KEY GUIDES

The Charity Treasurer's Handbook

6th edition

Elaine Alsop and
Gareth G. Morgan

dsc
directory of social change

What they said about the book…

'This is a very reliable book that, over the years, I have found really helpful for dipping into to answer both queries that arise in my work and queries coming in from my charity clients.'
Ian Barrett FCA FCIE, Barretts Chartered Accountants and Chartered Tax Advisers

'This plain-English guide will help trustees and managers navigate their way through the myriad of issues that any charity is likely to face. It will help them to make informed decisions, stay compliant and be more effective.'
Simon Bostrom FCIE, Chief Accountant, West Yorkshire Community Accountancy Service CIO

'Responsibility for the finances of a charity can be a daunting prospect – you need all the help you can get! This comprehensive guide navigates those challenges with clarity and authority while being easy to read. I urge you to learn from it.'
Richard Bray ACA DChA, Chair, The Charity Tax Group

'*The Charity Treasurer's Handbook* is written in a very accessible manner, balancing the legal, regulatory and finance aspects with practical examples. Well-structured sections and chapters make it easy to find the help needed on specific subjects. It's a ready reference for new and experienced treasurers, with the updates in the sixth edition being particularly useful.'
Carolyn Cordery, Adjunct Professor, Victoria University of Wellington and Chair, New Zealand Accounting Standards Board

'Written in an accessible style and helpful format, this comprehensive and incredibly supportive book will be of immense value to charity treasurers and anyone who needs an introduction to charity accountancy, law and processes.'
Jon Dean, Associate Professor, Sheffield Hallam University and Chair of the Voluntary Sector Studies Network

'*The Charity Treasurer's Handbook* provides a clear and concise account of charity finance and what charities must comply with and why. It explains all you need to consider to prepare for independent scrutiny. Recommended for charities of all sizes.'
Mark Heaton FCCA FCIE DChA, Chair, Association of Charity Independent Examiners

‘Having worked in the third sector for almost 30 years and served on several charity boards in this time, I find *The Charity Treasurer’s Handbook* an invaluable resource for anyone who wants to better understand and get to grips with what good financial governance looks like. This handbook brilliantly takes complex concepts and makes them accessible for both the finance novice and more experienced treasurer.’
Neil Mathers, Executive Director for Scotland, Samaritans

‘My copy of the previous version of this handbook was so dog-eared from overuse that I definitely needed a new edition! It’s my first port of call to check facts, which have been updated and comprehensively revised to reflect the world in which we, charity treasurers, now live. I happily recommend this sixth edition of the book to our members and anyone else concerned with charity finances.’
Nicola Silverleaf, Treasurer and Trustee, The Honorary Treasurers Forum

KEY GUIDES

The Charity Treasurer's Handbook

6th edition

Elaine Alsop
Gareth G. Morgan

dsc
directory of social change

Published by the Directory of Social Change (Registered Charity no. 800517 in England and Wales)

Registered address: Directory of Social Change, First Floor, 10 Queen Street Place, London EC4R 1BE

Tel: 020 4526 5995

Visit www.dsc.org.uk to find out more about our books, subscription funding website and training events. You can also sign up for e-newsletters so that you're always the first to hear about what's new.

The publisher welcomes suggestions and comments that will help to inform and improve future versions of this and all of our titles. Please give us your feedback by emailing publications@dsc.org.uk.

This is an introductory book. It seeks to explain the framework of charity accounting but it does not provide a full statement of the law. Where legal issues are covered, they are based on the position as at 9 August 2023, but there could be subsequent changes. Many accounting concepts are presented at an overview level only – particularly in areas such as accruals accounting, charity taxation and production of final accounts under the Charities Statement of Recommended Practice (SORP). It should be understood that this publication is intended for guidance only and is not a substitute for professional or legal advice. No responsibility for loss occasioned as a result of any person acting or refraining from acting on the basis of this publication can be accepted by the authors or publisher.

First published 2002
Second edition 2008
Third edition 2010
Reprinted 2012
Fourth print and digital editions 2014
Reprinted 2015
Fifth editions 2017
Sixth editions 2023

ISBN 978 1 78482 088 6 (print edition)
ISBN 978 1 78482 089 3 (digital edition)

British Library Cataloguing in Publication Data
A catalogue record for this book is available from the British Library

Cover and text design by Kate Griffith
Typeset by Marlinzo Services, Frome
Printed and bound in the UK by Page Bros, Norwich

MIX
Paper from responsible sources
FSC® C023114
FSC
www.fsc.org

Contents

About the series

This series of key guides is designed for people involved with not-for-profit organisations of any size, no matter how you define your organisation – voluntary, community, non-governmental or social enterprise. All the titles offer practical, comprehensive, yet accessible advice to enable readers to get the most out of their roles and responsibilities.

There are several other titles available in this series, you can find details about the whole range at www.dsc.org.uk/publication/key-guides.

For further information, please contact the Directory of Social Change (see page vii for details).

About the Directory of Social Change

At the Directory of Social Change (DSC), we believe that the world is made better by people coming together to serve their communities and each other. For us, an independent voluntary sector is at the heart of that social change and we exist to support charities, voluntary organisations and community groups in the work they do. Our role is to:

- **provide practical information** on a range of topics from fundraising to project management in both our printed publications and our e-books;
- **offer training** through public courses, events and in-house services;
- **research funders** and maintain a subscription database, *Funds Online*, with details on funding from grant-making charities, companies and government sources;
- **offer bespoke research** to voluntary sector organisations in order to evaluate projects, identify new opportunities and help make sense of existing data;
- **stimulate debate and campaign** on key issues that affect the voluntary sector, particularly to champion the concerns of smaller charities.

We are a registered charity ourselves but we self-fund most of our work. We charge for services but cross-subsidise those which charities particularly need and cannot easily afford.

Visit our website **www.dsc.org.uk** to see how we can help you to help others and have a look at **www.fundsonline.org.uk** to see how DSC could improve your fundraising. Alternatively, call our friendly team at **020 4526 5995** to chat about your needs or drop us a line at **cs@dsc.org.uk**.

About the authors

Elaine Alsop is a chartered accountant and has been working solely with charities and other third sector organisations for over 15 years. She is Director of EA Independent Ltd, which works with and advises smaller charities on a wide range of finance and governance issues, including annual reporting and independent examination. Elaine particularly enjoys working closely with trustees to support them in meeting their responsibilities by making charity finance more accessible.

Elaine is an ACA with the Institute of Chartered Accountants in England and Wales (ICAEW) and holds the ICAEW Diploma in Charity Accounting. She is a Fellow of the Association of Charity Independent Examiners (ACIE) and has a master's in Charity Resource Management from Sheffield Hallam University. In addition to running her accountancy practice, Elaine is the finance manager of a local charity supporting children and a trustee of a women's charity. Having these distinct roles provides her with a well-rounded insight into charity financial management.

Gareth Morgan was the sole author of the first five editions of this book but has acted as co-author for this latest edition. He has both directly contributed a few sections and reviewed all the new content prepared by Elaine Alsop.

Gareth has been involved in advice, research and teaching on charity accounting and regulation for around 30 years. He is Emeritus Professor of Charity Studies at Sheffield Hallam University, where he led a wide range of charity sector research and was course leader of the MSc in Charity Resource Management. Until recently, he also worked as senior partner of charity consultants The Kubernesis Partnership LLP, supporting a wide range of mainly small and medium-sized charities on issues such as charity accounting, fundraising, mergers and restructuring – both in England and Scotland. In 2018/19 Gareth chaired the *Charities SORP Governance Review* on behalf of the four charity regulators in the UK and Ireland. He has worked as an adviser or specialist committee member on charity issues with a number of professional bodies, most recently the Association of Charity Independent Examiners (ACIE) and the Institute of Chartered Accountants of Scotland (ICAS).

He is the author of *Charitable Incorporated Organisations*, also published by DSC in this series.

Acknowledgements

I first came across *The Charity Treasurer's Handbook* some time ago when I was looking to develop my understanding about charity finances. It was the first comprehensive guide I had found, and it has been extremely helpful in my work with small charities ever since. I was delighted, although daunted, to be asked to co-author this sixth edition, and I wish to thank Gareth Morgan for suggesting that I take this on. It has been an honour to work with him and I am most grateful for the extensive knowledge and enthusiasm for charity regulation and finance that he has shared, and for his support throughout the process.

I would like to thank the Directory of Social Change (DSC) for moving forward with a revised edition of this handbook, in particular for the support and guidance of John Martin and Gabi Zagnojute. I am extremely grateful to Ian Barrett for his comprehensive review of the first draft of the book and the comments and suggestions he made, which I have taken on board. And I also wish to thank copy-editor Hazel Bird for her input into the text.

It is the passion of the trustees, staff and volunteers that drives small organisations to make a big impact for their beneficiaries. I had the charities which I am privileged to be involved with in mind when writing, and I am thankful to those I have worked alongside for sharing their insight and enthusiasm for the charity sector.

Finally, I could not have co-authored this book without the encouragement and patience of my fantastic family – Matthew, Edward and Oliver – thank you.

Elaine Alsop, June 2023

I would like to thank DSC for their ongoing commitment to *The Charity Treasurer's Handbook* and extend a special thank you to Elaine Alsop for taking over as lead author. She has restructured the chapters and redrafted almost everything from scratch: a huge commitment. It has been a great privilege working with her.

I remain indebted to a wide range of people in the charity sector who have stimulated my thinking and especially to my former students at Sheffield Hallam University – including Elaine. I would also like to repeat the thanks I expressed in earlier editions for the amazing support of my wife and business partner, Sharon.

Gareth Morgan, June 2023

Foreword

We are delighted to introduce the sixth edition of this highly respected publication. Since the previous edition was published in 2017, the landscape for charities has transformed. We have lived through a global pandemic and are grappling with economic pressures and geopolitical uncertainties. Amidst these tensions, the role of the treasurer has become increasingly important to guide charity boards on the financial impact of their strategic choices.

The charity sector is a tapestry of diverse organisations, each with its own unique focus and mission. However, they all are united by a charitable endeavour and a commitment to serving the public good. While maximising charitable impact is rightly at the forefront of how charities are run, it is important for the board of trustees to understand the accounting and tax implications of their decisions. This is where the expertise of the treasurer shines and helps charities to connect financial realities with ambitious objectives.

Serving as a trusted companion for both seasoned and new treasurers, this book provides a solid foundation of knowledge on the wide range of responsibilities and duties of a charity treasurer. It guides the reader step by step through the different aspects of the role and delves into the nuances and peculiarities of charity finance, accounting and tax in an accessible and informative manner.

This is a reliable and up-to-date resource, covering developments such as the technological advances in fundraising and relevant changes introduced by the Charities Act 2022 in England and Wales. We hope that, by offering a valuable reference tool, this handbook will inspire new volunteers to take on the office of treasurer and make a meaningful contribution to society.

It is also vital to remember that the landscape of charity finance continues to evolve beyond the book's publication. As treasurers, it is our responsibility to remain up to date with future developments that impact our role. The release of the next Charities Statement of Recommended Practice (SORP) will impact the financial reporting of charities preparing 'true and fair' accounts, while developments in sustainability reporting may require our attention in the future. Additionally, we need to keep abreast with changes in tax and regulation.

Treasurers will remain at the forefront of instilling financial leadership within charities. By communicating financial insights, they support the whole board of trustees in playing their part in the responsible management of the charity's resources and to make informed decisions collectively.

We extend our congratulations to the authors of this guide and are sure that it will equip readers with the knowledge to fulfil the treasurer role with confidence.

Daniel Chan MBE, Chair, Institute of Chartered Accountants in England and Wales Charity Committee

Kristina Kopic FCA DChA, Head of Charity, Institute of Chartered Accountants in England and Wales

Preface

The Charity Treasurer's Handbook is designed to give a comprehensive introduction to charity accounting, even to those who have no previous finance experience. It aims to provide a balance of detailed technical knowledge and practical application that can be read gradually as a whole or picked up when needed to research a particular topic. For more experienced finance professionals, the charity-specific information will be useful if taking on a role in a charity.

The book was first written by Gareth Morgan in 2002 to help charity treasurers navigate the complexities and obligations they may face in their role. It has been updated through five editions to reflect changes in charity law and developments of accounting standards and to clarify issues that have become particularly important to the sector over the past twenty years. Charity law is devolved in the UK, which means there are specific rules to follow depending on whether your charity is based in England and Wales, Scotland or Northern Ireland, and this handbook has always attempted to make similarities and differences clear.

This updated sixth edition, authored by Elaine Alsop and Gareth Morgan, builds on the content of previous versions, looking at charity finances from the perspective of treasurers and finance officers in smaller charities. It uses the term 'treasurer' to mean the trustee role focused on the finances of a charity, and the term 'finance officer' to refer to a person (such as a bookkeeper or finance manager) employed by the trustees to manage the finances on their behalf and report back to them for decision-making. The term 'smaller charity' typically refers to charities under the audit threshold, which is currently set at an annual income of £1 million in England and Wales (and at £500,000 for charities in Scotland and Northern Ireland). However, treasurers and finance officers of larger charities will find much of the content is applicable to them too.

The book has a new structure compared to the previous five editions. It aims to take the reader through topics they may encounter on a regular basis, then concentrates on more specific charity situations and finishes by looking at annual reporting. In doing this, it first considers matters faced by all charities, such as trustee responsibilities, fund accounting, risks and financial controls. With evolving technology in mind, there are suggestions for how to protect your charity's resources in an increasingly cashless and digital society. The book contains comprehensive sections on bookkeeping and understanding reserves, and offers suggestions of how financial management can help with decision-making and to improve resilience. There is an introduction to more specific topics, including charity trading, and the potential considerations for VAT and corporation tax. There is a chapter setting out the Gift Aid regime, and another looking at the implications of working with volunteers and freelancers and employing people.

The final chapters of the book are concerned with the annual accounting and reporting process, regardless of the size of your charity. This includes information on what type of accounts a charity needs to prepare and what should be included in a trustees' annual report. There are chapters explaining how to prepare both accounts under the receipts and payments regime and accruals accounts under the current Charities Statement of Recommended Practice (SORP). There is information on what to expect from an independent examination or audit, and advice on whom to appoint to carry out either of those tasks.

While *The Charity Treasurer's Handbook* cannot possibly cover all situations or deal with every issue in full, we hope it gives the reader sufficient understanding to be able to approach a situation or know when to look for further advice. We also hope that the pointers to further information and useful addresses provided at the end of the book will come in handy.

Sometimes, it can be difficult to appoint someone to the role of treasurer for a charity, and many people are often daunted by what the role may involve or reluctant to take on the position as they feel they are not qualified. You don't need to be an accountant or finance professional, or even to have previous experience, to be appointed, but you do need to understand what the role involves and to work with the trustees in ensuring your charity meets its obligations. This handbook aims to guide you in those responsibilities in carrying out a worthwhile and important role.

List of abbreviations

ACAS	Advisory, Conciliation and Arbitration Service
AGM	annual general meeting
BACS	Bankers' Automated Clearing System
CAF	Charities Aid Foundation
CASC	community amateur sports club
CBS	community benefit society
CCEW	Charity Commission for England and Wales
CCNI	Charity Commission for Northern Ireland
Charities Act	unless stated otherwise, this means the Charities Act 2011 (applicable to England and Wales)
CIC	community interest company
CIO	charitable incorporated organisation
CSG	cost-sharing group
DBS	Disclosure and Barring Service (relates to work in England and Wales and in Northern Ireland)
EPS	Employer Payment Submission
FPS	Full Payment Submission
FR	Fundraising Regulator
FRS 102	Financial Reporting Standard number 102
GASDS	Gift Aid Small Donations Scheme
GDPR	General Data Protection Regulation
HMRC	His Majesty's Revenue and Customs
MTD	Making Tax Digital
NCSC	National Cyber Security Centre
NEST	National Employment Savings Trust
NFT	non-fungible token
NLW	National Living Wage
NMW	National Minimum Wage
OSCR	Office of the Scottish Charity Regulator
PAYE	Pay As You Earn
PVG	Protecting Vulnerable Groups (relates to regulated work in Scotland)
R&P	receipts and payments (when referring to R&P accounts and accounting)
RLW	real living wage
ROI	return on investment
RTI	real-time information (for PAYE)
SCIO	Scottish charitable incorporated organisation
SLA	service level agreement
SOAL	statement of assets and liabilities
SOFA	statement of financial activities

SORP	Statement of Recommended Practice on Accounting and Reporting by Charities (unless stated otherwise, 'SORP' will always be a reference to the Charities SORP – see chapter 14 for an explanation)
TPR	The Pensions Regulator
TUPE	Transfer of Undertakings (Protection of Employment) Regulations 2006
UTR	Unique Taxpayer Reference number
VAT	Value-Added Tax

Glossary terms

Terms which appear in **bold** in chapters 1–15 (when first used) are explained further in the glossary, starting on page 325.

References to endnotes

Superscript numbers within the text denote references to the legislation or further details – the corresponding notes appear on pages 311–312.

1 Charities in context

If you are taking on the role of a **treasurer** or **finance officer** in a **charity**, it is important to understand what a charity is and what having charitable status means, in particular in terms of the accounting and financial management responsibilities for your organisation and its **trustees**.

There are various types of organisation in the UK that are recognised as charities or as having charitable status, and they are often described as being part of the 'charity sector'. This chapter first describes what the charity sector is, examining and defining some other terms commonly used in the wider **third sector**.

As charity law is devolved in the UK, the chapter next provides an introduction to the **charity regulators** before considering what a charity is by examining **charitable purposes**, **public benefit** and the differing legal structures a charity can take. We discuss the forms of charitable status recognised across the UK (in England and Wales, Scotland and Northern Ireland) and introduce UK-wide issues, such as dual registration and taxation.

Some organisations operate in a similar way or deliver a similar service to charities but can never be a charity or obtain charitable status; the penultimate section of this chapter describes some of the more common organisations of this type. The chapter concludes with a useful reference table setting out the variety of organisations operating in and around the charity sector. Knowing where your charity sits, its legal form and the regulator it reports to is particularly important in your annual accounting and reporting process, as we will see in chapters 12–14. Understanding how your charity fits into the wider context of the charity sector can help to inform your role as a treasurer or finance officer.

What is the charity sector?

Organisations tend to fit into one of three sectors of the UK economy based on their ownership and purpose. The private sector includes commercial organisations whose owners are seeking to draw a profit. The public sector is owned by government and typically funded by taxes; example organisations are local authorities and national health service bodies. 'Third sector' is an umbrella term that covers a range of different organisations that do not belong to the public or private sectors. It is commonly referred to as the sector which encompasses voluntary and **not-for-profit** organisations, and those engaged in social enterprise. Organisations within the third sector are driven by social need rather than profit but are independent of government in terms of how they set their own priorities and direction. The charity sector fits within the third sector.

