



Understanding charity accounts

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What we will cover:

- Overview of the regulatory framework and accounting standards for charities
- Understanding the unique features of charity accounts and financial reporting
- Importance of the notes and their role in providing additional information

Any specific requests?





Framework for charity accounts

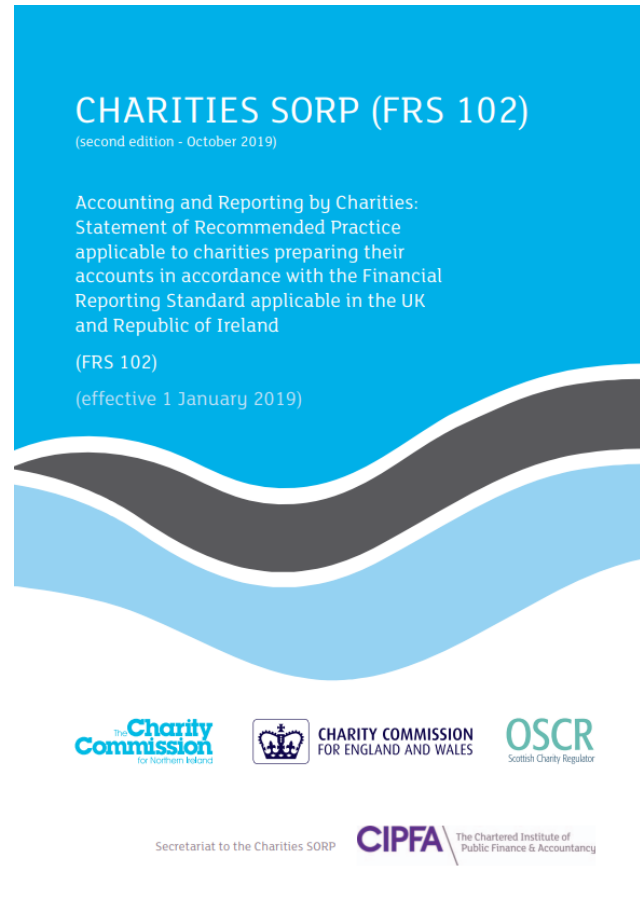
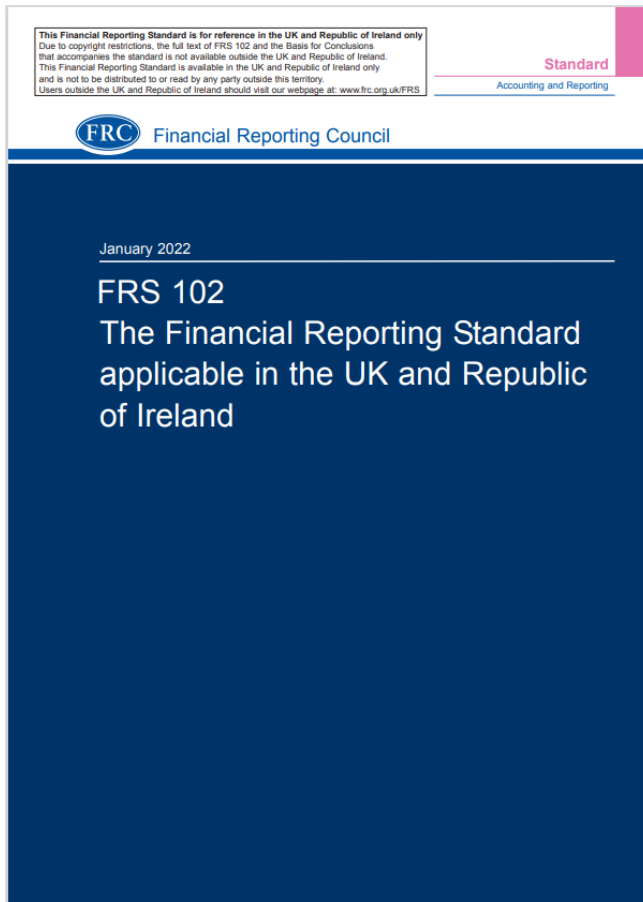
Receipts and Payments accounts

