you owe someone else.

**Although an organization can decide to use cash or accrual basis, it is preferable to use the accrual basis of accounting as this is the requirement for presentation under generally accepted accounting principles.**

## Sample chart of accounts – Balance Sheet

**Assets** – assets are what your charity owns

**Bank** – if you have more than one bank account, your chart of accounts will have a separate “account” for each bank account

**Petty cash** – only set up if you are using a petty cash system to pay cash for small items or to reimburse someone for small purchases

**Accounts receivable** – only set up if you are intending to record amounts owed to you by others

**GST/HST receivable** – this is a special receivable that records the portion of the GST you have paid for services and supplies and will receive from the federal government when you apply for the rebate (usually at your charity’s year end)

**Property and equipment** – if you decide to report your property and equipment as an asset instead of an expense, you would use this account

**Liabilities** – what a charity owes to others

**Accounts payable** – these are amounts you owe to others for goods and services provided to you, but that you have not paid for yet

**Equity** – resources you have available for future years. Businesses call their equity retained earnings. Most accounting programs use this term. For charities, their equity is usually called net assets or fund balances.

## Sample chart of accounts – Income Statement

The accounts used in your income statement are some of those outlined on the T3010B – Schedule 6. It is important for you to consider all users of your financial statements when a chart of accounts is developed. Remember, too, that the CRA is a user and there should be an ease of transfer of information from your accounting system to your T3010 form.

### Revenue

Government grants	Received donations
Non-receipted donations	Gaming revenue
Fundraising revenue	Interest income

### Expenses

Advertising and promotion	Travel and vehicle expenses
Interest and bank charges	Licenses, memberships and dues
Office supplies and expenses	Occupancy costs
Professional and consulting fees	Education and training
Compensation expenditures	Gifts-in-kind used in charitable programs

For a more detailed example, visit

<http://charitytax.imaginecanada.ca/browse-list-topics/record-keeping/keeping-books-records/keeping-financial-r/general-ledger> (English)

<http://infoimpots.imaginecanada.ca/browse-list-topics/tenue-des-registres/tenir-les-registres-/conservation-de/grand-livre-g%C3%A9n%C3%A9ral>  
(French)

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## Setting Up Financial Books and Records

Your financial books and records should be able to show others a financial picture of your organization at a particular point in time or over a period of time.

### Fiscal Year

Books and records are organized to provide financial reports on an annual basis. The start and end point of your year is something that the organization decides when it starts its activities and is usually stated in your incorporation documents. Your financial year is called your **fiscal period**.

Organizations may decide to set their fiscal period based on their activities. For example, a performing arts organization may decide that they would like their fiscal year to start on July 1 and end on June 30 because their performances usually start in September and end in June. Organizations that receive a lot of federal or provincial government funding may choose a March 31 year end so that they are reporting their funding to match the government year-end. You can change your fiscal year-end, although as a registered charity, you must receive approval from the Canada Revenue Agency before you make that change.

### Double Entry Bookkeeping

Once you have determined your fiscal period, you need to decide how you will record your organization's financial transactions. You may choose to use "off the shelf" accounting software

(such as QuickBooks or Simply Accounting), or you may choose to set up your records using an Excel spreadsheet. It is important to select a method that will require you to have two entries for each transaction. This is called double-entry bookkeeping.

Double-entry bookkeeping requires a debit and a credit for each transaction. All major accounting software programs will automatically require two entries for each transaction. If you set up a spreadsheet to record your transactions, you must have two entries for each transaction.

The main types of accounts are usually a debit or a credit:

- |               |        |
|---------------|--------|
| • Assets      | Debit  |
| • Liabilities | Credit |
| • Equity      | Credit |
| • Revenue     | Credit |
| • Expenses    | Debit  |

Here is an example of a simple transaction:

An organization buys some office supplies. They record the expense as a debit and the second entry credits the bank account. In this case, the credit is to an asset account as we are "using up" some of that asset to buy the supplies.

Once you have decided how you are going to record transactions, you are ready to set up a chart of accounts. Please refer to the tipsheet **Setting Up a Chart of Accounts** for more information on this topic. Once you have a chart of accounts, you can begin to enter your transactions.



## Monitoring Financial Performance

Another important part of an accounting system is monitoring your financial progress. Are you going to develop a budget? Will you use that budget as you look at your revenues and expenses to see how you are doing financially compared to how you thought you would do?