To appreciate the third sector, and in particular the context of the charity sector within it, it is helpful to understand four key terms: voluntary organisation, social enterprise, not-for-profit and relationship of trust. These terms describe key attributes of third sector organisations. Not all need apply and neither are they mutually exclusive, but they indicate the diverse range of entities that operate within the third sector. Understanding these terms will help us to consider what makes a charity and why the charity sector only forms part of the third sector.

Voluntary organisation

The third sector is often referred to as the voluntary sector as it includes organisations established voluntarily. Generally, these will be groups and organisations with a defined **constitution** and they will always have volunteers in positions of **governance** (this is covered further in chapter 2). There may be volunteers in other roles too, but these organisations may also employ staff. Voluntary organisations range from large national organisations, which tend to have charitable status, to small community groups, not necessarily with charitable status. This means the terms 'voluntary community organisation' and 'voluntary and community sector' are also used.

Many voluntary organisations do have charitable status, but many do not, either because they do not wish to become a charity or because they do not meet the precise requirements for charitable status. For example, a local sports club may not wish to have the extra layers of governance and requirements involved in being a charity in addition to the strict requirements of its national governing sports body membership. On the other hand, a group which operates as a club for the benefit of its own members, or to support one person or family, would not be considered to be providing a wide enough benefit to meet the criteria to be recognised as a charity. Whether or not an organisation has charitable status, the principle of unpaid governance is at the heart of the voluntary sector.

Social enterprise

'Social enterprise' is a term that, justifiably, can be used to describe many entities and activities within the third sector. As an entity, a social enterprise is a trading organisation, which, like a traditional business, seeks to make a profit. However, those profits are then reinvested or donated to bring about positive social change, such as by creating jobs and training opportunities, benefitting a local community, or meeting other social or environmental aims. A social enterprise does not have to be voluntarily governed; some have paid board members. A social enterprise is not a legal form in itself but can be constituted in a number of ways. Some examples include a **community interest company (CIC)**, a **co-operative society** or a **community benefit society (CBS)**. As will be described later in this chapter, CICs are able to allow investors to receive a modest return if required, and their directors can be paid. Co-operatives allow for profits to be distributed among members. For these reasons, CICs and co-operatives are not charities and are not directly considered in this book. Some CBSs can have charitable status; although this book does not consider CBSs in their entirety, much of its content will be relevant to any organisation with charitable status.

'Social enterprise' can also be used to describe an activity itself – one which produces income from **fees** and sales to put towards a social aim. Many charities do not rely on **donated income** (including **grant** funding); they may instead be funded by **contracts** or fees to deliver their service or carry out activities to fund their work, and all of this can be described as social enterprise. Sometimes the social enterprise activity consists of trading linked directly to the charity's aims, or it could be related to income from a non-charitable trading activity. Larger charities, in particular, may have a subsidiary company that undertakes non-charitable trading activities specifically to make a profit, creating income for the charity (for example, a **charity shop**).

A charity which describes itself as a social enterprise must still comply with charity law and produce charity accounts. To avoid confusion over the meaning of social enterprise, in this book, we use the terms '**primary-purpose trading**' and '**trading for fundraising purposes**' to describe trading activities undertaken directly by an organisation with charitable status. Refer to chapter 8 for more information on charity trading.

Not-for-profit

It is very common to hear the terms '**non-profit**' and 'not-for-profit' used in the third sector interchangeably; however, it is probably best to use the latter. 'Not-for-profit' describes an organisation or activity that is not intended to make a profit. This is distinct from the term 'non-profit', which can also describe businesses that are not making a profit. Being a not-for-profit organisation does not mean profits cannot be made. The definition of 'profit' is simply a financial gain: the difference between the amount received and the amount paid. Therefore, **fundraising** activities need to make a profit to be worthwhile. However, these profits are then reinvested back into a not-for-profit organisation to deliver its services and meet its aims. A not-for-profit organisation would not distribute profits to members, owners or shareholders. Not all organisations within the third sector are not-for-profit; for example, co-operatives may generate profits which are shared between their members.

For a charity, it is not common to use the term 'profits'. Where income exceeds expenditure in a given year, we tend to say a charity has made a **surplus** (or a **deficit** if the expenditure was more than the income). Often a charity will have years where it makes a surplus to be reinvested to cover those when it has a deficit. It is also good financial management to allow surpluses to build up sufficient **reserves** (see chapter 3) to allow the organisation to be sustainable. However, it is not appropriate for a charity to make surpluses indefinitely, as this would mean income earned for the charity is not being spent on the charitable purposes for which it has been established.

Relationship of trust

As discussed in the previous sections, organisations in the third sector are not profit-driven in the sense of benefitting owners and shareholders, and they are not under government direction. A third-sector organisation is primarily accountable to its own stakeholders – its members, beneficiaries, trustees and supporters. This independence creates a special relationship with **funders** and **donors**: a relationship of trust. For charities (and many other types of voluntary organisation), much of their income consists of money that is *given* to the organisation. Only a few people regularly make **donations** to commercial businesses or to the public sector, but people routinely give to charities without seeking anything in return other than assurance that their gifts will be used to advance the organisation's aims. This trust relationship can also apply elsewhere in the sector – for example, with gifts to political organisations or grants provided to CICs.

This relationship of trust is central to understanding voluntary sector finance and it is also the reason why much charity law has developed from trust law. For this reason, those with day-to-day control of the charity – for example, the management committee, church council or directors of a **charitable company** – are called 'trustees': they are entrusted with funds given by others to advance the charity's aims. The role of a charity trustee is discussed in chapter 2.

What is a charity?

We have seen that a charity can be described as a not-for-profit organisation, it may or may not carry out social enterprise activities, and it must be a voluntary organisation, with a group of trustees (generally unpaid – see page 27) responsible for the use of funds. However, charities can take on one of several available legal structures, and they are subject to different rules surrounding charitable status in the UK due to the differing legal **jurisdictions** in England and Wales, Scotland, and Northern Ireland. First we will look at the three regulators that oversee these jurisdictions, and then we will consider how an organisation meets the definition of a charity, and what legal structures are available.

The regulators

Charity law in the UK is devolved to three separate jurisdictions, and there are three charity regulators. The Charity Commission for England and Wales (CCEW) is responsible for charity regulation in England and Wales, in Scotland it is the Office of the Scottish Charity Regulator (OSCR) and in Northern Ireland it is the Charity Commission for Northern Ireland (CCNI). Each regulator has powers and duties under its respective legislation to deal with the regulation of charities. This includes registering and deregistering charities, maintaining a register of charities in their jurisdiction, investigating complaints, and providing guidance to trustees on managing their charity, including on accounting, reporting and external scrutiny. Ultimately, the regulators aim to support public confidence in charities and their work. They are independent of government control but do report to Parliament annually. The regulators have powers to take extensive action if they consider trustees are acting improperly, including to safeguard funds and wind up a charity if necessary.

All three regulators have a wealth of information and guidance available to assist charities and their trustees. It is all accessible online, and many applications can now be made online, such as to register a new charity. In addition, the charity registers and the documents available on them, such as **annual accounts** for some charities and a public record of key information for all, are available for the public to search – see the further reading section (page 313) for more details.

How charities are defined

The charitable status of an organisation depends on it meeting the definition of a 'charity' in law. In essence, in all three jurisdictions, charitable status is dependent on two tests:

1 The organisation must have exclusively charitable purposes.

2 The organisation's purposes must be for the public benefit.

Charitable purpose

A charitable purpose, often expressed in the charity's **governing document** as a charitable object, is the reason why an organisation has been established and the aim it wants to meet. The purpose (or purposes) must fall within those set out in the Charities Act 2011 and can be summarised as follows:

- the prevention and relief of poverty;
- the advancement of education;
- the advancement of religion;
- the advancement of health or the saving of lives;
- the advancement of citizenship or community development;
- the advancement of arts, heritage, culture or science;
- the advancement of amateur sport;
- the advancement of human rights, conflict resolution or reconciliation, or the promotion of religious or racial harmony, equality or diversity;
- the advancement of environmental protection or improvement;
- the relief of those in need by reason of youth, age, ill health, disability, financial hardship or another disadvantage;
- the advancement of animal welfare;
- the promotion of the efficiency of the armed forces or emergency services;
- any other purpose which may reasonably be regarded as analogous to the above (including purposes under existing charity law).[1]

This is a slightly paraphrased list applicable in England and Wales, but it indicates the wide range of work that can be carried out by a charitable organisation. There are some minor differences in both the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Act (Northern Ireland) 2008. Therefore, if your charity operates across the UK, it is important to ensure that you have considered your purposes in all jurisdictions you want to operate in. The constitution for your charity will list the purposes it is registered to carry out. Each of the three regulators also holds a public record of every **registered charity** which indicates, among other information, the purposes of the charity. Details on how to access the regulators' information are included in the further reading section (see page 313).

Public benefit

The purposes for which a charitable organisation is established must be for public benefit – that is, the purposes must make a positive difference to the public. For a purpose to be beneficial, it must be identifiable and capable of being proved. Any disbenefit (i.e. detriment or harm) from the purpose, whether to people, property or the environment, must not outweigh the benefit.

Some charities benefit the public in general (for example, an environmental charity concerned with climate change) and some benefit a wide range of people meeting specific criteria (for example, a UK-wide charity supporting people living with cancer), but some only benefit a relatively limited group (for example, a charity supporting children with autism in a particular town). In all cases there must be little or no private benefit. For example, except in very exceptional cases, the trustees must be unpaid (see page 27). A further factor to consider is that a charitable organisation should not impose any excessive condition which would prevent someone accessing a service or make any service unduly restrictive, such as by setting high fees. One example is private schools that are recognised as charities. Many of their service users (i.e. students' families) will pay high school fees and there may be strict criteria to access their services; however, if they are able to demonstrate they generate meaningful public benefit – for example, with defined bursary schemes open to a wider section of the public – then charity **recognition** is possible. In all three jurisdictions, guidance on public benefit is issued by the regulator in terms of what must be demonstrated and how it is assessed (again, see the further reading on page 313 for more details).

A charity's purposes and the public benefit it provides are not only considered when a charity is established; the charity must also continually demonstrate that it meets these two tests to maintain charitable status. This means trustees must ensure decisions they make regarding their charity's activities always have regard to the charity's purposes and always provide public benefit. They must confirm this in their **trustees' annual report**. These principles are further discussed in chapters 2 and 12.

Legal form

Charities can have one of a number of legal structures. Your governing document, or **constitution**, should make it clear which structure applies.

Charitable trust

This is the simplest structure. To create a **charitable trust**, someone (the **settlor**) simply needs to make an initial donation and, by means of a **trust deed**, define the purposes and appoint initial trustees. Many grant-making charities use this structure.

Charitable association

For a more democratic structure, with members electing a committee to act as trustees, the **charitable association** is the easiest model. Essentially, a group of people with common interests agree to associate themselves together and sign up to a constitution or set of rules that determines the criteria for membership and the procedures for electing the committee. A wide range of local community-based charities and service-providing organisations use this structure.

Both charitable trusts and charitable associations are **unincorporated**, which means that if something goes wrong and legal action is taken against the charity, the trustees could, in theory, be personally liable. Additionally, for an unincorporated organisation, any contracts will be entered into with the trustees rather than the organisation itself. Therefore, many charities, especially those employing staff, are constituted with a corporate status (i.e. one of the next two options).

Charitable company

A charitable company is created by establishing a not-for-profit company (a company limited by guarantee) under company law and then applying for the company to be registered as a charity. A charitable company has the advantage of being a legally separate **incorporated** entity. This means, for example, that if the charity wanted to purchase freehold property, the property could be registered in the name of the charity rather than the **holding trustees**. Also, if the charity entered into a contract that went wrong and the charity found itself being sued, the rules of limited **liability** would apply – i.e. the charity's own resources could be lost in a court action, but the trustees could not be sued personally for breach of contract. Although the protections of limited liability are not absolute, it is very rare for charity trustees acting in good faith to face legal action.

A charitable company has two completely separate registrations and must comply with, and report to, both regulators – as a company with Companies House and as a charity with the relevant charity regulator(s) (CCEW, OSCR and/or CCNI). Although this may not be too onerous if your charity has professional staff, if you are a smaller organisation – especially if you rely on a voluntary treasurer to comply with all regulations – you will probably welcome simpler regulation and reporting, while retaining the benefits of corporate status. This is where **charitable incorporated organisations (CIOs)** and **Scottish charitable incorporated organisations (SCIOs)** come in.

Charitable incorporated organisation or Scottish charitable incorporated organisation

These are relatively new legal forms which overcome most of the disadvantages of the first three forms. A CIO or SCIO is governed purely by charity law and is created simply by being registered with the relevant regulator, but it is an incorporated body with limited liability – thus giving most of the benefits of the charitable company without all the additional requirements of company law.

It became possible to register as a SCIO in Scotland with OSCR in 2011, and as a CIO in England and Wales with CCEW in 2013. CIOs should soon be possible in Northern Ireland through registration with CCNI, although at present the relevant sections of the Charities Act (Northern Ireland) 2008 are not yet in force. A high proportion of new charities are being formed as CIOs/SCIOs,[2] and a number of existing charities are converting to become CIOs or SCIOs. (For more on this legal form – and on comparison with other structures – see Gareth G. Morgan's book *Charitable Incorporated Organisations*, also published in this series (details can be found in the further reading, on page 313). This book also has much more on the legal definition of a charity and on non-charitable structures such as CICs and co-operatives.)

Even though the CIO form is proving very popular, and some existing charities are converting, there is no requirement to convert. Many charities use the existing structures, and these are likely to continue to be available for some time. There are also a few situations where the older structures may work better – for example, where a charity needs to borrow money which cannot be secured as a mortgage on property, some lenders may prefer to deal with a charitable company rather than a CIO because of the ability to register charges against a company at Companies House. Additionally, some people establishing new grant-making charities may prefer a charitable trust if they do not wish to reveal details of grants made in the charity's accounts. But these are quite specialised situations.

In the case of a CIO or an SCIO, the organisation only comes into being once it has been registered with the regulator, so it is a registered charity from the outset: it cannot exist without charitable status. This is unlike the other types, where organisations can exist with or without recognition as a charity.

Incorporation of existing charities

As mentioned, sometimes a charity which is established as a charitable trust or association wishes to convert to an incorporated charity – i.e. to become a CIO or SCIO, or a charitable company. This is sometimes described as 'incorporating the charity', but in law an unincorporated body cannot take on a new legal form. In practice, what happens is that a *new* charity is formed (a charitable company or a CIO) and then the *old* charity is wound up and all the **assets** are transferred to the new organisation.

This has important accounting implications: the old and new charities are separate organisations, with separate charity registration numbers, and in the year of the change two separate sets of published accounts may be needed unless the old organisation can be wound up on exactly the last day of its accounting year, or if **merger accounting** is applicable. In any situation, you should maintain completely separate **accounting records** for both charities while both are active on the charity register. You should also seek advice from an accountant where necessary.

Groups and subsidiaries

As a treasurer or finance officer, in addition to understanding the legal form of your charity, you must be clear on the boundaries of your organisation, in particular regarding control of all of the finances that are managed by the trustees. It is quite usual for charities to have several **funds** or projects within one charity (discussed further in chapter 3), and many charities have groups that run their own finances but that see themselves as part of the main charity. For example, a community association may run certain activities, such as an older people's support group, that are responsible for their own fund within the main charity. However, there could also be cases where an independent group uses a charity's premises to run its own activities on a regular basis. It is important to establish the boundary between what is and isn't part of your charity:

- If the group is *legally part of your charity*, its work is under the control of your charity's trustees and its finances must be included in your charity's published accounts.
- If the group is an *independent organisation simply using your charity's premises*, it must not attempt to use the same charity registration

number and should consider applying for its own registration status. Additionally, its finances must not be included in the published accounts of your charity.

Some charities may also have separately constituted subsidiary organisations that are under their direct control, for example **trading subsidiary** companies (see chapter 10). In this case, the subsidiary has to prepare its own accounts, but they may then need to be included ('consolidated') into the accounts of the main charity. If this applies to your charity, you may need help from an accountant or **independent examiner** with experience of **group accounts**. For more information, see pages 106 and 281.

Charitable status

We have seen that for an organisation to be a charity, it must meet the definition above, but it can be a constituted in a number of different legal forms. It follows that several factors are vital in determining charitable status: the governing document of the charity (its constitution, **articles of association**, trust deed or rules) and, in particular, the purposes of the organisation (as stated in that governing document) and where its beneficiaries and work will be located. Note that an organisation either is or is not a charity: unlike your legal form, it is not something you choose (see page 15 regarding non-charitable organisations).

Types of charitable status

There are currently six main forms of charitable status recognised in the UK.

Exempt charities (England and Wales)

Exempt status applies to a small number of bodies listed in Schedule 3 of the Charities Act 2011. They are mainly large national bodies whose charitable activities are regulated by a body other than CCEW (for example, universities and major museums), though charitable CBSs in England and Wales are also exempt charities at the time of writing. Much of the Charities Act 2011 does not apply to exempt charities, but the Charities Statement of Recommended Practice (**SORP**) (see chapter 14) is still the normal basis for presenting the accounts, unless a more specialised SORP applies.

Excepted charities (England and Wales)

Some charities are **excepted** from registration under section 30 of the Charities Act 2011, but they are still subject to other aspects of the Act, including the accounting rules. For example, charities (other than CIOs) whose annual income is £5,000 or less are excepted from registration. As a result of the changes that began from the Charities Act 2006, the category of excepted charities is being greatly reduced and it is anticipated that the majority of charities that were previously excepted (for example, places of worship, Scout and Guide groups, and armed forces charities) will in due course be required to register as charities in the normal way. However, at the time of writing no timescales have been confirmed for this: at present only formerly excepted charities with an income of more than £100,000 are required to register. Eventually some formerly exempt charities, such as CBSs, will also have to register.[3]

Registered charities in England and Wales

All other charities in England and Wales must be registered by CCEW and are given a registered charity number. This status must appear on all its charity literature, including websites, advertisements, fundraising literature, letterheads, invoices and receipts.

Scottish charities

Charities that operate in Scotland are registered by OSCR and given a Scottish charity number, beginning with 'SC'. It should be noted that charity registration is compulsory in Scotland – there are no exceptions. Even a small Scout group with £2,000 income per year would need to apply to register if it wanted to have charitable status. If a Scottish organisation chooses not to register, it is illegal for it to call itself a charity on any literature or documents. Any registered charity in Scotland must publicise its registered number on its charity literature and can obtain a specific logo from OSCR to add to its materials.

Northern Irish charities recognised by HMRC but not yet registered with CCNI

Until 2013, all decisions on charitable status in Northern Ireland were made by **His Majesty's Revenue and Customs (HMRC)**. At the time of writing, many charities in Northern Ireland remain in this category – though more and more are being called forward to be registered with CCNI (see below). Such organisations can describe themselves as 'recognised charities' (or, more accurately, 'recognised as a charity for tax purposes') but must not use the term 'registered charity'. However, organisations on this list are deemed (**deemed list**) to be charities and CCNI can still exercise authority in the event of concerns. These charities' status is thus similar to that of excepted charities in England and Wales.