- Option for small charities but not company charities

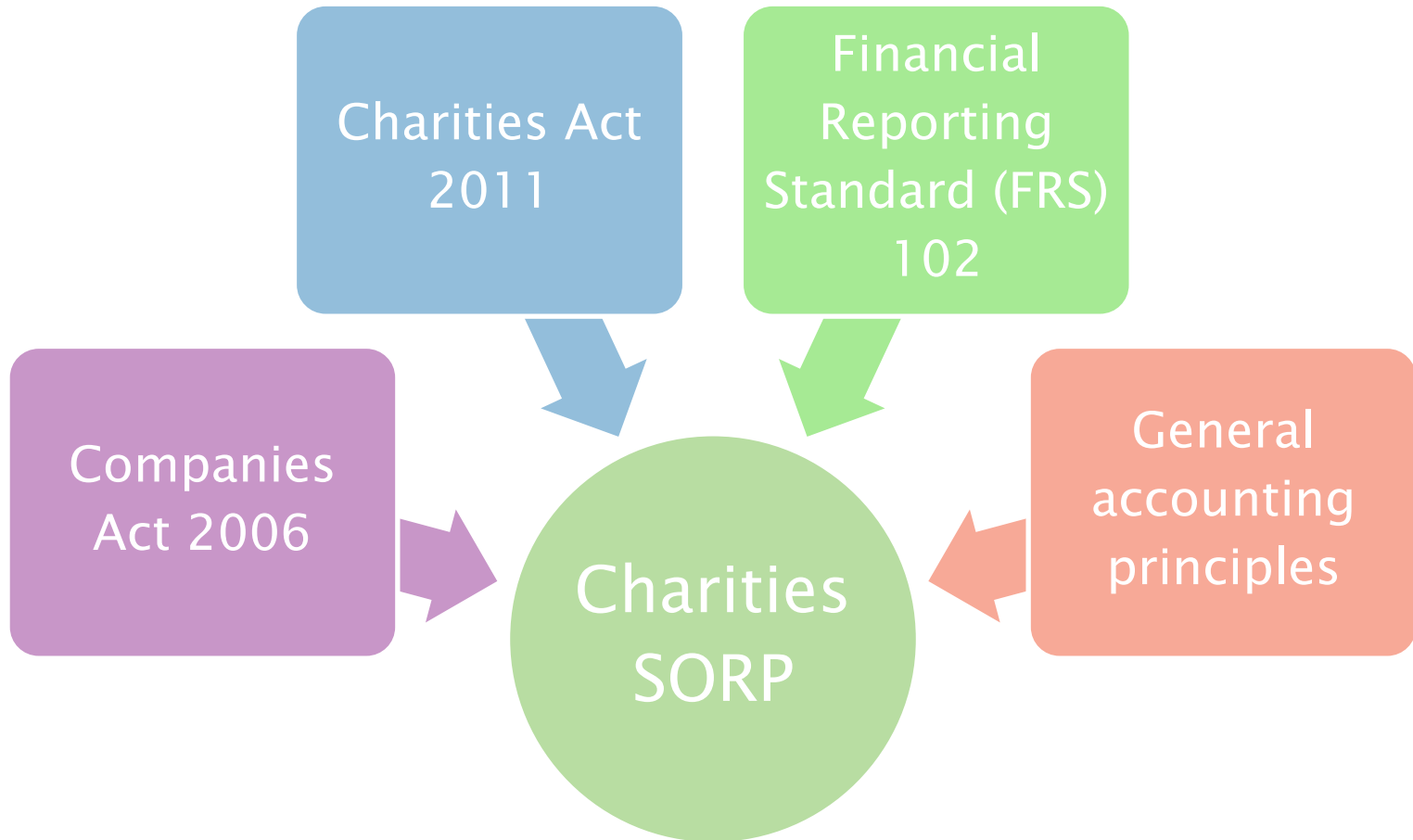
FRS 102 Charities SORP accounts

- Applies to all charities preparing “accruals accounts”

FRS 102 and Charities SORP



Regulatory background





What is the SORP?