Budgets are very useful tools to make sure that your revenue is what you planned on, so that you have the money to pay your bills. If you have funding from a government or a foundation, a

budget for your project will help ensure that you spend the money according to funder expectations and that you don't run out of money before the project is complete.

Keep monitoring on a regular basis at board or finance committee meetings!

The following will help you to develop a budget for your organization. The organization in this sample has a March year-end and begins budget planning in November.

Date	Action	Person or Group Responsible
November	Review plan for next year: April to March	Board Senior staff
December	Re-evaluate existing programs and services Set budget guidelines e.g., What cost of living increases will be provided to staff in the next year? Ask for input from committees	Board, committees Treasurer, senior staff
January	Input received from committees Collect necessary information on changes	Committees Board, treasurer
February	Determine costs of next year plans and realistic revenue amounts Prepare revenues and expenses budget Adjust to produce balanced budget	Board, treasurer Senior staff
March	Board approves budget	Board

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## Financial and Other Information Needed to Complete the Registered Charity Information Return (T3010)

In order to fulfill its monitoring responsibilities of charities, the Canada Revenue Agency (CRA) requires certain information about a charity on an annual basis. This information is a combination of financial information, program activities, fundraising activities, donations to qualified donees, and information about board and staff. The form used by the CRA to gather this information is the T3010 (Registered Charity Information Return). The CRA uses the T3010 and other information to determine whether the charity's resources have been used for charitable purposes and whether it has complied with other requirements under the *Income Tax Act*.

All the information requested on the T3010 must be contained in the charity's books and records and should be used to complete the T3010 on an annual basis. The T3010 is due no later than six months after the charity's fiscal year-end.

### What books and records should you keep and how do you transfer this information to the T3010?

The complete T3010 return package includes:

- Basic Information Sheet – TF725
- Completed T3010 return, including Schedules 1-6, as required
- Financial statements for year of return
- Completed Directors/Trustees worksheet – T1235E
- Completed “Qualified Donee” worksheets – T1236E, if applicable

#### Basic Information Sheet (TF725)

This sheet is included in your T3010 package that is mailed to you by the CRA. The mailing usually occurs around the 15<sup>th</sup> of the month immediately following your fiscal year-end. The information sheet asks for updates to organizational details such as address, phone numbers, and contact information. Any changes or additions to program areas are also required. The person signing the T3010 for the charity must be an authorized signing officer as they are certifying that the information on the Basic Information Sheet is correct, complete, and up-to-date.

## T3010 Return

### Section A

General information on changes in the charity – your basic information sheet will provide some of this information

### Section B

Information on board members – some is made public and some is kept confidential. To complete Section B you must attach Form T1235, Directors/ Trustees and Like Officials Worksheet.

- A board member list should be updated with **all** the required information as new board members are added to the board.
- If board member is not willing to provide their birth date, they can send it directly to the Charities Directorate with the following information:
  - Why they are sending it;
  - Their full name and address;
  - Their date of birth;
  - The name of the registered charity;
  - The charity's business number;
  - The fiscal period for which the return is being filed.

### Section C

- This section asks for information on your programs and other general information. The section is extensive and covers several of the charity's operations.
- Update your program information for both your **ongoing programs and any new programs undertaken in the fiscal year** for which you are reporting, **not including fundraising activities**. The information should provide a picture to the CRA and to the community at large about what you have done in the past year to carry out your charitable purposes.
- This section also asks about **funds transferred to qualified donees**. A qualified donee is

another Canadian registered charity and certain other organizations as outlined on the CRA website. You will need to complete the T1236 form regarding Qualified Donees Worksheet/ Amounts Provided to Other Organizations if you have made any such transfers in the year. If you have not transferred any funds to qualified donees, you do not need to complete the form. This information is not available from your accounting system so you should track it on a separate spreadsheet as the gifts are made. It can then be easily transferred to the T1236 when completing your return.