Registered charities in Northern Ireland

Charities that operate in Northern Ireland are registered by CCNI and given a Northern Irish charity number, beginning with 'NIC'. At the time of writing, there is no lower limit for charity registration in Northern Ireland and no exceptions are made from registration for churches or other religious bodies. However, the Charities Act (Northern Ireland) 2022 allows for the possibility of some smaller charities in Northern Ireland being exempted from registration. In 2022 the Northern Ireland Minister for Communities announced an intention to make registration voluntary for charities with an expected annual income of under £20,000, although the rules that will apply to these exempt charities are not yet known (and may not be implemented for some time).[4] New charities formed in Northern Ireland since December 2013 must apply for registration with CCNI before they can seek tax recognition by HMRC. Northern Irish charities that were recognised by HMRC before then are required to register with CCNI when called forward to do so. As in the other jurisdictions, the charity's registration number should appear on its literature.

Applying for charitable status

It is vital to appreciate that charitable status is not an optional 'badge'. Even in England and Wales, it is compulsory under the Charities Act 2011 for the trustees of a charitable organisation to apply for registration unless it is clearly exempted or excepted (and they are committing a breach of duty if they fail to do so). It follows that, once all the legislation is fully in force, any voluntary organisation will need to apply for charitable recognition unless any one or more of the following is true:

- Any of its aims fall clearly outside the headings of charitable purposes.
- It clearly would not meet the test of public benefit.
- It operates purely in England and Wales and has an income of £5,000 or less.
- It is established in Scotland but it does not make any claim to be a charity.

Detailed information on applying for charitable status can be found on page 299.

It is illegal to claim to be a registered charity unless your organisation is actually registered with the appropriate regulator (CCEW, OSCR or CCNI). Records of registered charities can be accessed online at the relevant charity regulator's website.

UK-wide issues

Although charity registration and regulation are devolved to the individual jurisdictions of England and Wales, Scotland and Northern Ireland, there are two considerations that are UK-wide – those of dual regulation and tax law.

Dual regulation

If a charity's work spreads across more than one country of the UK, its location for charity law is normally determined by the wording of its governing document or, if this is not specific, by the location of the majority of the trustees.

UK-wide charities may be subject to **dual regulation**. This means that if a charity established under the law of England and Wales has regular activities (such as a base, staff or projects) in Scotland then, under the Charities and Trustee Investment (Scotland) Act 2005, it will need to be registered with OSCR *as well as* being registered with CCEW. This will result in the charity having two charity numbers. If this applies, the charity must account to OSCR as well as to CCEW. Its accounts must then comply with the Scottish charity accounting rules as well as the rules for England and Wales. In most respects the Scottish rules are tighter.

If your charity simply fundraises in Scotland (for example, if you have members or supporters in Scotland but do not have any regular use of premises in Scotland), registration with OSCR is not required, but all your literature must make clear the country where you are established. For example, if you are making use of this rule, rather than just putting 'Registered Charity number xxxxxx' on your literature, take care to put 'Registered Charity in England and Wales number xxxxxx'.

Note that there is no converse requirement: charities established under Scottish law and registered with OSCR do not have to register with CCEW in order to operate in England or Wales.

The rules are slightly lighter in Northern Ireland – an external charity operating in Northern Ireland does not have to be registered on the main CCNI register but instead on a simpler register known as the **Section 167 Register**. At the time of writing this is not yet in force, and it is likely that the details of the legislation will be amended before the register is implemented, but affected charities can complete an online expression of intent to be entered onto the Section 167 Register (at www.charitycommissionni.org.uk/manage-your-charity/register-your-charity/combined-list-and-expression-of-intent-form).

Eventually, a UK-wide charity formed under English law will need to be registered with CCEW and with OSCR, and appear on the Section 167 Register with CCNI – and will have to make returns to all three regulators.

HMRC and taxes

In terms of tax law, all UK charities have essentially the same tax concessions, as tax law is for most purposes determined UK-wide. There are some minor differences, such as the replacement of Stamp Duty Land Tax (commonly known as 'stamp duty') with the Land and Buildings Transaction Tax in Scotland. However, even under this tax, the charity exemptions extend to charities established outside Scotland.

There are some possible complications because of differences between tax law and charity law. Charitable status for UK tax purposes is determined by the English definition of a charity and hence it is possible in theory that a Scottish charity could be registered with OSCR but fall outside the tax definition of a charity. Since 2010 there has also been a tax law requirement for charities to be managed by 'fit and proper persons' (a person is deemed to pass this test if they do not have any convictions for dishonesty, or involvement in tax fraud – see also chapter 2 about disqualification of trustees). But the definitions across the UK are so close (and, if anything, the Scottish and Northern Irish definitions are slightly tighter than those in England and Wales) that, in practice, there is little risk of a well-run charity anywhere in the UK failing to meet the tax definition of a charity.

It is important to note that an organisation will not qualify for charity tax concessions unless the charitable status is clearly established. There is no halfway house on this question – a non-charitable voluntary organisation is treated as a business for tax purposes. It is important that you ensure your charity is registered with HMRC as a charity, especially if you want to reclaim tax on Gift Aid donations or any other tax reliefs specific to charities. Taxes are covered in more detail in chapters 9 and 10.

What is not a charity?

There are some voluntary organisations that could never be charities, as their aims or ownership preclude them from meeting the charity test; however, they still form a vital role in the third sector. Examples of common organisations that would be prevented from achieving charitable status are those whose aims are deemed in law to be primarily political or linked to self-interest. This would include, for example, political parties or campaigning organisations whose main aim is to achieve a change in the law, or trade unions working for the benefit of their own members. Where an organisation does carry out political campaigning, but also has activities that are charitable in nature, it may be more suitable to split the organisation so that the charitable activities are managed under a charity and the political campaigning under a separate body.

Organisations which are deemed not to offer sufficient public benefit are also unlikely to achieve charitable status, even if they are not-for-profits. One example is a tenants' group working purely with the tenants in one block of flats or a club whose facilities are only available to its members (unless the membership rules make it easy for anyone to join).

Additionally, organisations constituted as CICs or co-operative societies would not gain charitable status. A CIC is a company which has social aims. It exists to benefit the community rather than private shareholders. It must be registered at Companies House and with the Regulator of Community Interest Companies. It is subject to company law and corporation tax just like a regular company. This type of organisation is intended to be flexible and easy to establish, and is specifically designed for social enterprise. It does not need the trustee governance of a charity, nor some of the regulation, and the directors can be paid. However, there are safeguards, such as an **asset lock**, which allows investors to receive a modest return but ensures that most profits are retained for the social aims, and requirements around transparency in reporting, to ensure the CIC continues to benefit the community.

Co-operatives are people-centred enterprises, jointly owned and democratically controlled by the members. They are registered with the Financial Conduct Authority. Their main purpose is to provide services to their members rather than the wider community, even though their aims may be to benefit the community. Profits are often distributed to their members, and this, along with their members being the beneficiaries rather than the public, means they cannot have charitable status.

An exception to not being able to obtain charitable status is made for CBSs. These are found throughout the UK and are regulated through the Financial Conduct Authority under the Co-operative and Community Benefit Societies Act 2014. A CBS can, but does not have to, have charitable status. In England and Wales, a charitable CBS could gain recognition as a charity by HMRC but it would be an exempt charity (see page 11). In Scotland and Northern Ireland, a CBS wishing to become charitable would have to be registered with OSCR or CCNI respectively. This book does not cover the specific accounting requirements or external scrutiny requirements for CBSs (charitable or otherwise).

Some organisations in the third sector

To illustrate the variety of organisation types within the third sector, table 1.1 provides a summary of some of the options available. For each example, it specifies whether or not the organisation may have charity status, the governing document and the general name the governing body is known by.

Table 1.1 Example organisation types in the third sector

Organisation	Charitable status	Governing document	Governing body
Charitable trust	Charity	Trust deed (or a will, or a scheme created by CCEW or CCNI)	Trustees
Charitable association	Charity	Constitution	Management committee
Charitable company (company limited by guarantee)	Charity	Articles of association	Directors or board
CIO or SCIO	Charity	Constitution	Trustees
Charities established by Royal Charter (e.g. Scouts, Guides and some professional bodies)	Charity	Charter	Council
Charities established by Act of Parliament (e.g. most Church of England bodies)	Charity	Act of Parliament (or regulations made under the Act)	Various
CBS	Can be a charity	Rules	Committee
CIC	Never a charity	Articles of association	Board of directors
Co-operatives	Never a charity	Rules	Committee or members

Understanding the make-up of the charity sector, the regulators, the attributes that make an organisation charitable and the legal forms a charity can take will help to inform the role of the treasurer or finance officer. If you have taken on either role, it is crucial to know the legal status of your organisation and to which regulator you must report. Although many aspects of managing a charity's finances are the same regardless of the type of charity, or where it is registered, there are some differences in accounting and reporting which you should be aware of. These are explained throughout the rest of this book.

2 Governance and finance

Governance can be described as the system or processes by which a **charity** is directed and controlled. Good governance is essential because of the relationship of trust that exists in charities; if you donate to a charity, you are entrusting those in charge of the charity to use your **donation** in the way you intended. Charity **trustees** – those involved in the general control and management of a charity – are therefore responsible for implementing good governance.

Understanding the role and responsibility of a trustee and what constitutes good governance is important whether you are a **treasurer** or **finance officer** as it underpins the work you will carry out. This chapter first considers the trustee role more widely, including who can and can't be a trustee, and what their duties are in governing a charity. It introduces the concept of **collective responsibility** and discusses the issues of **conflict of interest** and trustee benefits as aspects of good governance.

The chapter then looks more closely at the roles of the treasurer and finance officer and how managing the finances effectively is an important part of governance. It should be noted that although treasurers and finance officers may be involved in similar work, there is a critical distinction between the two roles. 'Treasurer' is the term usually used to describe a particular trustee role dealing with the finances of a charity. This is usually an unpaid voluntary role. In contrast, the term 'finance officer' refers to any person employed or appointed by a charity's trustees to manage its day-to-day finances – for example, a bookkeeper or finance manager. The finance officer is generally a paid position, but may be carried out on a voluntary basis, and this person will report the finances back to the trustees. The responsibilities of a treasurer and finance officer and the interactions between them are explained in this chapter.

Who can be a trustee?

You may be a trustee without specifically being called by this term. You may be a member of your charity's management committee or a director on a board (in the case of a **charitable company**), or have a distinct name, such as the treasurer. However, if you are involved in the general control of the charity as a voting member of the board or committee that takes the key decisions, you will be a trustee.

Your charity's **governing document** should set out requirements for trustees, such as how many there should be, how they are appointed, their powers and their duties. In all three **jurisdiction**s in the UK, charity legislation sets out trustee requirements, and the **charity regulators** (CCEW, OSCR and CCNI) provide guidance on good governance (see the further reading, on page 313).

It is important to ensure you are allowed to be a trustee, otherwise any actions or decisions taken in managing your charity may be invalid. There are some restrictions on who can be a trustee. The minimum age to be a trustee of a charitable company is 16, in line with company law. This age also applies for **CIOs** in England and Wales and in Northern Ireland, but it is 18 for **unincorporated** organisations and trusts (see chapter 1 for explanations of the different legal structures for charities). In Scotland, there is no minimum age for trustees of unincorporated charities; however, to enter into **contracts**, you must be 16. Therefore, it may not be practical to have trustees under the age of 16. There may be some conditions specific to your charity in its governing document regarding eligibility of trustees and conditions for appointment. For example, some charities require a proportion of their trustees to be from their beneficiaries or user groups, or to have relevant lived experience. In some cases, especially for charities working with children and vulnerable adults, there may be requirements for the trustees to undertake disclosure checks.

Disqualification from being a trustee

Charity legislation in all three jurisdictions sets out who is disqualified from acting as a trustee.[5] This includes anyone who:

- has previously been disqualified by any of the three regulators;
- is disqualified from being a company director;
- has an unspent conviction for certain offences, such as those involving dishonesty, deception, money laundering or terrorism;
- is an undischarged bankrupt (someone in ongoing bankruptcy who is not yet free of debts).

As well as ensuring you are not disqualified from being a trustee, you are expected to make reasonably certain no other trustee at your charity is disqualified. It is, therefore, good practice to ensure all trustees sign declarations to this effect, and to conduct checks where necessary.

These checks could include searching the Individual Insolvency Register for England and Wales, using the Insolvency Service website (www.gov.uk/government/organisations/insolvency-service), and the register of disqualified directors maintained by Companies House, available on its website (https://find-and-update.company-information.service.gov.uk/register-of-disqualifications/A). For Scotland, see roi.aib.gov.uk for the Register of Insolvencies, and for Northern Ireland, see www.economy-ni.gov.uk/services/individual-voluntary-arrangement-register.
There are also registers of all persons who have been removed as a charity trustee held by each of the regulators. If you are concerned that you, or another trustee, meet any of these criteria, the regulators do have comprehensive guidance available on their websites and welcome enquiries.

Duties of a trustee

Taking on the role of a treasurer, or a trustee in general, brings with it significant responsibility. As a trustee, you must comply with any specific provisions set out in your charity's governing document and ensure you follow relevant charity legislation. In particular, you must ensure your charity is operating in line with the purposes it is set up for and that it provides **public benefit**. All trustees (especially treasurers), and finance officers too, should be aware that spending a charity's funds on activities that do not further its purposes can be a serious offence. It is recommended that all trustees receive an induction on their appointment to the role to set out the purposes and activities of the charity. A good induction might introduce the trustees to key staff and volunteers, and also review past financial performance, current funding streams and any future plans.

As a treasurer, or trustee in general, you are expected to always act in the best interests of your charity, using reasonable care and skill to manage the charity's resources responsibly. How this is achieved may differ between charities, but this legal duty should always influence your decision-making as a trustee. What does this mean in practice?

Acting in the best interests of your charity means making balanced and informed decisions that will enable the charity to carry out its purposes for its beneficiaries both present and future. Considering the longer-term outlook is necessary for charities whose purposes meet an ongoing need. Could a decision taken now **risk** the charity's funds or reputation in the future? However, keep in mind that it is not always responsible to put the needs of future beneficiaries before those you are currently supporting. Acting in the best interests of your charity often also involves managing conflicts of interest or loyalty – no decision should serve the personal interests of trustees or provide them any benefit. When making a decision, trustees must be able to demonstrate that they have acted within their powers and in good faith, considered all relevant factors and taken a collective decision. The concepts of collective responsibility and conflicts of interest and loyalty are discussed in more detail in the next two sections of this chapter.

Acting with reasonable care and skill means making use of your own skills and experience and taking professional advice when required. In practice, this means ensuring you devote enough time in preparing for and attending meetings, and using your knowledge and experience to make decisions in the interests of your charity. For you as a treasurer, this may involve preparing financial updates to be sent to your fellow trustees in advance of meetings or considering the financial implications of a particular decision.

Often, trustee boards may incorporate a range of skills, but sometimes it is necessary to seek external advice, such as when dealing with human resources, health and safety, or legal or accountancy issues. Even treasurers should not be expected to know everything about charity finance. For example, it would be better to seek the advice of an accounting firm that deals with specialist charity tax if needed rather than make mistakes that could be costly to your finances or reputation. Acting with reasonable care and skill also means understanding the expectations of your position in the charity. Many charities have a trustees' code of conduct; this will set out what is required of trustees in taking on the role, making expectations clear. There should be ample opportunity to undertake ongoing training throughout your term of office, or even on specific aspects of your role, such as keeping up to date on changes to charity accounting legislation.

Managing your charity's resources responsibly means protecting **assets** and reputation, safeguarding beneficiaries and not exposing any of these to unnecessary risk. Such challenges can be either wide-ranging (such as an economic crash) or specific to individual charities (such as if a **funder** withdraws its support). It is therefore important that trustees assess the risks that their charity may face and implement appropriate internal controls and procedures to mitigate those risks (see chapter 5). As a treasurer, for example, you may be tasked with ensuring that your charity's finances are not put at risk. This could include controls over charity payments, ensuring funds are not invested in risky or inappropriate **investments**, and monitoring the financial position of the charity regularly.

Managing your charity's resources also means making decisions about the activities it carries out; you and your fellow trustees must make sure your charity has the resources available to deliver a particular project and that it does not over-commit regarding what it can achieve. This may mean that as a treasurer you need to produce financial **budgets** and plans to assist decision-making. A charity's resources are not only financial; they also consist of the skills and experience of the personnel involved. In many charities, the most significant resource is the staff and volunteer team who carry out the work. The trustees are ultimately responsible for fair treatment of those staff and volunteers and for ensuring their charity complies with any relevant legislation, such as on health and safety, employment, data protection and equality. Many treasurers find their roles involve some of this work, particularly concerning payroll and setting pay rates. This is covered in more detail in chapter 11, but if this is an unfamiliar area, it may be wise to seek training and further advice.

There are other matters that trustees are also responsible for, some of which are set out in charity legislation. These tend to be reporting or administrative duties but nevertheless must be complied with. They include, for example, ensuring your charity's details are kept up to date with the relevant regulator – these can easily be checked on the appropriate online register (i.e. CCEW, OSCR or CCNI). If you wish to make certain changes to your charity – for example, changing its name, altering its purposes or changing the accounting reference date (the year end of the charity) – you must also check with the charity regulator if its permission is needed.

Trustees should be aware of their reporting duty to the regulators. There is a requirement to complete an **annual return** and file **annual accounts** (chapter 12), and this usually falls within the remit of the treasurer. Trustees are required to report to the regulator where there has been a **serious incident** (CCEW and CCNI have an option to make a serious incident report, while for OSCR, it is referred to as a notifiable event) – for example, an action or event that may have a significant impact on the charity. These can include fraud, theft, misuse of funds and mistreatment of vulnerable beneficiaries. In such cases, contacting the relevant regulator promptly to discuss any issues is generally the best course of action. The role of a regulator is to support public confidence in charities and their work. As part of that they try to prevent problems happening or escalating and to minimise any impact. Contacting the regulator when an issue first presents itself can mean you get relevant guidance that enables you to take action to prevent the issue becoming a more serious problem.

Administrative matters required by the regulators include ensuring that your charity name and registration number appear on all public documents, and that no other person or organisation is using your name or logo without your permission. If anyone makes a reasonable request for your charity's annual accounts or governing document, you must provide them. The law (in each jurisdiction) allows a small fee to be charged, if the charity wishes, to cover printing and posting costs. Often such requests will be made by someone who wants to learn more about your charity in order to become a member or **donor**, or perhaps someone undertaking some research. In many cases, charities now make their **annual report and accounts** available on their website to comply with any such requests in advance and for the purposes of being transparent and accountable to the public.