- Statement Of Recommended Practice
- For statutory accounts
- Accounting rules in a charity context
 - Removes profit as measure of success
 - Surplus/deficit is often just a result of timing
 - Still have to follow core rules
- Activity based reporting
- Use of resources to further charitable aims
 - Objects, activities, achievements, impact



What is the SORP?

Accessible,
modular
document

- Core modules
- Additional sections
- Detailed glossary of terms

Specific
terms

- Must – has to be included
- Should – best practice to include
- May – options available
- Larger charities = over £500k income



SORP accounts components

- Trustees' annual report
- Auditor's / Independent Examiner's report
- Statement of financial activities (SoFA)
- Balance sheet(s)
- Statement of cash flows
- Notes to the accounts



What's the same as company accounts?

- Basic principles regarding the preparation of the accounts
- Statement of financial performance
- Balance sheet
- Statement of cash flow
- Notes



What's different about charity accounts?

- Funds – unrestricted and restricted
- SOFA (not profit and loss account)
- Income and expenditure by activity
- Focus on funds in total rather than result for the year
- Public Benefit reporting
- More disclosures



SORP: Activity based reporting

- Activity based reporting
- Reflected in statement of financial activities (SoFA) – funding for activities linked to expenditure on those activities
- Link to trustees' annual report



Trustees' annual report

Who are we?	Reference & admin
How do we work?	Structure, governance & management
What are we doing?	Objectives & activities
What did we do & how well did we do it?	Achievements & performance
How did we afford it?	Financial review
What are we planning?	Plans for future periods
What else do we look after?	Custodianship



Questions for you to consider:

- What are your charitable activities?
- Is there a clear thread running from your trustees' report to accounts?
- How do you report in your management accounts?
- Would your charity's accounts be easier to understand with clearer charitable activities?



SORP language

Profit and loss account	Income and expenditure account	SoFA
Profit	Surplus	Net income
Loss	Deficit	Net expenditure



Fund accounting

Total funds

Unrestricted

Restricted

General

Designated

Income

Endowment (capital)

Permanent

Expendable



Unrestricted funds

Funds received for charitable objects

- General donations
- General legacies
- Self-generated income from sales of goods or services
- Investment income

Designated funds

- Funds earmarked by trustees for a particular purpose



What are restricted funds?

- SORP definition:

“Funds held on specific trusts under charity law are classed as restricted funds. The specific trusts may be declared by the donor when making the gift or may result from the terms of an appeal for funds. The specific trusts establish the purpose for which a charity can lawfully use the restricted funds. It is possible that a charity may have several individual restricted funds, each for a particular purpose of the charity.”



Restricted income funds

- Restriction imposed by donor
- Restricted funds may be
 - For a specified project
 - For a specific geographical area
 - Funds raised in an appeal
 - Investment income (if generated from invested restricted funds)
- Funds must be spent for purpose
- Can be assets



Endowment funds

- Similar to restricted funds
 - Permanent – no **ability** to spend capital
 - Expendable – no **requirement** to spend capital
- Capital invested to generate a return to spend on charitable activities
- Income generated may be restricted or unrestricted – check terms



Fund disclosure

- Detailed analysis of funds in notes
- Separate income & expenditure by fund
- Transfers between funds
- Narrative explanations for each fund



Arts Theatre Trust

Analysis of movements in restricted funds

	Balance at 1 April 2019 £'000	Income £'000	Expenditure £'000	Transfers £'000	Funds 31 March 2020 £'000
Piano fund	9	-	(1)	-	8
Book festival	3	5	(3)	-	5
Poets course	-	20	(5)	-	15
Total	12	25	(9)	-	28