- Section C also asks about **activities** you may have been involved in **outside Canada**. If you have carried out any activities in any fashion outside Canada, you are required to complete Schedule 2 Activities Outside Canada. Schedule 2 asks for total expenditures you have incurred in these activities. This information can be drawn from your financial information. Other information will need to be tracked on spreadsheets for each international activity.
- The next question relates to **political activities** carried out in the past year and funds spent on them. If you have set up an expense account for this in your accounting system, you can easily transfer the information to the form. If not, you will have to review your expense category and identify expenses relating to political activities in order to determine the amount to record in this section.
- A lot of Section C focuses on information related to **fundraising activities**. If you hire an external fundraiser, you will have to complete the first question on Schedule 4 Confidential Data, which asks for confidential information about the fundraiser. An external fundraiser might be an individual or a company. Financial information is also requested in Section C. This financial information may have to be tracked outside of your accounting system for entry into this section.

- Section C asks questions about **compensation of directors, trustees, and/or employees**. If your charity has employees, you need to complete Schedule 3 Compensation. Some of this information is available from your financial information, but the number of employees and their individual salaries will not be.

#### Section D

- You need to complete Section D if you have
  - revenues of \$100,000 or less in the year
  - assets of \$25,000 or less not used in charitable programs
  - not been approved by the CRA to accumulate funds, and
  - not spent or transferred enduring property during the year.
- Section D financial information is in a simplified form and should be available from your accounting system.

#### Section E

This is the certification section and **must** be signed by a director, trustee, or like official of the charity who is authorized to sign on behalf of the charity.

#### Section F

This section asks for the registered office (the address of the charity's books and records), and the information on who has completed the return.

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### Additional schedules

#### Schedule 1

To be completed by foundations only

#### Schedule 2

For activities outside Canada. See Section C notes above.

#### Schedule 3

Compensation details. See Section C notes above.

#### Schedule 4

Confidential data on fundraisers and donors not resident in Canada.

#### Schedule 5

Information on non-cash gifts (that is, gifts-in-kind)

#### Schedule 6

This schedule is for organizations that are not eligible to complete Section D, as noted above. Unless you qualify to complete Section D, you must complete Schedule 6, which includes more detailed financial information.

More information is available on the Canada Revenue Agency website at

[www.cra-arc.gc.ca/chrts-gvng/chrts/chcklsts/t3010b-eng.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/chcklsts/t3010b-eng.html)

(English)

[www.cra-arc.gc.ca/chrts-gvng/chrts/chcklsts/t3010b-fra.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/chcklsts/t3010b-fra.html)

(French)

## Getting Ready for an External Audit – What Can You Prepare?

A financial audit by a professional auditor provides an opinion on whether your financial statements present your financial information fairly and in accordance with generally accepted accounting principles. This requires that your information be as ready for that audit as possible. You should make all the journal entries that you can; provide as complete a package as you can.

The information identified below assists the audit staff in completing your audit more efficiently. The audit staff may, however, request additional information or documents during the course of the audit. Some of the audit testing is completed on a randomly selected sample basis, which therefore cannot be identified in advance. Note also that not all the documents listed below may apply to your organization.

Item	Description
<b>General items</b>	
General ledger	<p>A copy of the accounting data file in electronic format to be used to select transaction samples for audit purposes</p> <ul style="list-style-type: none"> <li>• It should be complete, after any adjusting entries you intend to make;</li> <li>• Do not change the general ledger information without telling your auditor what additional entries you have made;</li> <li>• The accounting data file is also used to track accounting transactions through the system.</li> </ul>
Financial statements	Copies of the most recent interim and/or year-end financial statements available, if these are provided to your board or other oversight body
Minutes	Minutes of membership, finance and/or audit committee, and board meetings
Budget and/or business plan	<p>Copy of the current year budget, with actual to budget year-to-date comparisons if available</p> <p>The organization's business or strategic plan if one has been prepared or updated in the year</p>