Collective responsibility

An important concept for good governance is **collective responsibility**. This means that all of the trustees must collectively take responsibility for the running of the charity and making decisions. As a treasurer, you may feel as though you are solely responsible for the finances of your charity. This is not the case. You are collectively responsible, equally with all the trustees. The same applies to the person taking on the role of the chair. Although they may take control of meetings and often be a figurehead or spokesperson for the charity, they are no more or less responsible than any of the other trustees for the charity's affairs. Being a trustee requires you to act in the best interests of your charity and this means exercising independent judgement and challenging proposals where necessary; no trustee should be able to unilaterally direct the decisions of their charity, nor should any trustee simply not involve themselves in making a decision, leaving it up to the others. If there are instances where trustees do not actively partake in decision-making on a regular basis, it may be that the chair, or another appropriate trustee, needs to take time to understand why this is occurring and take remedial action.

It is important that all trustees are aware of this collective responsibility. It does not mean that they all have to agree, or even that every trustee has to take an active part in each decision – for example, with delegation to subgroups. However, they all should be concerned with actions and decisions that have been taken by the trustees as a whole. Unless there is any conflict of interest or loyalty (as discussed in the next section), all trustees have a duty to participate in the decision-making process and to ensure this process follows the procedures in their charity's governing document. For example, has the decision been made in a formal meeting or, if not, do the trustees have the power to make the decision in that way? Were the necessary quorum and majority met for a decision to be passed? Were all trustees given sufficient information and the ability to participate in the discussion, so they could make their own independent decision? There will be occasions where not all trustees are available for a particular meeting or decision. If this applies to you, it is important to read the minutes taken and the rationale behind a particular decision and ensure you are comfortable with them, as even an absent trustee will share responsibility for the decision made.

As mentioned above, there may be occasions when subgroups are established to make decisions. For example, it is common for larger trustee groups to operate smaller subgroups to deal with finance, staffing or communications. In these instances, there should be clear terms of reference regarding how the subgroups are to be operated and the extent to which they can make decisions before going back to the full board. Often a subgroup will discuss matters in detail before bringing its findings to the main trustee group for the final decision-making.

Even when everyone is acting in the best interests of the charity, and after much discussion, it may be that not all trustees agree with a decision that is made. However, once a decision has been reached following the proper procedures, even if they are not in agreement, all trustees must abide by that decision. If you strongly disagree with a decision, you can ask for your disagreement and the reasons for it to be minuted. If your disagreement stems from a genuine concern that the trustees are not acting in the best interests of the charity, it may be cause for you to resign, and in some cases report your concern to the relevant charity regulator.

Conflicts of interest or loyalty

Individual trustees can bring with them a wealth of skills and knowledge and often connections (both professional and personal) that can benefit their charity. However, in some circumstances, these connections may also lead to **conflicts of interest**, resulting in inappropriate decisions that are not in the best interests of the charity. A conflict of interest or loyalty exists if there is any possibility that a trustee's personal or wider interests and loyalties could influence their decision-making. Even if there could be a perception by the public that there is a conflict of interest within the trustees, this could damage the charity's reputation or lead to a loss of trust.

Potential conflicts of interest arise when a trustee may receive a benefit, financial or otherwise, from a certain decision. This could be to them personally, or indirectly to a **connected person**. A connected person is set out in law as a close relative (e.g. spouse, civil partner, parent, grandparent, child or sibling) or business partner of a trustee. It also refers to businesses that a trustee (or relative) has ownership or control over. The Charities Act 2011 (section 350) includes additional interpretations to include two people living together but not married or in a civil partnership as connected persons. Other familial relationships (e.g. uncle or aunt) and friends are not specifically defined as connected, but trustees should be mindful of how such relationships may be perceived when making decisions where such a person could benefit. For example, a charity may want to use the services of a cleaning company owned by the brother of a trustee. This constitutes a financial benefit to a connected person of a trustee. The trustee concerned should remove themselves from all discussions and decisions surrounding the appointment, and good practice means adopting procurement procedures such as obtaining and comparing quotes.

Potential **conflicts of loyalty** apply where a trustee's duty to their charity may compete with a duty or loyalty to another organisation. In this instance, the trustee may not receive any benefit personally, or indirectly via a connected person, but their allegiance to another organisation may affect their decision-making. This could arise due to the trustee's employment, membership or trusteeship of another organisation or loyalty to a connected person. The trustee may also be influenced by the body appointing them, or their own personal, political or religious views. As discussed above, trustees must always make decisions in the best interests of their charity, so a conflict occurs if a trustee's other interest could, or could be seen to (by the general public), affect that decision.

Conflicts of loyalty may occur in various ways and not always be obvious – it may be helpful to consider some examples. Say that an individual is a trustee for another charity, and the two charities compete for the same service provision contract. The trustee will have no personal benefit, but the decision at either charity may be influenced by their knowledge of and loyalty to the other charity. In this case, it is probably in the best interests of both charities that the trustee abstains from the two decision-making processes.

Another example of conflict of loyalty is where a community charity has trustees appointed by the local churches, schools and local authorities. There may be occasions when a decision affects both the charity and the appointing body. This could prevent the appointed trustees putting the charity's interests first. Affected trustees should disclose the interest and refrain from participating in the discussion and decision-making process for that matter.

Some conflicts of loyalty will have low levels of risk attached. In these instances, it may be possible that, once the conflict has been declared, the trustee's involvement can continue as normal. An example of this would be if a trustee were also a member of a community centre, and their charity was deciding whether to continue operating from it. In this case, the trustee's connection to the community centre is through membership only and this membership is not likely to influence their approach to the decision. Any benefits to the community centre resulting from the charity's decision would affect all members in the same way, so the trustee would not benefit from the decision going any particular way.

A trustee has a legal obligation to act in the best interests of the charity; therefore, it is essential for trustees to declare any conflicts of interest or loyalty, and for procedures to be in place to manage those conflicts – ideally so they can be dealt with before they arise. In some cases, it may not be appropriate for someone to remain as a trustee where there is a strong conflict of interest. However, in other situations, having a well-written policy in place can mitigate the risk if procedures are followed. For example, this could include anyone with a conflict of interest removing themselves from discussions and votes where they could have a personal interest. The policy should also include procedures for identifying potential conflicts, such as completion of annual declarations where trustees are required to list their employers and other positions of trusteeship or membership. There can also be a recurring agenda point at the start of each trustee meeting asking those present to declare any potential interests in the matters to be discussed. As the treasurer or finance officer, it is useful for you to know about any such declarations from trustees as this will assist you in identifying any **transactions** that could pose conflicts or that will need to be highlighted in the trustees' annual report and accounts (chapters 12 to 14).

Providing benefits to trustees

In general, under all three legal jurisdictions, a trustee role is not renumerated. A central principle of charity law is that charity trustees must not seek a tangible benefit from their role. You may be reimbursed for reasonable expenses to cover travel to meetings or events carried out in your role as a trustee, and potentially also for costs such as childcare necessarily incurred for you to attend a trustee meeting (although this will depend on your charity's policy and, often, governing document).

There are some exceptions to this rule. A few charities have special governing instruments that allow certain trustees to be paid subject to very strict criteria. Also, in England and Wales, the Charities Act 2011 (as amended by the Charities Act 2022) allows a charity to pay a trustee for specific services outside their role as a trustee, or for providing goods to the charity (for example, if a rural charity needed to buy supplies and the only local shop was run by a trustee or their relative). However, these arrangements are subject to very strict criteria: CCEW guidance (CC11 – see details in the further reading, on page 313) must be followed carefully. In other one-off cases, a charity may be able to apply for individual approval from CCEW for a transaction with a trustee. Payment for goods is specific to England and Wales; there are no similar provisions currently in Scotland or Northern Ireland. The provisions for services are comparable across all three jurisdictions. But the exceptions are relatively rare and, excluding these cases, paying anything to a trustee other than reimbursement of expenses is a clear breach of trust. To help safeguard against abuses, any payments to trustees must normally be shown separately in your published accounts (see chapters 12–14).

It is not usual for an employee of a charity to also act as one of its trustees. This is because their position as a paid employee would implicitly cause a conflict in any decision-making with regard to the charity's affairs. There are some charities where this is allowed, usually by a specific provision in a governing document that has been approved by the relevant charity regulator – for example, it is common for a minister in a church to be in a paid role as well as being a trustee, and similar arrangements sometimes apply to the artistic director in large arts charities. But, where this is allowed, the trustee concerned must always leave the meeting for any discussion of their remuneration. On the other hand, where a charity has a **trading subsidiary**, it is common for an employee of the charity to be a director of that subsidiary.

There may be other situations where a trustee receives remuneration or other benefit from their charity. For example, a trustee might sell or loan assets to their charity (or buy or borrow charity assets). In all cases, you should check your charity's governing document to see whether such payments are allowable, refer to any policies your charity has in place, and seek guidance from the relevant charity regulator. As the treasurer or finance officer, you will also need to consider whether any resulting transactions require **disclosure** in the annual accounts.

Role of the treasurer or finance officer

If you are a treasurer, the duties required of all trustees have implications for your role, such as providing financial information for decision-making and being aware of any transactions involving trustees that may require further disclosure in the annual accounts. However, the main connection between governance and finance is the legal requirement, under all jurisdictions, for charities' **financial records** to be properly maintained and for annual accounts to be prepared from those records. This requirement applies regardless of size and registration status (see page 11). However, certain aspects differ depending on the size of your charity and the jurisdiction: the format of your accounts, whether or not they must be subject to an **independent examination** or **audit**, and whether they are required to be filed with the regulator. These points are covered in detail in chapters 12–15.

Although the overall financial responsibility for your charity rests with the trustees as a whole, for practical reasons, the tasks of administering the financial records and transactions – such as recording receipts, paying bills and salaries on a day-to-day basis, and organising regular reporting (annual and more often as needed) – tends to fall to someone taking on the role of treasurer. Sometimes the term 'honorary treasurer' is used to make it clear that it is a voluntary role. The treasurer will always be considered a trustee where they are involved in the general control and management of the charity. Some charities may choose not to have a designated treasurer to reinforce that all trustees are responsible for the finances, but this will probably only work where a finance officer is employed to manage and report all financial matters back to the trustees. In such situation, there will probably still need to be one trustee who takes the lead on finances, even if not called a treasurer.

Relationship between the treasurer and finance officer

If the trustees choose to employ the services of a finance officer to manage the day-to-day finances, the finance officer is not a trustee – they simply report to the trustees. In larger charities with many transactions, employing a finance officer will be a necessity rather than a choice. Treasurer and finance officer are therefore considered to be two distinct roles for the purposes of this book, although they will both be concerned with managing the finances of their charity.

The following list gives three major examples of how the roles of treasurer and finance officer are distinguished and, potentially, how they may interact. The treasurer's level of involvement varies, generally according to the size of the charity and whether or not it employs staff:

1 In many *small local charities*, the treasurer (voluntary trustee) manages all the **bookkeeping**, payment of salaries, liaison with the bank and similar tasks. They are personally responsible for producing the year-end accounts (or for arranging for this to be done by the **independent examiner**) and will often handle the majority of the correspondence on financial issues – for example, arranging insurance.
2 In *slightly larger charities*, a member of staff may be employed (often part time) to act as a bookkeeper, or there could be an administrator whose duties include bookkeeping. The usual arrangement is that the treasurer (voluntary trustee) determines the broad financial procedures and the categories of transaction to be used in the books, while the finance officer (who may be paid or voluntary but not a trustee) handles the detailed work. In this case, the day-to-day financial procedures are shared between the treasurer and finance officer; for example, the treasurer might indicate the type of management report required for the trustee meeting, but the finance officer might produce it.
3 In *medium-sized and larger charities*, it is impossible for a treasurer (voluntary trustee) to have any more than a broad overview of the financial arrangements. In such cases, the paid staff of the organisation are expected to manage the financial affairs and simply consult the trustees (including the treasurer) on major financial decisions. There will usually be a senior member of staff with the job title of finance officer or finance manager (in larger organisations, often finance director). In organisations with this model, the treasurer's role is less operational, as the finance officer will usually attend trustee meetings and present reports directly. The treasurer will meet with the finance officer from time to time to discuss financial policy, propose formal resolutions of a financial nature at trustee meetings, and liaise with the independent examiner or **auditors** on issues at trustee level. Usually in this model, treasurers have limited day-to-day involvement in operational financial procedures but have a crucial role in supporting their fellow trustees in effective financial governance, especially on strategic decisions.

The first model has the advantage of simplicity. However, as an organisation grows, it can become too time-consuming for some volunteers, and at the same time the organisation may be hindered because of the dependence on one person. For example, staff may have no financial information if all books are kept at the treasurer's home or on the treasurer's personal laptop, and there may be considerable delays in making payments or acknowledging receipts as a result.

However, once a paid finance officer is appointed, the relationship between this person and the treasurer is crucial: the finance officer needs the direction of the treasurer on financial procedures; equally, the treasurer needs information from the finance officer in order to report to the trustees. This has to be handled with sensitivity and respect for each other's roles, knowledge and commitments.

In the third model, the relationship of knowledge may be the other way round. Even a treasurer who is a finance professional is unlikely to have as much knowledge and experience of charity finance as a full-time charity finance officer and will not have the same level of detailed financial knowledge of the organisation. Often, in cases such as these, it will be the finance officer who needs to educate the treasurer on particular charity accounting issues or financial matters affecting the charity. However, this relationship can work well, especially if the treasurer is able to take the lead on difficult decisions that would perhaps make the finance officer unpopular, and the treasurer should certainly take the lead on decisions such as staff remuneration.

Attributes of a treasurer or finance officer

There is no particular qualification or experience needed to take on the role of treasurer. Often, charities believe they need, or want to have, a qualified accountant or someone with a financial background as their treasurer. This does have advantages – for example, expertise with accounts, budgets and financial controls may help the charity to quickly adopt good financial procedures. Such a person may also be able to explain complicated financial issues to their fellow trustees to provide a better understanding around decision-making. However, caution needs to be taken in this case so that the rest of the trustees do not simply leave all the financial governance to the treasurer, believing that as an accountant they must know best. Dependence on one person, and disengagement of the other trustees over the finances, can leave the charity compromised (as discussed on page 24). There may be a risk that financial decisions are unchallenged, and other trustees may not feel as though they can question the skills of an accountant. It is also worth noting that a finance background can be wide-ranging – it doesn't necessarily mean a person will have specific knowledge or a good understanding of charity finance.

Regardless of whether you are a qualified accountant or have a finance background, the main skills required to be a treasurer are honesty and integrity, as you are managing funds given under a relationship of trust. You will also need to be numerate – to enjoy working with numbers and be able to understand them and explain them to others. It is useful to have skills in working with finance software and spreadsheets. You must also, of course, have sufficient time to dedicate to the role so that you are available when needed. Finally, you should be willing to be challenged on the numbers you present and be able to answer questions or know where to find the answers.

As the treasurer, especially if you have a finance background, you may be expected to have knowledge of all aspects of finance, including taxes, financial controls and even employing people. This often isn't the case, especially as these areas can be complex and often charity specific. Further chapters in this book introduce financial controls (chapter 5), taxes (chapter 9) and accounting requirements specific to charities (chapters 12–14); however, as previously mentioned, you should seek advice wherever needed. Do not just assume that if your charity is small, it will be okay if something is not quite right. For example, if your charity's trustees do not ensure that **fund accounting** is adopted correctly or that they meet the requirements around the minimum wage, they will be in breach of trust or employment law. One avenue of advice may be your independent examiner (or **auditors**), especially if they specialise in charity accounting. Their knowledge and experience with similar clients likely means they will be ideally placed to answer your questions or point you in the right direction.

If you are employed by a charity as a finance officer, in addition to the attributes of honesty and integrity, it will be expected that you bring some financial knowledge, and perhaps qualifications, to the role. In smaller charities, it may be sufficient to demonstrate that you have the relevant bookkeeping skills, even if your experience is not in a charity. However, you will need to be able to adapt to working with fund accounting (see chapter 3). In slightly larger charities, the trustees may want to employ someone with relevant experience who has more knowledge of charity finances and can prepare and communicate financial reports to the trustees. Where resources allow, some trustees may wish to employ a qualified accountant for the role.

Communicating the finances

It is vital that the treasurer and/or finance officer understand that their role is not to make the decisions on what can and can't be afforded, nor should that be enforced upon them by other trustees wishing to leave the finances to someone else. It is the role of the treasurer and/or finance officer to communicate their charity's financial position to the trustees as a whole so that they, collectively, are in the position to make informed decisions based on the charity's financial position.

This can often be a complex skill to master, especially for treasurers who work, or have worked, in a financial role. It is often difficult to appreciate that other trustees may not use figures regularly, that numbers may frighten them or that they may simply switch off when the financial discussions start. Often this is not because they are not interested; it may instead be a way to hide the fact that they are not comfortable with numbers or feel they don't understand them. A good treasurer will appreciate that there is a variety of skillsets on a trustee board, and equally varying levels of understanding of finances. It is therefore important to make your finance updates accessible to all the trustees. In general, this means you should avoid simply presenting a page of numbers and be careful about using technical accounting terms and jargon. It is not advisable to inundate the (other) trustees with lots of facts, but equally do not just present the bare minimum, assuming they won't want to hear more.

It is helpful to prepare a finance report that is clearly set out and easy to read, not just a spreadsheet. Include narrative, especially about key points to be brought to the attention of the (other) trustees, and add charts to visually communicate the position and draw out the information that is relevant to any required decision-making. Make sure the finance report is sent out in advance of the meeting to give the (other) trustees time to digest it and perhaps submit questions in advance – some trustees may feel uncomfortable asking a question in the meeting. If possible, the finance report should be one of the first agenda items; leaving it to the end may mean it's rushed, concentration may have waned and, generally, it is useful to know the organisation's financial position before decisions are made. The finances should be discussed at every meeting, or at least quarterly, and should be up to date. If there is a significant gap between meetings, the treasurer and/or finance officer could consider sending out smaller updates, especially if there are changes or concerns to highlight.

Further chapters of this book explore in more detail the various aspects a treasurer or finance officer may need to be aware of for their role. These include internal controls (chapter 5), financial management (chapter 6), taxes and reliefs (chapter 9), employing staff (chapter 11) and annual reporting (chapters 12–14). For a more in-depth understanding of the concepts and issues surrounding trusteeship in general highlighted in this chapter, see *The Charity Trustee's Handbook*, also in this series (details can be found in the further reading, on page 313).

3 Funds and reserves

When you are appointed to a **charity** as a **treasurer** or employed as a **finance officer**, one of the first things to understand is **fund accounting**. Having to manage different **fund**s may be new to you as a treasurer, even with an accounting background, as it tends to be a concept specific to charities.

Although all funds received by a charity must be spent in ways that support its **charitable purposes**, sometimes funds are given for a more particular reason. Therefore, it is important that **accounting records** can distinguish between these different funds. The first part of this chapter examines what a **fund** is and why accounting for funds makes charity accounting very different from commercial accounting. It sets out the different types of fund a charity can hold and offers some practical advice on how to approach fund accounting.

