

## **CHAPTER 7**

### **THE INLAND REVENUE INSPECTION**

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#### **7.1 Introduction**

7.1.1 The Inland Revenue has a duty to ensure that any tax repaid to charities is properly due and correctly calculated. IR (Charities) undertakes inspections to check that any claims charities make for repayment of tax are for the correct amounts and are backed by clear audit trails.

7.1.2 The objectives for charity audits are set out in Appendix F below. In carrying out the audit the Inland Revenue auditor will

- review charities' accounting records, systems and procedures,
- check the calculation of claims,
- carry out checks on declarations and donations,
- verify any other income on which repayment of tax has been claimed

as appropriate.

7.1.3 The Inland Revenue have published a Code of Practice (Code of Practice 5) entitled "Inspection of Charities' Records". The leaflet tells charities how the Inland Revenue carry out their inspections. In particular it explains charities' rights, and promises that charities will be treated fairly and courteously. It also promises that the Inland Revenue will provide help where appropriate. A copy of Code of Practice 5 will be issued to charities before an inspection. A copy can also be obtained from the charity pages on the Inland Revenue website ([www.inlandrevenue.gov.uk](http://www.inlandrevenue.gov.uk)), or by post from IR (Charities).

- 7.1.4 IR (Charities) is always willing to give advice to new charities (or existing charities implementing major systems or procedure changes) and, if necessary, arrange a help visit.
- 7.1.5 Most inspections are routine. The timing and frequency at which charities are inspected depends on
- the size of claim
  - the results of any previous inspection, and
  - any other information.

However, other factors, such as significant fluctuations in claim size, can also affect the timing of an inspection. Audits are generally conducted after repayment and are based around a particular claim or series of claims. Some claims, however, may be selected for review prior to repayment.

- 7.1.6 Some charities may be the subject of an **integrated audit**. These inspections will go beyond the audit objectives outlined in Appendix F below. The auditor will not only wish to review the records relating to specific claims but will also conduct a wider review of the charity's activities and accounting procedures. For example, the expenditure of the charity may be reviewed to determine whether all sums paid out by the charity were for charitable purposes only.

## **7.2 Records to be retained**

- 7.2.1 Charities must make available for inspection all records to show that they have submitted correct repayment claims. The Code of Practice 5 explains the Inland Revenue's general approach to the examination of records. Auditors will want to see, or have available on request, the following documents or records:
- Gift Aid declarations (originals or copies where stored on computer or microfiche) and related correspondence. These will include sponsor forms where the donors' declarations are made on the sponsor forms.
  - records of Gift Aid donations
  - certificates verifying income received under deduction of tax (for example, R185 forms), and
  - all computer records, printouts, reconciliations, bank statements, microfiche ledgers, etc. relating to the production of claims for the current and preceding tax year.

## **7.3 How long should records be retained?**

- 7.3.1 Although auditors will wish to inspect recent records, trusts which are charities should retain all records until the later of:
- the 31 January next but one after the end of the tax year to which the tax reclaim relates (for example, if you make a tax reclaim for the tax year 2000-2001, until 31 January 2003)

- one year after you make your tax reclaim, rounded to the end of the next quarter (for example, if you make a tax reclaim on 25 May 2002, until 30 June 2003)
  - when IR (Charities) completes any audit it has commenced.
- 7.3.2 If the charity is not a charitable trust (a charitable company, for example), it must keep records until six years after the end of the accounting period to which the tax reclaim relates.
- 7.3.3 These are the minimum periods for which records must be kept. In the event that an auditor from IR (Charities) audits the charity's tax reclaim, he or she may re-open tax reclaims for earlier years if errors are identified. Therefore, it may be in the interests of the charity to keep records for longer than the minimum period.
- 7.3.4 Auditors may need to see other records to check charities' systems and procedures. If an integrated audit is undertaken (on which, see paragraph 7.1.6 above), the accounts of the charity may also be reviewed.