Item	Description
Other general items	<p>Membership list</p> <p>Bylaws</p> <p>Board of directors listing</p> <p>Officers</p> <p>Audit and/or finance committee members</p> <p>Bank signing officers</p>
Financial policies	<p>Board approved financial policies</p> <p>Details (names and positions held) of authorization levels for:</p> <ul style="list-style-type: none"> <li>• purchases;</li> <li>• hiring;</li> <li>• contracting;</li> <li>• receipting.</li> </ul>
Insurance	Copy of insurance policy summary or certificate of coverage (auditors will review the policy, but do not require a copy of the entire document)
Commitments, contingencies and claims	<p>Copies of leases for property or equipment</p> <p>A description of any claims and potential claims against the organization, for example lawsuits or guarantees provided for others</p>
<b>Assets</b>	
Bank accounts	<p>Bank reconciliation reports for all bank accounts</p> <p>Copies of bank statements for last month of year under audit and for first month after year-end</p>
Investments	<p>Copy of broker statement or</p> <p>Other documentation supporting investments held at year-end, for example GIC certificates</p> <p>Market values for any investments that are publicly traded</p>
Accounts receivable	<p>Aged list of accounts receivable, agreeing to year-end trial balance</p> <p>List of any accounts from whom collection is in doubt</p>
Inventory	<p>List of inventory on hand, priced at cost</p> <p>Memo describing:</p> <ul style="list-style-type: none"> <li>• inventory count procedures;</li> <li>• how cost was determined;</li> <li>• process followed to ensure all items in inventory have been included in accounts payable and vice versa.</li> </ul>
Property, plant and equipment	<p>Schedule showing beginning balance, additions, disposals, amortization calculations, and ending net book value</p> <p>Calculations related to any significant purchases or disposals during the year</p>

Item	Description
<b>Liabilities</b>	
Bank debt	Loan agreement for any new debt incurred in the year Summary of interest paid in the year, agreeing to trial balance
Accounts payable	List of accounts payable, agreeing to trial balance Explanation of any items that have been due for more than 90 days
Accrued expenses	Details of expenses (including how amounts were calculated) for any accruals recorded Details of any expenses incurred which have not been recorded (for example, utilities, loan interest)
Payroll liabilities	Copy of payroll remittance form for the last month of the year List and amount of any vacation time owed to employees who have not taken their full vacation List of any bonuses to be paid after year end Copy of most recent T4 summary
GST and other taxes	Copy of GST remittance or rebate form for the last reporting period of the year Copy of property tax invoice and assessment if real estate is owned Copy of the most recently filed T3010 return (unless prepared by auditor)
Long-term debt	Copy of agreement for any new debt assumed in the year Schedule of payments in the year showing interest and principal payments Copy of any long-term leases entered into in the year, including property and/or equipment
Deferred contributions	Schedule showing beginning of the year balance(s), new contributions, and amounts spent for each source of funding with specific purposes Contracts, funding agreements or letters indicating funding purpose from each funder Descriptions of how amounts spent in current year were calculated



Item	Description
<b>Revenue</b>	
Contributions and grants	Copies of all funding agreements Gaming commission reports to support casino or other gaming revenues Copy of gaming approval for eligible expenses to be paid through gaming bank account
Donations	List of charitable donation receipts issued in the year List and amount (value) of any donations “in kind” with supporting documentation for donation
Fees or other service revenue	Brief description or list of other source(s) of revenue
Sales revenue	Brief description of nature of items sold, and what process is followed to ensure that sales revenue and related costs are recorded in the correct period
<b>Expenses</b>	
Payroll	Copy of most recent month’s payroll reports from payroll service (if external service is used) List of all employees showing: <ul style="list-style-type: none"> <li>• name;</li> <li>• salaried or hourly;</li> <li>• pay rate;</li> <li>• start and/or termination date if not employed for full year;</li> <li>• position or department;</li> <li>• program (if salaries allocated to program).</li> </ul>
Other expenses	Invoices to support all expenses paid for the year Invoices paid in month following year-end

## Other Tips on Working with your Auditor – Common Issues During an Audit

This tip sheet identifies some areas where problems may arise in the audit of a charity's financial statement. These problems may result in time delays or higher audit fees.

Common Problem	Solution
<b>Adjusting entries</b>	
1. Prior year adjusting entries are not recorded.	1. Request adjusting entries from auditor if not provided; make adjusting entries at prior fiscal year-end date or on first day of new year; after posting entries, reconcile to prior year audited closing trial balance.  If you have questions or difficulties understanding the adjusting entries, ask your auditor for help. Send auditor reconciled trial balance.
2. Significant adjusting entries added after auditor is provided with accounting data.	2. Send auditor accounting data after recording all journal entries or let auditor know as soon as you identify any required adjusting entries so that they can be adjusted by auditor as well.
3. Adjusting entries to allocate expenses do not have proper supporting documentation.	3. Develop and retain documentation to support calculations and adjustments made for allocation of expenses.
<b>Audit Documentation</b>	
1. Even when provided with a description of the requirements for the audit, the client only provides part of the list.	1. When provided with the list of requirements by your auditor, do not ignore any of the items. If you do not understand what is requested, ask your auditor.
2. The audit documents are not well organized.	2. Use an audit binder to organize documents for the auditor. You can add to your audit binder throughout the year any items you know the auditor will need. The binder can be electronic or hard copy.