Some of a charity's funds will form part of its **reserves**. Reserves can be defined as the resources that are freely available to be spent – at the **trustees**' discretion and in line with the charitable purposes. Reserves represent the money that is held aside to protect a charity against drops in income, to meet some unexpected expenditure or to allow the charity to take advantage of new opportunities. This means reserves are critically important and they are often perceived as one of the most useful figures in a charity's **annual accounts**, particularly for **funders** looking to make decisions on funding applications. However, a reserves figure on its own is not very helpful if it is not given context, such as how it is calculated and what it means for the future. A **reserves policy** is a good starting point for understanding how to calculate and communicate your charity's reserves. The second part of this chapter considers how to determine and evaluate reserves and what should be included in a reserves policy.

Charitable funds

The best way to describe a **fund** is as a pot of money, with resources coming in and expenses being paid out. Sometimes a fund is for general use, and other times it is ring-fenced for something specific. For most business organisations, there is just one fund – usually called the profit and loss account. When a business receives income, for example through sales of goods, all income will go into the profit and loss account. That income is used to pay for the costs of running the business, such as salaries, costs of producing goods and general running expenses. The difference between the income and expenses forms the profit or loss of the business as a whole. Where businesses are more complex – for example, if they have very varied products to sell – they often choose to use cost centres to divide their income and expenditure according to particular products to measure their profitability. This is for internal management purposes only and, at the end of the year, the results from all costs centres are combined in the overall profit and loss account for the business.

In contrast, charities often find themselves with more than one fund to manage. Most charities start with one fund, usually called the **general fund**, into which **donated income** (including **grants**) is received and expenses are paid. The results of these **transactions** form an account, the same as for a business. However, instead of a profit and loss account, this is called an **income and expenditure account** or **receipts and payments (R&P) account** (for charities able to use **R&P accounting**; eligibility is covered in chapter 12).

The general fund can be used for any income or expenditure that furthers the charitable purposes, but it is likely that, at some point, your charity will raise money or apply for a grant for a distinct project or piece of work. Where grants or **donations** are received specifically for a certain project, the relationship of trust (as explained on page 4) means that the trustees must ensure the money is only spent on the purposes for which it was given. Therefore, detailed **bookkeeping** is needed to identify specific expenditure relating to the project and confirm that funding is actually spent on the purposes intended. It would be extremely difficult to track this in the general fund, so a separate fund should be used.

Many charities, even small straightforward local organisations, often find themselves managing multiple funds and larger organisations could have hundreds of funds. Fund accounting recognises two primary classes of fund: **unrestricted funds**, which can be spent for any of the charitable purposes of the charity, and **restricted funds**, which under trust law can only be used for the specific purpose for which they were given. As a treasurer or finance officer, it is therefore necessary for you to understand what constitutes the different types of fund that you may encounter and how best to manage them.

Restricted funds

Restricted funds arise where there is some external condition on how a fund can be used. Strictly speaking, the term is **restricted income fund** (also known as a 'special trust' in charity law in England and Wales); however, these are commonly referred to as ‘restricted funds’. The condition can arise in two ways: from the **donor** when they gift money to the charity or by the way in which the charity asked for the money in the first place. As the treasurer or finance officer, you must be clear about the intention of these conditions so that the trustees do not inadvertently find themselves in breach of trust. It may be helpful to consider some examples.

Example 1

Your youth club charity, which helps young people in the local community, receives a donation from an individual with an accompanying letter saying they want to make a donation to carry on the work of your charity. In this instance, the donor has made no specific condition and so no restricted fund is needed. However, if the donor had said they wanted the charity to use their donation to buy musical instruments for the young members to use while at the youth club, there would clearly have been a condition attached to the donation. In this case, you would need to set up a separate restricted fund in your accounting records to contain the donation. It could then only be used for the purchase of musical instruments. The donor might not want to see evidence that the charity had only bought musical instruments with their money, but your charity accounts would need to reflect the condition to comply with charity law.

Example 2

The charity where you volunteer as treasurer employs several support workers to deliver activities for the health and well-being of older members of your community. To recruit an additional employee post to support members with dementia, the charity applies to a major grant funder. The grant is successful and the paperwork states that the funding must be used for a ‘dementia support worker’. The funder-imposed condition means that this grant is restricted funding, and a separate fund must be set up in your charity’s accounting records. The salary for the dementia support worker can be paid out of this fund, and it may also be possible, depending on what you asked for in the application, to use this fund to provide equipment, training and supervision for the dementia support worker. It is likely that the funder will want a report to be submitted at the end of the grant period, which, along with a narrative report on the achievements of the post, will require details of how the money has been spent. Recording the transactions in a restricted fund in your accounting records means you will easily be able to complete this financial report.

In both examples, the conditions – and therefore the need (or not) for separate restricted funds – were specified by the donor or funder. A restricted fund also arises if a charity decides to raise money for something in particular – often through what is called a fundraising appeal – as in the next example.

Example 3

The community centre your charity runs wants to add an adventure playground to its garden. This project is likely to need a substantial amount of funding and you set up a fundraising appeal to reach your target. You have applied for a grant for community projects, asked for donations from local organisations and intend to carry out several fundraising events at the community centre over a period of time. In all cases, when you are approaching funders or donors, you are specifying that the funding will be used to build an adventure playground. In this case, all of the funding raised must be included in a restricted fund – named something like 'Adventure Playground Fund' (although a more specific fund may be needed for any grants or donations with more exacting requirements). You (as treasurer) and your fellow trustees must then ensure that all of this funding is used on costs for the adventure playground. If some of the funding was used to cover the charity's general running costs, or for other items in the community centre, then those who had given to the appeal (whether individuals or large grant-makers) might, rightly, be concerned; they could ask for their money back, and the trustees would be guilty of a breach of trust.

When wording fundraising appeals, you should take care not to add an unduly restrictive condition. For example, if your charity is raising money to buy a freehold property to run its activities, it is unwise to mention a specific property in the fundraising appeal literature until the purchase is formally agreed. If that property purchase failed, your charity would have a restricted fund that it could not use. It is much better to make the appeal more general to give some flexibility, such as to buy any property that fits the needs of the charity.

Managing and budgeting fundraising appeals requires careful consideration – if you receive more income than needed, then it is not simply the case that the excess funding can be used for your charity's other activities. For example, where a restricted grant has provided more funds than needed, the **surplus** will likely need to be repaid to the funder.

In the case of a restricted fund that came entirely from one funder or donor, always contact the funder to agree what should be done: while the funder has the right to ask for the grant to be repaid, many funders will be willing to change the terms of the restriction – if so, there is no need to involve your **charity regulator(s)**.

In the case of a fundraising appeal involving many donors where the funds cannot be spent as originally intended, and where the wording of the appeal did not contain some provision for alternative use of surplus funds, the charity must normally contact the individual donors and the regulator. In the past this was very complex, including requirements for public advertisements to make contact with donors.

However, the changes brought about by the Charities Act 2022 have made this framework much simpler for charities in England and Wales. The following steps are involved.[6]

1 First of all, if any donor specifically asked for their donation to be returned if it could not be spent on the original purpose, you must do so (but it is very rare for donors to make such requests except with very large gifts).

2 If the total value of the remaining donations from the appeal is no more than £1,000, the trustees can simply pass a resolution to apply them to a new purpose (within the overall purposes of the charity – for example, you could decide to treat them as unrestricted donations). There is no need to seek consent from CCEW, but the trustees' decision must be properly minuted.

3 Where the funds from the failed appeal are more than £1,000, the trustees can still resolve that they should be applied to new charitable purposes, but in this case the resolution will only take effect with consent from CCEW. In order to give consent, CCEW will need you to provide a realistic plan to contact identified donors who gave more than £120 to the appeal and provide them with the option of requesting their money back by a reasonable deadline. This could be done by contacting them individually or perhaps by means of a notice in a magazine or newsletter (printed or electronic) if you are confident that it will reach a high proportion of your supporters. But you do not have to contact donors who only gave through cash collections, lotteries or competitions, or donors whose total contribution to the specific appeal was £120 or less in any one of your charity's financial years. You must take reasonable steps to add up separate gifts from the same donor (so, someone who gave £50 per quarter would need to be contacted, but not someone who gave £10 per month).

4 Typically you will then ask CCEW for consent to apply all the funds to the specified new purposes after a certain time except for donations over £120 where the donor asks for their gift back before the deadline specified. (You could, of course, offer to return gifts of £120 or below if you think it would promote goodwill among your supporters, but the law only insists on communications with donors above this level.)

> Such requests for consent should be made using the CCEW General Enquiries online form (https://forms.charitycommission.gov.uk/enquiry-form). Be sure to give full details of the trustees' resolution, the steps you propose to take and the timescale you wish to follow.

There is no direct equivalent to these powers for charities in Scotland and Northern Ireland. If such circumstances arise, the trustees should certainly contact OSCR or CCNI (as appropriate) for advice. However, it is much simpler to word fundraising appeals in the first place in a way that allows flexibility than to end up seeking consent from charity regulators at a later stage.

It is best to avoid making Gift Aid claims (see chapter 10) until such issues are resolved. If you have claimed a Gift Aid tax refund on any donation which is subsequently returned, your next claim must be adjusted accordingly.

Unrestricted funds

Any funding that is not given to a charity with specific conditions attached will be an unrestricted fund. Charities often call this their general fund. Unrestricted funds can be spent at the discretion of the trustees to further any of the charity's purposes. They may be used to meet any shortfall in restricted funding where the costs of the project outweigh the specific funding received. Unrestricted funds are therefore more flexible and, potentially, more useful to your charity than restricted funds, and this should be considered when fundraising. If your charity is carrying out general fundraising, ensure that the message behind the fundraising reflects that and doesn't unintentionally add any restriction. For example, instead of including strong statements such as '£10 buys an activity pack for a child', soften it with '£10 could buy an activity pack for a child'. The first statement suggests to the donor that if they give £10 it will be used for the activity pack (adding restriction), whereas the second statement suggests what the £10 donation could be used for (allowing more flexibility and no restriction).

From the unrestricted funds, trustees are able to set aside some funds for a particular future project or commitment – this creates a **designated fund**.

Designated funds

To understand designated funds, it may be helpful to think on a personal finance level, for example putting money aside to pay for a holiday or big event – such as a 'holiday fund'. You have made a decision to designate some of your money to pay for a holiday. However, if you needed to use that money for something more urgent, you could make that choice and spend it as needed. The same is the case for the designated funds of a charity; the trustees have earmarked the funds for something in particular but can use them for something else more urgent if needed. Designated funds form part of the unrestricted funds of a charity as the designation made by the trustees is for management or financial planning purposes and does not form a legal requirement in the way that restricted funds do.

In your role as treasurer or finance officer, you may come across situations where the trustees decide it will be useful to set aside some money as a designated fund. The reasons will vary depending on the nature of your charity and perhaps the trustees' plans for the future. A common example of designated funds for charities managing buildings is a 'repairs fund'. Every year, a transfer can be made into it from the general fund, providing some funds to cover (or put towards) the cost of any repairs when they happen. This can prevent the cost of repairs becoming a challenge (for example, if the charity tried to cover them out of its regular annual income). If your charity employs staff, the trustees may find it useful to earmark some funds for staff training, building a designated fund to ensure resources are available to train and develop staff.

Designated funds do not need to be retained, or added to, year on year. For example, if your charity finds itself with a surplus of unrestricted funds at the end of the financial year but has plans to develop a new activity or project, or put on a special event in the following year, it may be useful to consider a designated fund intended to be fully spent on that specific new initiative. However, a designated fund should have a specific purpose related to costs likely to be incurred at some point in the future. A designated fund with a title such as 'contingency fund' or 'general reserve' (or any similarly vague title) is not really a designation and should be queried by the charity's **independent examiner** or **auditor**.

Endowment funds

A restricted fund (or restricted income fund), as discussed previously, is expected to be spent within a reasonable period from its receipt to further your charity's aims. However, if funds are gifted to your charity to provide benefit for the longer term, there is a further type of restricted fund, known as an **endowment fund**. Endowment funds arise when someone gives money, usually a substantial amount, to a charity asking it to be invested. Often an endowment arises from a legacy where someone leaves a gift in their will to create a long-term resource, or **investment**, that could continue to make grants long after their death. In charities with endowment funds that are invested in stocks and shares, it is usual for an investment management company to manage those funds on the charity's behalf. However, an endowment fund can also comprise a property.

The dividends and interest from the invested endowment will then flow back to the charity, creating a continuous source of income. This income may be restricted, if the donor specified how it should be spent, or unrestricted, if the only condition was to further the charitable purposes of the charity. The value of the endowment itself will go up and down over time in line with the stock markets, changing the value of the restricted endowment fund.

Endowments are more usually found in grant-making charities, which may have held them for many years, using the income they provide to make grants. Charities aiming to raise significant amounts of money may also appeal specifically for an endowment fund – for example, to provide long-term running costs for specialist medical equipment.

Endowment funds are further divided into **permanent endowments** and **expendable endowments**. In a permanent endowment, the capital value of the fund cannot be spent at all (except by following special procedures in charity law, which generally need the consent of CCEW, OSCR or CCNI). In an expendable endowment, if the trustees specifically decide to do so, they can spend some of the capital held.

Whether an endowment should be classed as permanent or expendable will depend on how it was given to your charity. For example, if your charity received a legacy in a will which specified it was to be invested to provide income for grants, then it would be clear the legacy should be invested and not spent, forming a permanent endowment. However, in newer grant-making charities set up with an initial large gift, it is common to specify that the gift should be an expendable endowment. This allows much more flexibility for the trustees – on one hand, they are under no obligation to spend the gift quickly (so they can invest for the longer term) but, on the other, the option is there to spend some of the funds if the trustees want to make more grants than the income the endowment generates in a particular year. The caution here is that reducing the endowment's value may reduce the future returns that can be generated.

A charity may have a fundraising appeal to fund a capital item – such as a building or equipment. This may also result in a restricted fund. If the donations are for capital items which have a limited life – such as a minibus or office equipment for operational use – the fund will be considered spent when the items are fully depreciated. This would therefore be considered a restricted income fund. Any such item could not be sold and used to cover other costs, except to replace it with a similar item.

However, with **assets** that only have a life of a few years, some funders are happy that the terms of the restriction have been met as soon as the asset is purchased and they may not require the asset to remain restricted until it is fully depreciated. In that case, once the purchase is made, the value of the asset could be transferred to unrestricted funds (this would be shown in the accounts as an **inter-fund transfer** – see page 46). In theory, the charity could then sell the asset and use the proceeds for something else – but only if the funder was genuinely happy that the restriction ceased when the purchase was made.

If the asset were more permanent – for example, a freehold building to be used by the charity in perpetuity – the funds received (and subsequently invested in the building) would usually create a permanent endowment fund. The appeal would not necessarily need to state that the asset was to be held 'in perpetuity'. Any appeal seeking funds to purchase or to construct a permanent asset with the clear intention that it would be held indefinitely as a resource for the charity's operational work should normally be treated as an endowment fund, unless the charity has received clear professional advice to say otherwise.

These issues around allocating assets to the various types of fund can be complex. It may be helpful to discuss them with your auditor or independent examiner (see chapter 15) or take other external advice.

Multi-fund accounting

Figure 3.1 illustrates how the various charitable funds fit together as classified by the Charities **SORP**.[7]

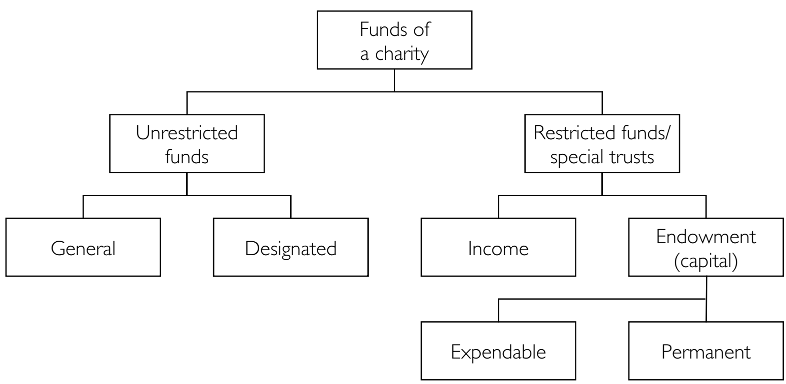

Fig. 3.1 The Charities SORP's classification of charitable funds

Bearing in mind that there could be numerous designated and restricted funds, the proper administration of individual charitable funds is essential if charity trustees are not to act in breach of trust. If you are a treasurer or finance officer with a business background, the need to account for several separate funds may be one of the biggest differences you find between commercial and charity accounting.

On a practical level, if you have more than just a general fund, your accounting records will need multiple categories for income and expenditure. Any donations for a specific purpose will need to be recorded separately. And, in the same way, any expenditure related to that income should also be separately identified. For example, donations specifically to fund a particular programme should be distinguishable from general donations, with any expenditure supporting that programme reported against it. In some cases, this may not be a whole cost – it could be part of a salary of one of your charity's staff members or an allocation of the cost to hire a hall. The simplest way to manage this is that every item of income or expenditure in your accounting records should be clearly labelled with the fund to which it relates. Chapter 4 looks at bookkeeping and explores some practical ways to keep the books of a small or medium-sized charity.

If you can structure your books into multiple funds on a day-to-day basis, you will be able to see what has come into and gone out of each fund at any time, and report that position to the trustees at your meetings. This will give the trustees the information they need to make decisions – where they have overspent, where they need to raise more money or where they still need to spend. It will also provide the information you need to report back to funders. Finally, it will help to explain what the cash held in your bank account relates to – is it there to be spent on general activities or is it tied up in restricted funds?

Some treasurers or finance officers may try to avoid multi-fund accounting throughout the year, leaving it as a year-end exercise for their accountant to resolve. This is not advised and could have serious consequences. Bear in mind that if this analysis were left to the year end and it was only then discovered that money in restricted funds had been spent on something else, the trustees would have committed a breach of trust. Alternatively, realising too late that all cash was tied up in restricted funds could lead to the collapse of your charity.

It is inevitable that some restricted funds won't be fully spent at the year end – in fact, some grants cover multi-year periods anyway. This means that at the end of the financial year, you will need to work out the final balance (opening balance plus income received less expenses paid) on each restricted fund to carry forward to the next financial year. In a charity with multiple restricted funds, there will need to be a separate figure for each fund balance brought forward. These are shown in the annual accounts (chapters 13 and 14) and will have implications for financial planning (chapter 6).

Do you need separate bank accounts?

Separate bank accounts are often seen as a solution to multi-fund accounting, with an individual bank account opened for each restricted fund. Sometimes it may seem that funders require this in their documentation – that each grant should be held in a separate account. Usually, they simply mean a separate fund in your accounts. However, if you are in any doubt, you should check with the funder.

Some long-standing charities have multiple bank accounts that were set up historically to cater for different restricted funds. If you are a treasurer or finance officer with several bank accounts set up in this way, you will often find that the balance in a restricted fund's bank account bears no resemblance to what is now reported in your accounts. This can be due to various factors, such as transfers having been made between the funds without the physical cash being moved between the bank accounts, or simply paying an invoice from the wrong account and not correcting it. It can therefore become confusing, and the balances of general and restricted funds can become blurred until the year-end accounting is carried out.