#### **7.4 Means of keeping records**

- 7.4.1 Charities may hold the records (including Gift Aid declarations and related correspondence) on computer or other non-paper medium (e.g. microfiche). Records held in this way must be
- retrievable, and
  - easily accessible by auditors.
- 7.4.2 The Inland Revenue will accept Gift Aid declarations in an imaged form without paper originals, provided the imaged document and any hard copy print-outs are easily legible, and
- on the day on which a paper document is captured, the operator signs and dates an authentication certificate to the effect that, to the best of his or her knowledge and belief, the facsimiles are a complete and accurate record of the documents,
  - on the day on which the documents are destroyed, the person who destroys them signs and dates a destruction certificate to that effect,
  - on being required to do so by an officer of the Board of Inland Revenue, the charity will, within a reasonable time, provide the officer with a hard copy of the imaged document and the appropriate authentication and destruction certificates.

Authentication and destruction certificates may be completed for batches of documents - for example, declaration forms received in a period and imaged on a particular day.

- 7.4.3 Photocopies of original declarations will be accepted in instances where the declaration has been sent to a bank because the document contains

instructions from the donor to the bank. The photocopy should contain an authentication certificate by the person making the copy.

## **7.5 Before the inspection**

- 7.5.1 IR (Charities) will generally give a charity four weeks notice of inspection. The auditor will always make contact with the charity by telephone, prior to the visit, to discuss arrangements for the inspection. If the charity's claims are large or the inspection is being conducted as part of an integrated audit, with aspects of the charity's tax return also being considered, a pre-inspection meeting may be appropriate.
- 7.5.2 IR Charities may also issue a pre-audit questionnaire at the same time as they issue the formal notice of inspection. The pre-audit questionnaire is designed to give auditors enough information on the charity to enable it to identify the type of issues that may arise in the course of the inspection. There is no standard format for this questionnaire. It will vary according to the circumstances of the particular charity. The questionnaires will be as short and simple as possible.

## **7.6 The Inspection**

- 7.6.1 Auditors will normally visit the location where the charity's records are maintained. Records must be available for inspection in the UK. If any records are held by another person or organisation, the charity must ensure that they are made available to the auditor at the time of the visit.
- 7.6.2 For smaller charities the auditor may ask for the records to be submitted to IR (Charities) for a desk-based audit at the auditor's offices.
- 7.6.3 Auditors use the audit objectives listed at Appendix F to test that charities' claims to repayment are correct.
- 7.6.4 Auditors will review the charity's procedures, Gift Aid declarations and donations, and any other certificates used to support the claim. In larger cases they will examine a statistically valid sample, which will allow the results to be accurately extrapolated.

## **7.7 After the inspection**

- 7.7.1 Auditors will usually report their findings to the charity within 28 days of an inspection visit. This will be in the form of a written audit report.
- 7.7.2 Where auditors are satisfied that claims by the charity have been made correctly, they will advise that no further action is needed.
- 7.7.3 Where auditors believe that the charity has submitted incorrect claims, they will ask it to repay an amount based on the incorrect amount claimed.
- 7.7.4 Incorrect claims by a charity may attract interest.
- 7.7.5 Incorrect claims may also attract penalties where claims were made fraudulently or negligently.

## **7.8 Recovery for previous tax years**

7.8.1 The Inland Revenue's Statement of Practice SP8/91 explains the circumstances in which the Inland Revenue will recover tax where a claim or an assessment has previously been settled by agreement (for example, following a previous audit). Briefly, the Inland Revenue will not go back on an agreement unless the information on which that agreement was based was such as to mislead the Inland Revenue. In line with this practice, IR (Charities) will not seek to recover on claims made before the end of the period covered by the last inspection (whether or not that earlier inspection resulted in any recovery), unless

- the settlement was based on misleading or incorrect information provided by the charity
- the settlement was based on computational errors which the charity could not reasonably believe were correct or intended, or
- errors arose that were not readily susceptible to inspection checks.

7.8.2 The protection afforded by the Statement of Practice does not extend to claims made after the end of the period covered by the last inspection.

## **7.9 Other issues**

7.9.1 There may be some particular issues which arise out of an inspection or which are of special concern to a charity. IR (Charities) will be pleased to give advice or explain their approach on any issue that arises. The charity will always receive an Audit Commitment Statement with the inspection notice. This contains details of the person the charity should contact if there are any issues that cannot be satisfactorily resolved with the auditor. Further copies of the audit Commitment Statement can be obtained by telephoning 0151 472 6129.