Common Problem	Solution
<b>Availability of key client personnel</b>	
<p>1. Key personnel are on vacation or away at crucial times during the audit. Key personnel may include executive director, financial coordinator or accounting manager, bookkeeper, member of audit committee or board.</p>	<p>1. Planning in advance for the audit is important. The audit timelines should be set out with the auditor ahead of time. Staff should be available to answer questions throughout the audit. The auditor and the charity's staff are collectively responsible for meeting timelines and carrying out an efficient audit.</p>
<b>Backdating of accounting transactions in accounting system</b>	
<p>1. Invoices related to prior year but received after year-end are entered in system as if received before year-end.</p>	<p>1. These invoices should be entered as accounts payable so that the expense is recognized in the prior year, but the accounts payable is properly stated.</p>
<p>2. Invoices continue to be added to the prior year as received after audit is completed.</p>	<p>2. The invoices should be entered into the current year and the auditor made aware if the amount is significant.</p>
<p>3. Revenue is entered into prior year after year-end is complete.</p>	<p>3. The revenue should be entered into the current year and the auditor made aware if the amount is significant.</p>
<p>4. Cheques are written in month following year-end and dated using year-end date.</p>	<p>4. Use date written on cheque and set up accounts payable to record.</p>
<b>Changes made to equity accounts during year</b>	
<p>1. For various reasons, transactions that do not have any rationale are recorded to net assets or fund balances accounts during the year.</p>	<p>1. Do not make adjusting entries to these accounts unless you have discussed with your auditor in advance.</p>
<b>Using cash and accrual basis of accounting within same year</b>	
<p>1. Many charities do not completely understand cash versus accrual accounting. This usually happens when cash flow is confused with accrual accounting.</p>	<p>1. Organizations can use one or the other, although it is preferable to use accrual accounting if you are being audited as this is the requirement for presentation under generally accepted accounting principles. If cash accounting is being used, ensure that the adjusting entries are made at year-end to address all accrual accounting requirements.</p>

Common Problem	Solution
<b>Significant changes to the chart of accounts</b>	
<p>1. Different situations will cause an organization to change its chart of accounts. These situations might include addition of new programs or activities, more logical numbering system, change in treasurers or accountants, change in accounting software.</p> <p>A change to the chart of accounts in one year creates problems in providing comparative numbers for the prior year's audited financial statements.</p>	<p>1. If making significant changes to the chart of accounts, it is important to provide the auditor with the information on how the new chart of accounts compares to the prior year. You should provide this information to the auditor in a spreadsheet when you change the chart of accounts so the auditor's records can be updated as well.</p> <p>Make sure that new account numbers do not duplicate numbers used on other accounts in the prior chart of accounts.</p>
<b>Confusing filing systems for documents</b>	
<p>1. Documents are not filed in a logical way making them very hard to locate in a timely fashion.</p>	<p>1. Develop a logical and consistent filing system for documentation.</p>
<p>2. Documents are not in one central location.</p>	<p>2. If documents are with different people such as the officers of the organization, develop a binder indicating where everything is held and who is responsible for keeping it up-to-date.</p>
<b>Multiple sets of accounting records</b>	
<p>1. Different sets of accounting records are set up for each program in the same organization.</p>	<p>1. Use the functions that are present in accounting packages that allow for accounting on an individual program basis as well as an overall organizational basis.</p>
<p>2. The records contain "due to" and "due from" accounts that do not reconcile.</p>	<p>2. If continuing to use this system, ensure that the "due to"/"due from" accounts reconcile on a regular basis, such as monthly.</p>

Please note: Not all issues related to internal controls and the understanding of accounting principles for the not-for-profit sector have been covered in this tip sheet.

# We're Calling to Set Up a Time to do an Audit

W. Laird Hunter, Q.C.

The Charities Directorate of the Canada Revenue Agency (CRA) has many responsibilities toward charities. One that creates a chilly wind for most charities is the telephone call saying that CRA wants to do an audit. While concern might be reflexive, it isn't often warranted. The *Income Tax Act* (Act) requires every registered charity (and every registered Canadian amateur athletic association) to keep certain records and books of account at a Canadian address. These books need to contain and present information so CRA can satisfy itself that the charity is operating within the requirements of the Act. One specific requirement is for a set of duplicate receipts, with related detail allowing CRA to verify donations, which might result in a possible deduction or tax credit.