Therefore, even though it may seem to make sense to have a bank account for each fund to keep the transactions separate, it is not always practical. Another difficulty is that if one invoice covers multiple funds, you will need to either pay a portion from each account or make transfers between accounts to cover it. Yet another concerns changing signatories on bank accounts when trustees change: it can be time-consuming and frustrating to make the change on one account, let alone numerous accounts. If a bank account hasn't been used for some time, there is the **risk** signatories will not be changed when required, which can make accessing the bank account for the current trustees very difficult.

Although it may not be practical to have a bank account for each fund, it may be wise to have more than one bank account for the charity – often an account for day-to-day transactions and a **deposit account** where your charity can earn interest on any funds that do not need to be spent immediately. If possible, these should be held with different banks, especially if your charity's funds are substantial, to make use of the Financial Services Compensation Scheme, where cash deposits held at a single bank are protected to the amount of £85,000 in case of bank failure. Charity bank accounts are covered further in chapter 5.

Transfers between funds

Sometimes you will need to make transfers between funds. When this happens, you record an inter-fund transfer. As part of fund accounting, this is unique to charity accounting and so is not necessarily covered in general bookkeeping and accountancy textbooks.

As mentioned previously, it is possible to designate unrestricted funds – for example, a repairs fund. To do this, you would record an inter-fund transfer from the general fund to the designated fund – it is essentially showing expenditure from one fund as income into another fund and is a simple transaction to make.

However, sometimes the transfer involves a restricted fund. As discussed, a restricted fund only arises due to conditions imposed by the donor or as a result of the intention and way in which a specific fundraising appeal was carried out. Trustees cannot restrict money artificially and simply put funds into a restricted fund without good reason, but such a transfer may be justified in a case of meeting unfunded costs on a restricted project. If there is a restricted grant being used to fund a project but it only partly meets the costs, the trustees can make an inter-fund transfer from the unrestricted funds to the restricted fund to meet those costs and prevent the restricted fund being in a **deficit**.

There is also the possibility to make inter-fund transfers from a restricted fund to an unrestricted fund. This tends to happen where a grant includes an element of funding to cover a proportion of the core administration, or overhead costs, of your charity. One way of reflecting this would be to transfer the relevant portion of the grant from the restricted fund to the general fund. There is an alternative way, where administration costs are apportioned to the restricted fund as incurred, but sometimes using the inter-fund transfer method makes the costs clearer. Core costs and overheads are covered in chapter 6.

As explained in the section on endowment funds above (see page 41), there may be the opportunity to transfer some assets purchased with restricted funds to unrestricted funds as soon as they are acquired. For example, a community transport charity might raise money specifically to buy a minibus that will then be used for its general activities. All donations and fundraising are included in a restricted fund for the 'minibus appeal'. However, once the minibus has been purchased, it is used in the general course of meeting the charitable purposes of the transport charity. If the funder clearly awarded the funding on the basis that the charity would be free to do what it wanted with the minibus once it had been purchased, a transfer could be made of the value of the minibus from the restricted fund into the unrestricted funds. Note that this is only relevant to charities preparing **accruals account**s (see chapter 14).

Inter-fund transfers should be agreed by the trustees but are solely an accounting entry unless separate bank accounts are held, in which case there will need to be physical transfers between the bank accounts to reflect the movements. It is important to note that these transfers do not increase or decrease the funds of the charity overall – they are simply the movement of resources between funds. However, these are important transactions in fund accounting and, as described in chapters 12 and 13, they form a separate line in the annual accounts.

Reserves

Like any other type of organisation, charities need to have sufficient money on hand at any time to meet their immediate and possibly unexpected expenses. Although charities receive income to spend on their charitable aims, they wouldn't be sustainable if they spent that money straight away. Charities therefore need to build reserves. Where a charity makes a surplus (i.e. when the income received is more than the expenses paid in a particular period), that surplus can be put aside and will start to form a reserve.

As discussed, charities have different funds, and at the end of the year there may be a surplus of income on some or all funds. Effectively, these are the charity's reserves – the surplus left over to meet future expenses. But some of these funds may be restricted and therefore only able to be spent on something specific. They won't be as useful in making the charity sustainable as unrestricted funds will. Charity reserves are often described (for example, in guidance from the regulators) as the part of a charity's unrestricted funds that is freely available to spend on any of the charity's purposes. There is a calculation that can be used to determine these, as described later in this chapter (see page 50).

Why do charities need reserves?

Generally, a charity is expected to spend its income on advancing its purposes, unless there is a specific reason for keeping that income. Accumulating money is not itself a charitable purpose, and so retaining large amounts towards general running costs is not acceptable; this is seen as putting the needs of future (unknown) beneficiaries ahead of current (known) beneficiaries. However, if there are reasons the charity is holding on to money, and this can be explained, then this is usually acceptable. In recent years, with the challenges brought by the COVID-19 pandemic, having reserves helped many charities to stay sustainable and financially resilient. When charities collapse, it is often because they have insufficient reserves, in particular if they do not have enough money available to pay bills when they are due (see also page 117 on cash flows).

The reserves a charity needs are unique to the charity itself – there is no one-size-fits-all approach. As the treasurer or finance officer, your role is to help the trustees understand why your charity needs reserves. There are several factors to consider, all of which involve looking ahead. It can be helpful to think in terms of not only the running costs that need to be covered in the immediate future but also the risks and opportunities that your charity will face moving forward.

Firstly, it is important to have money put aside to protect your charity in case there are any drops in income. This is a challenge all charities face at some point, especially those relying on grants as their main funding stream. The questions to consider include: When will our current funding streams run out? Will our project be finished by then or do we need to apply for further funding? What happens if our funding applications are unsuccessful? Consider too that if your charity provides a service to vulnerable beneficiaries, it may be harmful to them to abruptly end a service when funding runs out. Having some reserves to rely on can give you breathing space to manage the 'What happens next?' question.

Secondly, reserves can be called on to meet unexpected or unavoidable costs, such as unplanned repairs to a building. They can also be used to fund the gap that often happens between starting a project and receiving a grant. And sometimes funding, especially from a local authority, is paid in arrears; reserves can be used to fund the salaries and expenses that may need to be paid before that first payment is received.

Finally, thinking more positively, reserves can allow your charity to grow – for example, to take advantage of opportunities that present themselves as a new way to meet your charitable purposes, to develop or expand your projects, to recruit for a new role that is desperately needed, or perhaps to develop other more sustainable funding streams.

Considering these factors, it is easy to see that different charities will need different levels of reserves. A small grant-making charity that only makes one-off grants and has no ongoing regular obligations may be able to manage with almost no reserves. On the other hand, a service-providing charity running a number of complex projects with uncertain income streams will usually need more significant reserves. And charities whose income is seasonal, or where long-term commitments are made (for example, in a charity funding medical research), may need even higher reserves.

Reserves policy

A charity must have a **reserves policy**. It is a legal requirement for charity trustees to state that policy in their **trustees' annual report** (see chapters 12–14), and it fits with the good **governance** principles of acting in the best interests of your charity (discussed in chapter 2). Your reserves policy explains why you are holding a particular amount of reserves and gives confidence that your charity's finances are being properly managed. This can be especially useful to help potential funders understand both why your charity needs their money and that it is financially resilient enough to carry out the work for which it is requesting funding.

Your reserves policy should not allow your charity to tie up money unnecessarily, but it should set out the factors that influence your reserves, such as potential risks (see chapter 5), current funding streams, how diverse and sustainable those streams are, and future spending plans. Importantly, these factors need to be quantified – in other words, it should be established what they mean in terms of the amount of money your charity should be holding. Your policy should set out how often the required reserves are reviewed, how they are compared to actual reserves, and the actions that may need to be taken where the required and actual reserves do not match.

Calculating required reserves

As previously noted, the level of reserves needed differs from charity to charity and therefore so will the policy and the level of detail required. The following provides some practical ways to calculate a required – or target – reserves figure.

A common approach, and often a good starting point, is to look at three months of costs. This means considering the funds needed to meet the normal running costs of your charity over the very short term. The easiest way may be to divide the annual expenditure in your latest charity accounts by four as this will give you an approximate number for three months of costs. Be aware that the amount could be skewed if the annual expenditure in your latest accounts is not a true reflection of your regular costs. For example, do they include an unusual cost your charity incurred, or has the rent increased since the previous year?

An alternative way to calculate reserves is to consider your forward financial planning (this is covered in chapter 6). If you have a **budget** in place that has looked at all the costs your charity is likely to incur, then this may provide a more accurate figure on which to base your target reserves amount. However, even with this calculation, you will need to consider how relevant the policy is to your charity's needs ahead – does three months seem too short to find alternative funding? It may be more appropriate to calculate a six-month figure.

Some charities, perhaps those with more complex service provisions working with vulnerable beneficiaries, may need to put aside additional money to cover the costs of running a particular service for a period of time while additional resources are found.

If your charity employs staff, it would be wise to consider the costs of redundancies, and it is also useful to find out about any terms, conditions and exit payments for ending **contracts** such as leases. In the unfortunate situation of your charity not receiving any funding, what would happen when the reserves ran out? Redundancy payments would need to be made and agreements for renting premises, equipment and ongoing services (such as HR support) would need to be ended. When you take into account factors such as these, you are moving towards a risk-based approach of calculating reserves, focussing on the individual circumstances of your charity and the level of reserves that is appropriate to hold.

Having looked at these considerations, you may conclude that the required reserves you have calculated are better expressed as a range rather than a single figure. Whichever option you choose, you will have a target against which to compare your actual reserves.

Calculating actual reserves

Calculating your actual reserves (often called free reserves) does not require as much judgement as determining your required reserves; however, it is not always a straightforward process. You usually calculate your actual reserves when you complete your end-of-year accounts, and the figure is based on the balances of your charitable funds. The best way to think of the calculation is to look at those charitable funds that are not restricted, tied up in **fixed assets** or otherwise already committed to meet some required expenditure – in other words, the ones that are freely available to use:

Reserves = Total unrestricted funds – Unrestricted fixed assets – (Committed) designated funds

Note that if your charity reports on an R&P basis, there will be no fixed assets included in the fund figures, and therefore none to deduct in this calculation.

You can then translate the value of your reserves to how many months of expenditure it covers using the following formula:

$$\text{Number of months' reserves} = (\text{Current reserves} / \text{Annual expenditure}) \times 12$$

If you are considering a more risk-based approach to reserves, you may not need to calculate the number of months. Instead, it may be more suitable to compare the actual reserves you have calculated with the required reserves you determined. Reserves calculations are often carried out annually. However, if your charity is experiencing financial difficulties, you could measure and compare your reserves on a more regular basis as part of good financial management (see chapter 6).

Communicating reserves

As the treasurer or finance officer, it is important for you to communicate the required reserves and the actual reserves to the trustees. If the actual reserves are much lower than the target reserves, the trustees will need to take action to ensure your charity remains viable. For example, they may need to delay planned projects or source additional funding. It may also be necessary to budget for general fund income to be more than expenditure for the next few years, until your reserves have reached a sensible level.

On the other hand, if your actual reserves are much higher than your target reserves, then your trustees must plan how best these can be spent to meet your charitable purposes. It may be that fundraising efforts are decreased for a year or two to make sure your charity does not hold on to donated funds for too long, or the trustees might consider running an additional project or expanding the charity. The charity does not need to use these surplus funds all at once but it should have a plan for how they will be used over the following years.

This plan must be communicated in your annual report. You should outline not only the resulting figures but also how they have been calculated, what they mean for your charity and what the trustees plan to do to bring the actual reserves in line with the required reserves (if required). For smaller charities, this does not need to be complicated. The following example wording would suffice:

> The trustees have set a policy of maintaining unrestricted reserves equivalent to six months' expenditure. At present, the reserves amount to just under four months' expenditure, and the trustees will therefore be seeking to increase this in the coming year.

The reserves figure is often considered the most useful number in a set of charity accounts – especially for funders. It may not be straightforward to determine what reserves your charity needs or how to calculate the actual reserves you hold, but it will all help you to understand the financial resilience of your charity.

Fund accounting and managing reserves are two key areas that, as a treasurer or finance officer, you will need to be able to understand and communicate to your charity's trustees. When trustees have a clear appreciation of the financial position of their charity – based on its funds and reserves – they are able to make better decisions about how to use the charity's money.

4 Bookkeeping

All **charities** must keep **accounting records**. This is a legal requirement under all **jurisdictions**, regardless of the charity's size or registration status (as covered in chapter 2). It is often thought that the entire role of the **treasurer** is **bookkeeping** – looking after the accounting records (sometimes called the books or **financial records**) of the charity, recording the financial **transactions** and producing the accounts. This is generally not the case; the role encompasses much more than keeping the accounting records, and the level of involvement depends on the size and complexity of the charity concerned.

Bookkeeping is the process of recording and organising the **transactions** of the charity on a day-to-day basis – the starting point for financial record-keeping. This chapter looks at what makes good accounting records in terms of what should be kept and the formats to use. It considers the process of bookkeeping, from simple recording of transactions through to **double-entry bookkeeping**, and provides some practical examples of common situations you may come across. Finally, the chapter introduces the basics of **accruals accounting**.

Accounting records

It is important for somebody – usually the treasurer or **finance officer** – to keep the books and wider accounting records of your charity for two main reasons. Firstly, they provide an accurate financial record of what has happened to your charity over a period of time. This historical information is used to produce **annual accounts** – to demonstrate how resources received by your charity have been used. Secondly, the information within the financial records can be used to manage your charity going forward. Data extracted from the books also forms the basis of financial planning – what resources are needed, how much it costs to carry out a particular project, what decisions should be taken and so on. Tools to help with financial planning are discussed in chapter 6.

For these reasons, it is essential that your charity's books are kept in sufficient detail, are up to date and are easily accessible. In fact, charity legislation in all jurisdictions requires that the accounting records are sufficient to show and explain all the charity's transactions.[8] The **trustees** must be able to use those records to state the financial position of your charity, with reasonable accuracy, at any point in time. The legislation requires that the records show all money received and spent by your charity on a day-to-day basis, as well as all **assets** (what the charity owns) and **liabilities** (what the charity owes). These accounting records must be retained for six years from the end of the financial year to which they relate.

The accounting records are not only a list of transactions, a spreadsheet or output from a software package. Bank statements, invoices, receipts, **grant** applications and remittances, **fundraising** details, payroll reports, tax records and all other documents relating to financial transactions all form part of the accounting records of your charity. This will even include minutes of trustee meetings where financial decisions are taken. These records are often called the 'supporting documentation' to the transactions as they provide the proof of what has happened – they back up the reporting. It is therefore extremely important that these documents are retained and filed appropriately. All these records will be required when the annual accounts are **audited** or **independently examined** (see chapter 15).

Who keeps the accounting records and how they are maintained will depend on the specifics of your charity. If your charity is small, the bookkeeping and the task of maintaining the accounting records may be down to you solely as treasurer. If your charity is slightly larger, a paid bookkeeper or finance officer may complete these tasks on behalf of the trustees, but as treasurer you will need to have some understanding of and involvement with the accounting records (see page 29 for further detail on the relationship between the treasurer and finance officer). Bookkeeping itself is not simply a mechanical process – discussion and decisions may be needed as to where to record items, especially if a cost should be split across more than one **fund** or if a new **restricted fund** (see chapter 3) is required for a **donation**. Therefore, where there is a dedicated finance officer, communication between them and the treasurer is vital – as is the question of who has access to the records, so that the information contained in them can be readily available to the wider trustee group.

Problems can arise if a bookkeeper is employed for a limited amount of time per week or month, especially if there is not much engagement with the treasurer, other charity trustees or staff. If they do not have the opportunity to gain sufficient knowledge of the charity, they may be unable to make informed decisions about where to record a transaction. They may need to ask so many questions to account for the transaction correctly – or they may even make assumptions that must be corrected later – that you may feel, as the treasurer, that it would have been easier to keep the books yourself! But be aware that in smaller charities it is often the case that much of a treasurer's time is also taken up with making payments, banking receipts, chasing outstanding payments and other finance-related tasks, as well as attending trustee meetings. Therefore, if you are a treasurer who is also keeping all the books without the additional support of a finance officer, it is essential for you to ensure you have sufficient time available and manage that time well.

In setting up and managing accounting records and a bookkeeping system, there are generally three distinct stages to consider:

1 designing or adopting a system that works for your charity;

2 recording the day-to-day transactions;

3 **closing off** the books at the end of a financial period to prepare accounts.

If you are a treasurer in a larger charity with an experienced finance officer, you may have minimal involvement in these three stages – perhaps only when consulted on issues when decisions are needed, and to ensure you have an overview to fulfil your trustee responsibilities (see chapter 2). On the other hand, if you are a treasurer who carries out all finance tasks, you will need to be fully involved with all three stages. And if you are a treasurer at a charity that employs a bookkeeper, it is likely you will be heavily involved in levels 1 and 3, with the bookkeeper managing level 2, unless there are issues to resolve.

Designing or adopting a system that works for your charity is not only a task you need to consider when a charity is first established. If you have recently taken on a treasurer role, if your charity has quickly grown or if there have been changes in your charity's restricted funds or activities, there will be merit in assessing whether the system in place is fit for purpose.

Bookkeeping tends to follow one of two approaches: using a cashbook or implementing accounting software. The benefits and drawbacks to each, as well as some good practices to follow regardless of approach, are as follows.

Cashbook approach

Many small charities adopt a cashbook approach either by using actual paper cashbooks, which is much less common now, or a computerised spreadsheet package. The term 'cashbook' does not imply all transactions are made with physical cash; in its simplest form, a cashbook is a method to record a list of transactions – receipts and payments – that have been made through your charity's bank account(s) or in cash.

Paper books require the least financial investment; there is no need to have a computer available to use or be computer literate. Pre-drawn paper books can be purchased from most stationery outlets, or you can adapt a normal notebook. A pre-drawn book, usually stapled in the spine, makes it more difficult for pages to be lost, removed or changed, and some treasurers will value this physical permanent record. However, extracting the data from a paper cashbook in a useful form can be problematic and time-consuming.

It is more common for charities to computerise their cashbooks by using a spreadsheet application. Spreadsheets can have many advantages, especially for those with skills in this area. They can be set up to automatically calculate totals, and data can be sorted, searched and presented in useful ways, including graphically, to help communicate your finances at the click of a mouse.

However, whenever you open a spreadsheet, you have access to all the cells at once, which can provide an overwhelming amount of data, and there is the risk that a transaction will be entered in the wrong cell. You need to take care to ensure essential formulae are not overwritten or records changed inadvertently. Unlike with paper records in pen, where changes can be identified, it can be quite difficult to spot a cell or previous transaction that has been changed or even deleted in error. It is possible to lock or restrict access to certain parts of a spreadsheet – for example, protecting formulae in cells so that they are not manually changed.