Arts Theatre Trust

Analysis of movements in unrestricted funds

	Balance 1 April 2019	Income	Expenditure	Transfers	Funds 31 March 2020
	£'000	£'000	£'000	£'000	£'000
General fund	(243)	1637	(1,704)	(13)	(323)
Designated development fund	50	-	(12)	-	38
Designated props and costumes	82	-	-	(9)	73
Designated property assets fund	1760	-	(82)	22	1700
Total	1,649	1637	(1798)	0	1,488



Arts Theatre Trust


Analysis of group net assets between funds

	General Fund £'000	Designated Funds £'000	Restricted Funds £'000	Total £'000
Tangible fixed assets	-	1700	-	1700
Cash at bank and in hand	136	38	28	202
Other net current assets/(liabilities)	(159)	73	-	(86)
Creditors of more than one year	(300)	-	-	(300)
Total	(323)	1,811	28	1,516



Statement of financial activities (SoFA)

- Grouped by activities, not types of income/expenditure
- Income headings link to expenditure
- Distinguish between funds
- Support and governance costs allocated to charitable activities
- Should correspond to trustees' annual report
- Detailed notes



	Note	Unrestricted Funds £'000	Restricted Funds £'000	Total Funds 2020 £'000	Total Funds 2019 £'000
Income:					
Donations and legacies	4	35	25	60	44
<i>Income from charitable activities:</i>					
Operation of theatre and arts centre	5	1,105	-	1,105	1,163
<i>Income from other trading activities:</i>					
Commercial trading operations	6	479	-	479	595
Investment income	7	18	-	18	16
Total income		1,637	25	1,662	1,818
Expenditure					
<i>Costs of raising funds:</i>					
Commercial trading operations		323	-	323	390
<i>Expenditure on charitable activities:</i>					
Operation of theatre and arts centre	8	1,475	9	1,484	1,422
Total expenditure		1,798	9	1,807	1,812



Incoming resources

Donations
and legacies

Charitable
activities

Other trading
activities

Income from
investments

Other



Donations and legacies



Gifts given on a voluntary basis



Grants of a general nature



No expectation of a service
in return

Can include subscriptions if
substance is donation



Donated goods and services



Charitable activities

Grants and donations for specific charitable activities

Fees for services from charitable activities (primary purpose trading)

Use sub-headings to report your charitable activities in line with those in the trustees' report



Other trading activities

Non-charitable trading

Fundraising events

Retail income

Property income

Sponsorship

Membership subscriptions

Lottery income



Income recognition

Recognition criteria are :

- Entitlement – control over right or access to economic benefits has passed to the charity
- Measurement – the value can be measured reliably
- Probable – it is **more likely than not** that the economic benefits associated with the transaction of gift will flow to the charity

What do you find difficult in relation to income recognition?

- If you prepare the accounts, what is tricky to calculate/estimate?
- If you reviewing the accounts, what is hard to understand?
- What disagreements have you had with your examiner/auditor?





Common SORP issues for income

- Restricted or unrestricted?
- Grant or contract?
- Recognise income or defer?
- Gifts in kind
- Services in kind
- Legacies



Restricted or unrestricted?

- Grants may be restricted or unrestricted
- Are purposes of grant narrower than objects of charity?
- Contracts not donations so usually unrestricted
- Unless terms of contract limit use of “surplus”, so in substance are restricted



Grants v Contracts

Grants	Contracts
Gift, given freely by the donor (Goods / services not received in return)	Agreement between 2 parties: Direct link between consideration and service
Funding sought for existing service	Commissioned service
Likely areas to benefit	Detailed specifications
Failure to use grant as intended: repay full grant or trustees are personally liable	Failure to deliver services / provide consideration: sue for compensation and damages
Unspent grant can be clawed back	Surplus on contract can be kept



Grants v Contracts (continued)

Grants	Contracts
Accounting treatment: May include amount before service delivered (unless performance related)	Accounting treatment: Recognise to extent services have been performed
Restricted if purpose is narrower than the overall objects of the charity	Usually unrestricted.
Donation and legacies or Incoming resources from charitable activities	Income resources from charitable activities
Non-business activity – outside scope of VAT	Business activity for VAT
Trust Law	Contract Law



Recognise income or defer?