This column reviews some of the issues relating to audits of charities by CRA. The vast majority of audits result in a confirmation of compliance from CRA or direction from it to the charity about some minor record transgression. Knowing what an audit involves and why it might happen can be helpful both in lessening anxiety and being sure that if it does happen, the proper records are available.

## What is an Audit?

An audit is an examination of records or financial accounts to check their accuracy. The word comes from the Latin *auditus*, which has its origins in the concept of hearing, because originally accounts were read aloud. Looking at a charity's financial and other records allows CRA to make an assessment about whether the charity is following its charitable purposes in accordance with the requirements of the Act.

## Why Do Audits Occur?

CRA indicates that there are a number of possible reasons a charity is identified for audit:

- by random selection;
- to review specific legal obligations under the Act;
- to follow-up on possible non-compliance or complaints;
- to confirm assets have been distributed after revocation; and
- to help CRA understand the purposes and activities of an organization that is applying for registered status.

This last point is little known. An applicant for charitable registration can be audited before that status is granted to help the Directorate determine if it meets the Act's requirements as a charity. The CRA is required to ensure that all charities comply with the Act. In the audit context, CRA carries out its mandate by reviewing information provided to it by the charity in its application and otherwise, including making notes of phone conversations and looking at the annual filing of the T3010.

## What is Required from the Charity When an Audit is Done?

CRA expects that the charity will within reason

- make available all requested information and office space;
- provide time to conduct the review without any unreasonable delays; and,
- during the course of the audit, treat the CRA representative in a professional and courteous manner at all times.

Once the audit has been reviewed, there are four ways the audit may conclude:

- Confirmation of Compliance;
- Education;
- Undertaking; or
- Administrative Fairness Letter (AFL).

Except for confirmation of compliance, it is the degree and material nature of the non-compliance that will be the key factor determining which letter CRA sends.

## Confirmation of Compliance Letters

Where CRA reviews a charity's operations and doesn't find a failure to comply with the requirements of the Act – the most common situation – CRA sends a letter confirming compliance with the Act, explaining that the audit is complete and that the charity is in full compliance.

### Education Letters

CRA sends an education letter when the auditor finds minor non-compliance with the Act and CRA determines that it can inform and educate the charity on ways to correct the non-compliance. Usually no response is required from the charity.

### Undertaking Letters

In a number of situations, undertaking letters are issued where the non-compliance, while serious, does not warrant revocation of the charity's registration as a charity. When this happens, CRA asks the charity to provide a written undertaking, specifying how it will put measures in place to correct the situation identified.

Where a request for an undertaking is not answered, CRA might decide to send an Administrative Fairness Letter to stress how serious a situation the charity faces. When undertaking results in a response that CRA accepts, it will expect the charity to comply. If later there is a further visit or partial audit and it is determined the charity is not complying with the Act, CRA may then, without more notice, issue an Administrative Fairness Letter.

### Administrative Fairness Letter (AFL)

An AFL is sent to a charity when CRA determines that the failure to comply with the Act is serious and that CRA is justified in revoking the charity's registered status. This situation is set out in a proposal letter and representations from the charity are invited. The charity is given time to present its case before a Notice of Intent to Revoke Registration is issued. All representations by the charity are answered by CRA. It usually requires a response from the charity within 30 days of the AFL being sent, though no reasonable request for an extension will be denied.

**An applicant for charitable registration can be audited before that status is granted to help the Directorate determine if it meets the Act's requirements as a charity.**



## **A Notice of Intent to Revoke**

Registration confirms CRA's decision to revoke registration. Where the status of a charitable organization is revoked, the charity still has 30 days from the mailing of the notice to file a Notice of Appeal with the Federal Court of Appeal.

## **Future Audits**

While it is possible that a charity may be audited in the future, where there is compliance and the charity otherwise remains in compliance with the Act, CRA as a matter of practice will not select the charity for audit again for a period of not less than three years from date of the last audit.

*This column is based on information provided by the Charities Directorate. For more information see CRA's webpage on Audits and Sanctions at [www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/dts-eng.html](http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/dts-eng.html)*

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