If you are maintaining a spreadsheet-based cashbook, you will need to create back-ups – preferably dated and always saved to an alternative hard drive to minimise the risk of loss. You will also need to consider how the file can be passed on to the next treasurer or finance officer – especially if you are using your own computer. Using cloud-based file-storage and sharing software (such as Dropbox or OneDrive) is a good option to mitigate the failure or loss of hardware (but great care is needed with regard to security – bear in mind that your charity's accounting records will likely contain a great deal of personal data regarding **donors**, employees and others). If responsibilities are shared, cloud-based software becomes especially useful, as both the treasurer and the bookkeeper or finance officer can access the file – access to it could also be made available to other trustees and your **independent examiner** or **auditor** (but this comes with the caution that errors can occur if more than one person works on a file at the same time). Also bear in mind the ongoing costs of cloud-based storage: in particular if your charity's records can *only* be accessed through the cloud-based system, it may be necessary to pay subscriptions for many years in order to meet the legal requirement to have access to records for the current year and six prior years.

Whether on paper or in a spreadsheet, a simple cashbook is normally split into columns for the date, the transaction type, details of the payee or the nature of the transaction, and then the amount received or the amount paid out. Figure 4.1 sets out a simple example.

Date	Transaction type	Details	Receipts £	Payments £
01 Apr	BGC	Grant from council	5,000.00	
18 Apr	DD	Rent		300.00
20 Apr	FPO	Jingles Ltd: music therapy activity		500.00
30 Apr	FPO	Wages to administrator		200.00
06 May	Cheque: 000316	ABC Printers: leaflets		65.00
11 May	Pay in	Cash takings from coffee morning	135.00	

Fig. 4.1 Simple cashbook: transaction list (BGC is a bank giro credit, DD is a direct debit and FPO is a faster payment outwards – all common terms you may see on your bank statement).

Although this method is simple to prepare – often only copying what is shown on your bank statement – there are some potential drawbacks to consider. The information will not be readily available to show, for example, how much you have spent on a particular project in a month, or how much you have spent on resources for the Christmas fayre, or even how much a particular fundraising event generated. To report this kind of information back to your fellow trustees, you may need to identify and add up various figures, and moreover you will only be able to do this if the description of each transaction is full enough to identify the category to which it belongs. Therefore, although the initial recording of the transactions may be quick and simple, the reporting for trustee meetings and in particular annual accounts may be troublesome for all but the simplest of charities.

It is possible to add in additional columns to help you more easily identify the type or purpose of the receipt or payment, as shown in figure 4.2. If you are using a spreadsheet, there will be the ability to sort the data by column to easily identify all transactions relating to a particular purpose. For example, in figure 4.2, the 'Payee/donor' and 'Purpose' columns have replaced the 'Details' column in figure 4.1. The data can then be sorted using the 'Purpose' column to pull together all transactions relating to a particular activity. To work effectively, this does rely on specifying transactions in a consistent way, but it is a helpful way to find information quickly. In saying that, care should be taken when sorting data to avoid permanently re-ordering the information. Therefore, unless you are confident with your spreadsheet skills, it is often best to re-order the data on a temporary copy.

Date	Transaction type	Payee/donor	Purpose	Receipts £	Payments £
01 Apr	BGC	Midshire Council	Grant	5,000.00	
18 Apr	DD	Edwards Properties Ltd	Rent		300.00
20 Apr	FPO	Jingles Ltd	Activity – music therapy		500.00
30 Apr	FPO	F. Oliver	Wages		200.00
06 May	Cheque: 000316	ABC Printers	Printing		65.00
11 May	Pay in	Cash	Coffee morning	135.00	

Fig. 4.2 Simple cashbook: with name of payee or donor, and purpose

But to avoid searching through the transaction list to pull out particular items, it may be helpful to have further columns and create an analysed cashbook. An analysed cashbook has columns for different types of receipt and payment. When you record a transaction, the value is entered into a specific column. This means that when you are looking to report back on a particular type of receipt or payment, you will be able to readily identify the relevant transactions as they will all be set out in the relevant column. An example of an analysed cashbook is shown in figure 4.3.

Most manual bookkeeping systems are based on an analysed cashbook approach. In a paper cashbook, there will be limitations on how many columns can be added. For example, you might need one book for receipts and one for payments for each bank account or petty cash tin. And you should also consider how **fund accounting** (see chapter 3) will be managed – will there need to be a separate book for the **unrestricted fund** as well as each restricted fund?

Managing an analysed cashbook using a computer spreadsheet application will be easier – more columns can be added as required. That said, too many columns can be difficult to both see on the screen and print out in an easy-to-read format. Different tabs (instead of using different paper books) can be used within a single spreadsheet. For example, you could have one tab for all receipts, split into columns to reflect various funds, and a second tab for all payments organised in a similar way. Alternatively, each tab could be used to record the receipts and payments for each of the different funds your charity has. If you have advanced spreadsheet skills, you may soon find you have a complicated

Date	Transaction type	Payee/donor	Purpose	Bank balance	Receipts		Payments			
					Grant	**Fundraising**	**Premises**	**Wages**	**Activities**	**Printing**
				£	**£**	**£**	**£**	**£**	**£**	**£**
31 Mar	Balance brought forward			3,540.00						
01 Apr	BGC	Midshire Council	Grant	8,540.00	5,000.00					
18 Apr	DD	Edwards Properties Ltd	Rent	8,240.00			300.00			
20 Apr	FPO	Jingles Ltd	Activity – music therapy	7,740.00					500.00	
30 Apr	FPO	F. Oliver	Wages	7,540.00				200.00		
06 May	Cheque: 000316	ABC Printers	Printing	7,475.00						65.00
11 May	Pay in	Cash	Coffee morning	7,610.00		135.00				
18 May	DD	Edwards Properties Ltd	Rent	7,310.00			300.00			
30 May	FPO	F. Oliver	Wages	7,110.00				200.00		
	Total				5,000.00	135.00	600.00	400.00	500.00	65.00

Fig. 4.3 Analysed cashbook: single fund, with totals and running bank balance

model with figures pulling through from one tab to another to provide overall summaries, with the spreadsheet perhaps also linked to your annual **budget** (see chapter 6). It is worth pointing out that, in addition to considering the potential drawbacks noted above regarding spreadsheets, you may need to ensure that a complex spreadsheet has not become too difficult to pass on to the next person taking on the role of treasurer.

Accounting software

In many charities, the number of transactions incurred may make running a cashbook – either paper or spreadsheet based – impractical. In this case an accounting system will be more appropriate, and even in small charities with simple accounting needs, trustees may choose to invest in accounting software. If your charity has over ten transactions a month on a regular basis, you may find the software option is beneficial. This is both in terms of time taken to record the transactions and ease of reporting the information. It could also reduce the costs of an **independent examination**. It is worth noting that if your charity is registered for VAT, or perhaps may be in the future (see chapter 9), your VAT returns will need to be submitted with Making Tax Digital (MTD)-compatible software. Most accounting packages do offer this.

Accounting software is in essence a computer program that assists accountants and bookkeepers in recording and reporting financial transactions. There is a vast array of options available and choosing which to invest in will be a decision for the trustees, albeit influenced by those using the software – perhaps the treasurer and/or finance officer, or with advice from the independent examiner or auditor, who will probably have experience of several accounting packages.

The software may be a stand-alone package installed on one computer or a cloud-based package that can be accessed from any computer connected to the internet via a user login. There is a choice of general-purpose accounting software and more charity-specific software. Although general-purpose accounting software packages are primarily focused on the business world and profit-making organisations, most of the popular ones do have options for charities. This includes the terminology – such as 'net income' rather than 'profit' – and the ability to carry out fund accounting. Accounting software will be based on the **accruals** principles (discussed later in this chapter), but often with an option to change to cash-based accounting for charities preparing **R&P accounting** (see chapter 13).

As explained in chapter 3, fund accounting is integral to charity accounting, and it is vital that you can determine the balance of any fund at any time. If you are going to use general-purpose software with charity options, it is worth checking how the facility for fund accounting works. Some work very well, allowing costs to be split across different funds as the transaction is recorded and offering the ability to produce reports split by funds so it is easy to determine the progress of a particular fund. The software company may not use the term 'fund', so look out for options that allow 'class' or 'tracking'.

There are some accounting systems designed specifically for the charity sector. For larger charities with more complex needs, it may be more appropriate to use a charity-specific system which can manage multiple levels of projects, funds and activities, reporting across multiple years if needed. And there is always the option of engaging software designers to develop a bespoke system, although this will be costly.

In the long term, having accounting software which is tailored to charities will probably be more beneficial than trying to make business-specific software fit. Most of the popular cloud-based software options do offer charity functions and are competitively priced, easy to set up and intuitive to use. Some also offer discounted fees to **registered charities**. Whichever system you adopt, it is worth bearing in mind that it will not replace the need for some charity accounting knowledge, and it is unlikely that a fully prepared set of annual accounts will emerge directly from the accounting software. You will likely be able to produce reports that will form the basis of your accounts (**annual reporting** is discussed in chapters 12–14).

Running an accounting software system tends to be more reliable than the cashbook approach. Many packages can now be linked to your bank account(s), pulling transactions into the system automatically from a bank feed, meaning that the transactions only need to be classified to a particular account and linked to a specific fund where needed. Any software offering this option has to comply with the tight data security requirements of the banking institutions, reducing the risk of unauthorised access to your charity's data or banking system (note that it is not possible to access your charity's bank account or make payments from it using accounting software). These automatic bank feeds help with consistency, and some packages can learn to predict where transactions should be processed and can match receipts to invoices raised. It is even possible to attach invoices and supporting documents to the transactions in some packages. The systems may also be able to produce user logs and other information, helping with the **audit trail** – information which enables an auditor or examiner to verify how any figure in the accounts was reached.

Even with automatic bank feeds, accounting software does need the same level of human interaction and skill in determining where to record a transaction that is needed for cashbook accounting. However, there is less scope for error, and the major benefit is the wide range of reports that can be automatically generated from the transactions. This means you can access relevant financial information when it is needed – for example, a list of donations for a particular cause, the costs involved in a particular activity, or even a full analysis of the receipts and payments across all funds for a period of time. Many packages will allow you to generate a report showing current and prior year figures, so you are able to make comparisons as to how successful a particular event was at raising money this year compared to last. Some packages also have the option to add in a budget, which makes it easier to compare your budgeted and actual results (see chapter 6). Analysis between years and against budget using cashbook records would take significant effort and time.

As with any new system, learning may be needed, and most packages have in-built training elements and comprehensive help functions. It may be useful to ask for the help of your independent examiner or auditor in the initial set-up if you are unsure which categories of accounts and funds to add. It is also important to consider access, security and back-ups of the data so as to prevent unauthorised use or loss of financial information. Some software packages will let you set up multiple users with different access levels. This can be extremely helpful – for example, you could give a limited level of access to a fellow trustee or your **charity co-ordinator**, so that someone has access to the accounting information if you are unavailable. It can also assist with transparency among trustees and internal controls (see chapter 5) over the finances. However, unauthorised access may be a risk to your charity, so general computer security measures should be taken, such as strong passwords, not leaving applications open in public places and quickly removing any access rights from anyone leaving the charity.

Bookkeeping principles

Regardless of whether you are running a paper cashbook, using a spreadsheet approach or operating accounting software, there are some general recommendations to follow for successful bookkeeping.

Recording a transaction

When recording a transaction in your charity's books, there are four main points to consider:

1. Which bank account or petty cash tin does the transaction relate to? You will need to ensure the transaction is logged against the correct bank or cash account.
2. Is this an unrestricted transaction or does it need to be allocated to a particular fund?
3. What type of transaction is it? For example, is it a donation or **fee** for services, or a payment for a utility bill or printing leaflets?
4. What was the date of the transaction? It must be recorded using the actual date in the correct **accounting period** (this could mean your charity's financial year or a shorter period, such as VAT quarter where applicable).

It can be tempting to have many different categories covering all eventualities for different types of receipts and payments. This may be necessary if your charity has a lot of transactions and complex activities, but it can also be cumbersome, and one category may only end up containing one or two transactions. For example, do you need separate categories for postage, telephone, computer costs and stationery, or could they be combined to an 'administrative expenses' category? Whatever categories you choose, it is important to be consistent when allocating transactions to them. It is generally better to use categories such as 'miscellaneous expense' as little as possible. Often these are used when there is no immediately obvious category to allocate a transaction to, but this can result in a very large miscellaneous expense at the year end, which will need to be reallocated to more suitable categories. A further consideration is the needs of the trustees. Think about how they will need income and expenditure broken down to understand your charity's finances better and make decisions for the future.

It is also useful to reference the supporting documentation for a transaction. This can be as simple as adding a reference number to each transaction and writing that reference number on the supporting document – the receipt or invoice. Supporting documents can be filed as paper copies in a binder. If someone needs to look at the transaction later, it will be easy to identify the document to which it relates. Alternatively, if you are only retaining soft copies of documents, the invoice, receipt or similar supporting document should be filed in an appropriate folder under that reference number and perhaps the name of the supplier. Many accounting systems now have the function to attach a soft copy of the document to the transaction itself.

The no-offset rule

Accounting rules do not allow transactions to be offset against each other; receipts or payments should be shown gross. For most transactions there will be no issue, as the receipt or invoice will show the full amount. However, the following example illustrates where it would be easy to offset and so care should be taken.

> Example
>
> A team from your charity attends a tabletop sale at the local summer fête selling items made by the beneficiaries of your charity. Cash sales made over the day amount to £300. At the end of the day, the fête organisers collect £50 from the fundraiser for hire of the table. The fundraiser banks the remaining £250 in the charity account. When you come to record the transaction from the bank statement in your accounting records, it would be easy to record it as 'fundraising income' of £250. But this would be understating your total receipts by £50. It would also not recognise that there was a cost involved in raising that income. Therefore, the transactions that should be recorded are: 'fundraising income' at £300 and 'fundraising expense' at £50.

Although in this example there may be a minimal effect, if this happened multiple times or with a larger transaction there could be a significant understatement of your charity's income. As covered in chapters 12–14, your charity's income level is critically important in determining what type of accounts you can prepare and what level of scrutiny of those accounts is needed.

Multiple bank accounts and petty cash

It is quite normal for a charity to have more than one bank account and often more than one petty cash tin. If this is the case, it will be easier to keep records for each account separately, otherwise transactions may become confused, and it will not be easy to see the balance on each. Where possible, it is advisable to bank money and cheques as soon as practical and hold as small an amount of cash as possible. This reduces the risk of loss of funds (covered in chapter 5, on risks and controls).

If a bank account is solely an investment or **deposit account**, it may not be necessary to keep a full cashbook and a simple note of the interest received and any transfers in or out may suffice for the records. However, the interest will form part of your charity's overall income. Therefore, if there is no actual cashbook for the deposit account, there must still be a method to record it in your overall books. If you are using accounting software, you will need to set up each bank account separately within the system, even if there are minimal transactions in each account. Remember that any transfers between bank accounts are simply movements and do not affect your overall receipts or payments, as your charity has not actually received new funds or paid anything out, but they will still need to be recorded in your charity's books to reflect the correct balances in each account.

If your charity does operate with petty cash, the easiest way to treat this is just like another bank account. If you are using the cashbook approach, it will probably be easiest to set up an additional book, or a separate tab on a spreadsheet. In accounting software there may be numerous ways to manage petty cash, but usually it is handled as a distinct petty cash account. As with a deposit account, transfers between your bank account and petty cash, such as when you write a cheque for cash or deposit petty cash into the bank, are cash movements only. They still must be recorded in your charity's books, but it is only when cash donations are received or cash payments are made to suppliers that your income and expenses will be affected.

It may be tempting not to have a fully analysed petty cashbook and simply input your cash entries as a separate column in your main books, but this will usually mean the purpose of the cash transactions has not been explained. This could lead to a lot of additional work at the year end trying to analyse a year's worth of cash receipts.

Double-entry bookkeeping

When you record a transaction in a cashbook or spreadsheet, you are essentially only recording one side of the transaction – the receipt or payment. But every transaction has two sides. For example, if your charity receives a donation of £500, the amount held in your donations pot goes up and your bank balance also goes up. The reason everything is recorded twice is to provide valuable information on what the transaction was for – in this case it was a donation (a receipt) – and to explain the change in your bank balance – in this case, £500. Therefore, if you manage a cashbook which also includes a running bank balance (as shown in figure 4.3), you are in fact creating a double entry – you can see both the receipts and payments and their effect on your bank balance.

Almost all accounting systems are based on the double-entry principle (known as double-entry bookkeeping) – although that may not be obvious when you record a transaction. If you have an accounting or bookkeeping background, you will be very familiar with this process. If you do not, it will be useful to understand how it works, including the two main terms involved: **debits and credits**.

Every transaction gives rise to a debit and an equal credit. One way to think about this is in terms of transactions through your bank account and what the opposite side will mean:

- A *debit* flows into your bank account – it provides more money, and it is something your charity owns. The opposite and equal credit is therefore the money your charity has received, for example a donation or grant.
- A *credit* flows out of your bank account – it occurs when your charity spends money, and it is something your charity owes. The opposite and equal debit is therefore something that your charity has paid, for example a rent payment or a purchase of supplies.

For a charity, having a debit balance on its bank account is a good thing – it is the money it holds. This can be confusing, as bank statements will say you are in credit. This is because the statement is from the bank's point of view – your charity has deposited the money with the bank, and it is not the bank's money; the bank owes the bank balance back to your charity.

When looking at a transaction, think first about whether it is a flow into (debit) or out of (credit) your bank. This will give you the first part of the double entry. The opposite side will describe the transaction. For example, any receipt is a flow into your bank, as shown in the following examples.

A donation of £500 paid into your bank for any purpose

Debit: Bank £500

Credit: Donations (unrestricted) £500

An incoming grant of £2,000 paid into your charity's bank for a residential weekend

Debit: Bank £2,000

Credit: Grants (restricted: residential) £2,000

These examples show that while the flow into the bank is recorded as a debit, the other side of the transaction – the actual type of receipt – is recorded as a credit.

On the other hand, anything your charity pays is a flow out of your bank, giving the following examples.

> A payment of £250 to the local community hall for rental of the facility for an activity day
>
> *Credit*: Bank £250
>
> *Debit*: Venue costs £250

> A payment to a hostel of £1,200 for accommodation on a residential weekend
>
> *Credit*: Bank £1,200
>
> *Debit*: Activity costs (restricted: residential) £1,200

> A payment of £70 to a local shop which included £45 for printing paper and cartridges and £25 for paper cups and plates for an upcoming event
>
> In this case there are more than two entries to capture the costs properly:
>
> *Credit*: Bank £70
>
> *Debit*: Printing £45
>
> *Debit*: Event supplies £25

These examples show that while a flow out of your bank is recorded as a credit, the other side of the transaction – the actual type of payment made – is recorded as a debit.

In some cases, you may need to take money out of your bank to put into a petty cash tin. The double entry here reflects the flow out of the bank and into petty cash. No receipt or payment is created, as in the following example.