- Recognise income as it is earned
- Consider extent to which services have been provided
- Defer unearned income – so income received in advance of services delivered
- Defer grants only if not entitled to grant income
 - ?? Grants for salary costs??



Donated goods and services

- Recognise if you would have paid for it
- Benefit is quantifiable and measurable
- Value to charity receiving
- **Do not** include volunteer time
 - Report in trustees' report



Gifts in kind

Type of gift	Accounting treatment
Capital equipment for charity's own use	Recognise fixed asset and donation at fair value
Goods for distribution to beneficiaries	<ul style="list-style-type: none">• Recognise stock and donation at fair value on receipt• Consider impairment• When distributed, expense at carrying value of stock
Goods for re-sale	Recognise stock at fair value (expected proceeds less expected costs to sell) on receipt, unless impracticable



Services in kind

- E.g. office space, legal services
- Recognise as donation if:
 - For use of the charity
 - Charity would otherwise purchase the service
- Value to the charity
 - The amount charity would pay in open market for an alternative item that would give equivalent benefit
- Income and expenditure
- Not general volunteers



Income recognition – some examples

- Donations
- Grants
- Income from fundraising
- Membership subscriptions
- Legacies
 - Entitlement – Probate? Challenges? Estate accounts?
 - Measurement – pecuniary vs residual
 - Probability



Legacies – considerations

- Circumstances of each legacy
- Portfolio approach permitted
- Entitlement
 - Evidence gift left to the charity
 - Executors satisfied legacy not subject to claims
- Receipt probable
 - Probate granted
 - Conditions of legacy met or within control
 - Executors established sufficient assets in estate to settle liabilities and pay legacy
- If notified post year end – accrue if executors’ decision made before year end



Resources expended

Charitable activities

- Activities that further the charity's aims and purposes
- Activities reported should align with those described in trustees' report

Costs of generating funds

- Fundraising and trading
- Investment management

Support and governance costs

- Undertaken to support the activities of the charity
- Not activities in their own right



Support and governance costs

- Allocate to the activities they support
- Disclosure and analysis of total support costs in notes
- Amount or percentage of support costs allocated to each activity
- Accounting policies should also explain methods of cost allocation

Analysis of expenditure on charitable activities – Current year

	Concerts and stage performances	Visiting arts exhibitions and installations	Education including residences	Total
	£'000	£'000	£'000	£'000
Artists' and exhibition fees	389	35	-	424
Production expenses	129	6	19	154
Courses and residences	-	-	68	68
Education and outreach	-	-	59	59
Box office and front of house	164	-	-	164
Promotion and marketing	76	5	4	85
Central premises costs	187	15	21	223
Bank loan interest	60	-	-	60
Depreciation	78	3	1	82
ATC Park – commissioning	12	-	-	12
Piano maintenance	1	-	-	1
Governance costs (see note 10)	42	3	3	48
Support costs (see note 10)	92	6	6	104
Total	1,230	73	181	1,484

Analysis of support and governance costs

	General support £'000	Governance function £'000	Total £'000	Basis of apportionment
Catering and venue hire for trustee and other business meetings	21	1	22	Invoiced events
Salaries, wages and related costs	64	22	86	Allocated on time
General office	19	6	25	Pro rata to staff full time equivalents
Audit fees	-	10	10	Governance
Accountancy services	-	5	5	Governance
Legal and other professional fees	-	4	4	Governance
Total	104	48	152	



Allocation methods

- Common allocation methods:
 - Staff numbers
 - Staff time
 - Staff costs
 - Number of clients/beneficiaries
 - Space occupied



Staff and trustee costs

- Staff paid > £60k
 - State number in each £10k band
 - Salaries and benefits only
- Termination and redundancy costs
- Trustee payments and expenses
- Other disclosures
 - Key management personnel
 - Staff numbers



Other disclosures for trustees

- Expenses
 - reimbursed
 - paid to third parties
- Disclose expenses waived by trustees, unless immaterial
- Disclose aggregate donations from related parties (including trustees)



Trustees' annual report – all

- Objectives and activities
 - Public benefit
- Achievements and performance
- Financial review
 - Reserves policy and going concern (more detail if large)
- Structure, governance and management
- Reference and administrative details
- Requirements of Companies Act



Trustees' annual report

Who are we?	Reference & admin
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Trustees' annual report – a few challenges

- Financial review
 - Principal funding sources & how expenditure has supported key objectives
 - Reserves policy
 - Risk policy, principal risks and management of those
 - Any funds in deficit
 - Investment policy & ethical policies, if relevant
 - Remuneration policy



Reserves

- Policy
 - Why you need reserves, how much and what for
 - Compare with actual level
 - No standard formula or approach
- What does this depend on?
 - Income volatility and risk
 - Nature of costs – fixed or flexible
 - Future plans and needs
 - Scenario planning and stress testing



‘Free’ reserves

Reserves the charity holds at the end of the reporting period *after* making allowance for any *restricted funds*, and the amount of *designations, commitments* (not provided for as a liability in the accounts) or the carrying amount of *functional assets*



Going concern

A basic underlying accounting assumption that an organisation will be able to continue operating for a period of at least 12 months from the date the accounts are signed

- Can meet all liabilities as they fall due



Going concern

- Trustees must make their own assessment and confirm this at point of approval
- If uncertainties, the nature of these must be explained in the trustees' report
- Auditors are required to review and conclude



Fundraising disclosures

- **Must include:**
 - The charity's approach to fundraising, including its activities and whether it uses professional fundraisers or commercial participators
 - Participation in fundraising regulation and compliance with codes
 - Any non-compliance with any code
 - The number of complaints received
 - How the charity protects vulnerable people
 - How the charity monitors its fundraising activities undertaken by third parties



Charity governance code

- Not statutory requirements but application is ‘strongly recommended’
- ‘Apply or explain’
- Report application in trustees’ report

<https://www.charitygovernancecode.org>



What does good reporting look like?

Link to
activities on
SOFA

Visuals for
financial
review

What we said,
what we did

Set clear
objectives for
next year

Use of
questions

Case studies
or stories



Jo's Recipe for the Report

- Reason for being
- Review of the year
- Results
- Reserves
- Risks
- Remuneration policy
- Relationships & related parties
- Raising funds (fundraising approach)
- Reference & admin info



Thresholds

Large charity – income in excess £500k

Charity audit threshold (charity):

- E&W: £1 million
- Scotland: £500k

Non-small company – exceed 2 of 3 for two years of:

- Turnover > £10.2 million
- Gross assets > £5.1 million
- Employees > 50 (average head count)



SORP concessions for smaller charities

- Statement of cash flows not required
- Simplified Trustees' Annual Report
- Option to use natural classifications in SOFA

Watch this space for new SORP...



Signposting to resources

SORP microsite www.charitySORP.org

- FRS102 SORP
- Illustrative example accounts
 - Arts Theatre Trust
 - The Rosanna Grant Trust
- Information sheets and help sheets



Signposting to resources

Sayer Vincent www.sayervincent.co.uk

- Free resources to download
 - Made Simple guides
 - SORP 2015 made simple
 - Grants and contracts made simple
 - Reading charity accounts made simple
 - Beyond Reserves
 - Honorary Treasurer's Handbook
 - Re-Thinking Risk: Beyond the Tick Box

Questions?

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