> A transfer of £50 from your bank to petty cash
>
> *Credit*: Bank £50
>
> *Debit*: Petty cash £50

There are some transactions where it is much more complicated to form a double entry. One of these is wages and salaries. Many accounting systems have add-on payroll systems which will create payroll **journals** automatically. 'Journal' is an accounting term for a transaction formed by one or more debit and one or more credit. If the finance officer, bookkeeper or treasurer at a charity is confident with the rules surrounding payroll, then running online payroll software may be an option, although many charities use an outsourced payroll service. Employing staff is covered in chapter 11, which also includes explanations of deductions and payments to **HMRC** and pensions providers, but for completeness in this bookkeeping section an example of a double entry for wages is given as follows.

Double-entry bookkeeping: payroll example

An employee is paid £1,200 gross. The employee deduction for income tax is £95, the employee's National Insurance is £20 and the employee's pension contribution is £60. The employer's payments are £55 for the employer's National Insurance contribution and £36 for the employer's pension contribution. This means the following payments are needed.

To the employee: gross pay less deductions = £1,200 – £95 – £20 – £60 = £1,025:

- *Credit*: Bank = £1,025
- *Debit*: Wages (net) = £1,025

To HMRC: tax and National Insurance payments = £95 + £20 + £55 = £170:

- *Credit*: Bank = £170
- *Debit*: Wages (tax and National Insurance payments) = £170

To the pension provider: £60 + £36 = £96:

- *Credit*: Bank = £96
- *Debit*: Wages (pension) = £96

These transactions result in three payments to wages: £1,025 + £170 + £96 = £1,291. Note that this is more than the employee's gross pay, as it includes the employer costs (sometimes called 'on-costs' of salaries) and reflects the true cost to the employer. If an employee has worked on more than one project, it may be that some of this cost also needs to be split between unrestricted and restricted funds, creating even more debits and credits.

Non-cash transactions

All transactions considered so far occur as a result of a receipt or payment, either as cash or through a bank. And although these will form the vast majority of the transactions in your books, there are also some non-cash transactions to consider. A common non-cash transaction for charities is a transfer between funds (see chapter 3). For example, let's say your charity needed to transfer £500 from your **general fund** to a restricted fund to supplement a shortfall. In some situations, if you were managing separate bank accounts for your restricted and unrestricted funds, there would be a cash flow involved and two double-entry journals as follows.

Non-cash transaction with separate bank accounts

Credit: General bank account £500 (the cash flow out of the bank)

Debit: General fund (expenditure) £500

Debit: Restricted bank account £500 (the cash flow into the bank)

Credit: Restricted fund (outreach income) £500

However, if the funds shared the same bank account, no bank entry would be involved. This means the two bank entries above would cancel each other out, leaving a non-cash double entry as follows.

Non-cash transaction within the same bank account

Debit: General fund (expenditure) £500

Credit: Restricted fund (income) £500

It is best to record fund transfers in columns or accounts separately from other receipts and payments, so that they can be identified as such for your annual accounts and not be confused with external receipts or payments. Also note that there are several other types of non-cash transaction that can be considered which are only needed if your charity is using accruals accounting, discussed later in this chapter.

Double-entry bookkeeping on a manual basis involves more work than a simple cashbook. It relies on having several books (often called 'ledgers'), each with two columns, called 'debits' and 'credits'. Every transaction is written with a value in both the debit column and the credit column. This does provide an in-built check to help you detect errors as the debits and credits must balance, but the number of ledgers needed may be cumbersome. Although it is very rare to see double-entry ledgers carried out in paper books now, the double-entry system may be used in more complex spreadsheets which come together to form a **trial balance**. The trial balance is a list of the total amounts in every account (i.e. the various types of receipt and payment categories together with the bank and fund balances) at a point in time. Because the debits and credits must be equal for every transaction, it follows that total debits and total credits should be the same across all of your transactions. This results in the trial balance – the total of all debits are equal to (balance with) the total of all credits. If you find that they are not equal, there will be a mis-recorded double entry somewhere. The trial balance is used to form the basis of your annual accounts.

In a book of this length, there is no space to explain the double-entry system in detail; however, most computer-based accounting systems work internally on a double-entry basis, without any need for the user to even consider debits and credits (and with the guarantee that the debits and credits will balance). If you don't use an accounting system and don't have full knowledge of double-entry bookkeeping on a manual or spreadsheet basis, and have instead maintained an analysed cashbook, at the year end your auditor or examiner will be able to support you in the actual preparation of your final trial balance and resulting accounts.

Closing off the books

The previous sections have considered the approaches available to manage the books and how day-to-day bookkeeping is carried out. The final stage of the bookkeeping system is how to close the books (often called **closing off** or balancing off) at the end of a period (such as a month, quarter or year) and to provide meaningful financial information for management purposes or your annual **financial accounts**.

How you close off your books will depend on which system you have adopted. If you are using accounting software, this is a very easy exercise as the books are automatically closed after each accounting period. At any point in time, it is possible to generate various reports – for example, a trial balance, which will show the total on each account, or an **income and expenditure account**, which will summarise all the receipts and payments in the period and provide a net result. Although this can be done at any time, when setting up an accounting system, it is necessary to enter your charity's year-end date. This means that when a year end is passed, it is possible to see only those transactions that fall into that particular year, which is necessary for preparing your annual accounts. Note that accounting software packages do retain transactions for all previous years that they have been in place, so it is always important to check you are working with the correct year.

Manual and spreadsheet approaches require more work to close off the books; however, before any system is closed, you should check the information in it is complete.

Once it is confirmed that all entries have been entered into the books, the process for closing off paper- and spreadsheet-based books can be carried out. There are various ways to do this depending on how the records are being held, but in essence you are looking for four main figures:

1. Total receipts
2. Total payments
3. Opening funds in hand: bank and cash balances
4. Closing funds in hand: bank and cash balances

You may have already balanced your books during the year, for example at the end of each month or quarter. However, for your actual year-end position, your total receipts and payments are those for the entire year, your opening funds are those at the start of the financial year and your closing funds are those at the year end.

Your total receipts for the year less your total payments will provide your **surplus** for the year (or **deficit** if your payments were more than your income). Adding this surplus (or deficit) to your opening funds gives your closing funds for the year – this is the balance in hand to carry forward to the next year. Figure 4.4 provides an example.

Common omissions to look for when closing off the books

As many accounting software packages have automated bank feeds, it is likely all bank entries will be included – though it is still vital to check that they have been recorded in the correct categories. But you may have transactions that do not come through your bank – for example, payments made through petty cash, bank accounts that cannot be connected or internal transfers between funds. For these transactions and if you are maintaining manual books, before closing you should check through all entries on your bank statement to ensure nothing has been missed.

Common omissions are items such as direct debits, bank charges, bank interest and donations that have come directly into your bank account – often from giving platforms (discussed in chapter 7) or from **BACS (Bankers' Automated Clearing System)**, a facility often used by **funders**. These transactions tend to happen automatically without you

Date	Transaction type	Payee/donor	Purpose	Balance forward	Receipts		Payments			
					Grant	Fundraising	Premises	Wages	Activities	Printing
				£	£	£	£	£	£	£
31 Mar	Balance brought forward			3,540.00						
01 Apr	BGC	Midshire Council	Grant		5,000.00					
18 Apr	DD	Edwards Properties Ltd	Rent				300.00			
20 Apr	FPO	Jingles Ltd	Activity – music therapy						500.00	
30 Apr	FPO	F. Oliver	Wages					200.00		
06 May	Cheque: 000316	ABC Printers	Printing							65.00
11 May	Pay in	Cash	Coffee morning			135.00				
18 May	DD	Edwards Properties Ltd	Rent				300.00			
30 May	FPO	F. Oliver	Wages					200.00		
etc.	etc.	etc.	etc.							
31 Mar	Totals for year				10,000.00	2,750.00	3,600.00	2,400.00	5,400.00	300.00
	Total receipts and payments					12,750.00				11,700.00
	Subtract payments from receipts					–11,700.00				
	Net surplus for year			1,050.00		1,050.00				
	Balance carried forward			4,590.00						

Fig. 4.4 Example of closing off the books

having to trigger them and often are only identified when they appear on your bank statement. On the other side you may have recorded transactions that have not yet appeared in your bank – for example, fundraising takings that haven't been banked. A bank reconciliation is imperative for this purpose. Bank reconciliations are discussed in chapter 5 as part of **internal financial controls**, but they form a check that everything going through your bank account is also reflected in your books, and vice versa.

If you are relying on paper bank statements, this may cause a gap between the period end and when you can close off the books; however, the use of online banking prevents these delays. If you have had to wait for statements, it may mean that items in your books are not necessarily in the same order as they appear on your bank statement. This shouldn't cause any problems, but remember that items in the books should be given the date when the money came into or went out of the bank account (or, where used, when the cheque was written).

Introduction to accruals accounting

So far this chapter has considered transactions that have mainly occurred because of income received and payments made either through your bank or in cash, which form R&P accounting. This tends to be the simplest form of accounting and can be sufficient for small and medium-sized charities to manage their finances on a day-to-day basis.

However, looking to annual reporting and the requirements for annual accounts, some charities must prepare them on an accruals accounting basis. Accruals accounting is based on the concept that transactions should be recorded in the period when the income or expenditure commitment *actually occurs*, rather than when the cash flows that relate to them occur.

The limits, requirements and formats of annual accounts are discussed fully in chapters 12–14, but as a summary:

- Any charity constituted as a company must prepare accruals accounts.
- Any other charity with an annual income of over £250,000 must also prepare accruals accounts.
- Any charity that is not a company and that has an annual income of under £250,000 can choose to prepare accruals accounts or much simpler **R&P accounts**.

If you are not familiar with accruals accounts but your charity's accounts must be presented that way, it is possible to keep the books on an R&P (or cash) basis during the year (as discussed in the previous section of this chapter) and appoint an accountant at the year end to convert everything to accruals for your final accounts. However, the results may look very different. For example, in the books, it may look as though there is a large surplus on one fund. However, once your accountant has added a journal to include a bill that has not been paid yet, that surplus may disappear.

Therefore, even if you are a treasurer whose role does not involve working with accruals, it will be useful to have a basic knowledge of the principles. This is especially important when it comes to understanding the annual accounts and communicating that information to your fellow trustees or using the details to answer questions from funders. If you can master even the basic principles of accruals accounting, it will probably give you a greater grasp and awareness of the financial position of your charity.

Alternatively, if you are a paid finance officer of a charity that prepares accruals accounts, you will probably be expected to have at least a working knowledge of accruals accounting, even if some of the more complex issues may require you to ask for advice from someone with more specialist knowledge – for example, your charity's auditor or examiner. As previously noted, most accounting software is based on the principles of accruals accounting.

The following sections consider some common accruals concepts that charities may come across. More complex accruals issues, including complying with the **accounting standards** and presentation in the annual accounts, are covered in chapter 14.

Concept of accruals accounting

As mentioned, in accruals accounting, transactions are recorded in the period when the income or expenditure commitment *actually occurs*. Putting this another way, accruals accounts should show the *income due* to your charity during the year and the costs and *expenses incurred*. This represents a much clearer picture of your charity's resources and demands than a presentation of the receipts and payments through your bank account, because it demonstrates financially what has happened in the year.

Accruals accounting and cash accounting (the basis for R&P accounts) are not totally distinct, and the vast majority of your day-to-day transactions (such as receiving a donation or paying wages) will be entered in the same way in both systems. In some cases, adjusting for accruals accounting may be relatively easy. It may involve, for example, including an invoice for work done before the year end that you paid a few days after the year end. In this case, you can easily determine the amount to include – in fact, you will probably have the actual amount on the invoice, which you will have received before you even produced the annual accounts. But some adjustments for accruals accounts may not be straightforward – they may require estimates and judgements to be made to determine when **recognition** of the income or expense is needed – that is to say, the point in time when your charity is entitled to the income or liable for the expenditure.

Accounting guidance exists to assist preparers of accounts and these principles can help you to determine the specific bookkeeping entries that you need. For charities the current guidance is the Charities **SORP** (**FRS 102**), which includes approaches to making estimates and judgements.[9] Sometimes, there are no right or wrong answers in calculating a value: depending on the judgements made, different sets of accounts could be produced for the same charity. However, estimates or judgements do have to have some reasonable basis and follow guidance where applicable. If your auditor or examiner does not agree, they could issue a **qualified report** (this means they have a concern over some of the accounting treatment used in the accounts). The subject of the SORP and the topic of accruals accounts themselves are explored in more detail in chapter 14, and qualified reports are covered in chapter 15. The remainder of this chapter looks at some scenarios that can result from accruals accounting and where estimates or judgements may be needed.

Debtors

Under R&P (or cash) accounting, the accounts reflect receipts – the actual cash your charity receives. However, under accruals accounting, the accounts reflect the wider 'income due'. For the income that is due but not yet received, the term **debtor** is used. Debtors are people or organisations who owe money to your charity. They exist when a commitment has been made to pay money to your charity, but the actual flow of funds has yet to be made. Debtors form part of your charity's **current assets**. **Asset** is an accounting term used to refer to any money, object or resources which an organisation owns or controls in order to carry out its work. Current assets are those assets which can be readily transferred into money within 12 months, and so they include debtors, stock held for resale, and cash and bank balances. (Note that if the amount is not due to be received within 12 months, a debtor is said to be 'recoverable in more than one year' and will need to be separately identified in the annual accounts.)

For example, a charity charges £100 to another organisation for a training course and raises an invoice. Under accruals accounting, the charity will include the £100 in its income when the invoice is raised. It will record the amount as a debtor. The double entry created is as follows.

Debit: Debtors £100
Credit: Fee income £100

When the payment is received, there is no effect on the income. There will be an inflow to the bank, and the amount owed to the charity (the debtor) is reduced, as follows.

Debit: Bank £100
Credit: Debtors £100

If your charity regularly raises invoices, you may want to set up a **sales ledger**. This is a term used for an account which records the invoices raised to customers (people or organisations) and, therefore, the debtors due to the charity. Once an invoice has been paid, the sales ledger is reduced by that amount. Therefore, a sales ledger helps you to keep track of your various customers and all amounts due to your charity at any time and is useful for year-end reporting. Accounting software packages that have an invoice function will automatically create a sales ledger.

Note that if money accounted for as a debtor is never received, you will need to make an entry to correct it. The entry needed will depend on the particular circumstances. For example, if it was because the work couldn't be fulfilled, you would raise a credit note to cancel the invoice. This would be sent to the customer so that they knew not to pay the invoice. You would then create a double entry with a debit to 'Fee income' and a credit to 'Debtors'. This reverses the original transaction. On the other hand, if the customer was not in a position to pay and the trustees approved waiving the debt, you would need to make a double entry to **write off** the amount owed (a debit to 'Bad debts' and a credit to 'Debtors'). This entry cancels the debtor but, instead of removing the fees, it creates an additional expense item.

A more complex debtor situation may occur with a legacy. For example, a charity is notified that someone has left it a £10,000 legacy in their will, although the money will not be paid over to the charity for many months. The charity is legally entitled to the money, and under accruals accounting it is now part of the charity's funds, so the trustees can decide how to spend it (but if cash flow is tight, it may be best to wait until the money is received before it is spent). The legacy is accounted for as a debtor with a double-entry journal as follows.

Debit: Debtors £10,000
Credit: Legacy income £10,000

When the legacy is received, there is no effect on the income as the legacy has already been included in the charity's funds. There will be an inflow to the bank, and the amount owed to the charity (the debtor) is reduced, as follows.

Debit: Bank £10,000
Credit: Debtors £10,000

In both examples, it is relatively straightforward to confirm that the charity was entitled to the money and the amount of the transaction. This may not always be the case, though. When looking to determine balances for your year-end accounts, you will need to take care in both identifying and valuing potential debtors. The more complex accounting rules around income and debtor recognition are examined in chapter 14.

Creditors

Under R&P (or cash) accounting it is easy to identify payments – the actual cash your charity pays out. However, under accruals accounting, the accounts reflect the wider 'expenditure incurred'. For the amounts due but not yet paid, the term **creditor** is used. Creditors are people and organisations who your charity owes money to. They occur when costs and expenses have been incurred for goods and services provided by suppliers (people or organisations), but the actual flow of funds to settle those costs has yet to be made. The term 'liability' is used to represent the wider obligations, including creditors, your charity has towards any third party. If that liability is expected to be settled within 12 months, it is termed a **current liability**. Where there is no obligation to settle the amount due until more than 12 months into the future, it is classed as a **long-term liability** (or non-current liability), and for the annual accounts it is classed as an 'amount falling due after more than one year'.

As an example of a creditor, a charity receives an invoice for £250 from an activity provider that has delivered a music therapy session. The provider has asked that the payment is made within two weeks. Under accruals accounting, when the charity receives the invoice, it will record the amount it is due to pay as a creditor. The double-entry journal created is as follows.

Credit: Creditors £250

Debit: Activity expenses £250

When the charity pays the invoice, there will be a flow out of the bank, and the amount owed by the charity (the creditor) is reduced, as follows.

Credit: Bank £250

Debit: Creditors £250

In this example, the creditor relates to a single activity, and probably one fund. However, typical creditors include regular bills such as from utility companies. In these cases, the double entries will remain as above, but the cost of the bill may need to be split (perhaps based on actual usage or an estimate based on activities) across the general fund and one or more restricted funds.

In a similar approach to the sales ledger, it may be useful to set up a **purchase ledger**. This lists all invoices received by your charity from suppliers. When an invoice is received from a supplier, you enter the details and amount due in the purchase ledger. When the invoice is paid, the amount on the purchase ledger is reduced. This helps you to keep track of all payments that need to be made to suppliers and, therefore, to identify year-end creditors. Accounting software will have this functionality.

Accruals, prepayments and deferred income

When it comes to your accounts at the end of the year, there may be some bills or costs that your charity has incurred but where no bills have been received. In these cases, it may be necessary to make an **accrual** – an accounting entry to recognise the value of a cost that has been incurred but not yet billed. These are often called 'accrued expenses'. Common examples include utility bills, especially when paid quarterly, and the fee due to your auditor or independent examiner. In this case, although the work is carried out following the year end, it relates to the year of the accounts concerned and, therefore, is a cost for that year. A double-entry journal for an accrual is similar to one for a creditor. For example, to accrue a fee of £800 for an independent examination, you would create the following double entry.

Credit: Creditors – professional fees payable £800
Debit: Independent examination fee £800

Then, when your charity paid the invoice, there would be a flow out of the bank, and the amount owed by your charity (the creditor) would be reduced.

Credit: Bank £800
Debit: Creditors – professional fees payable £800

Whereas creditors and accruals are needed to recognise expenses that have been incurred and not yet paid, sometimes the converse can apply at the year end – money has been paid in advance. For example, you might have to pay a large deposit to hire a venue for an event next year, or you may pay rent in advance. These are examples of **prepayments**. In this case, a double entry is needed to remove the expense from the current year and reflect an amount paid in advance – something owned for the future. For example, if your charity had made a payment of £1,000 before the year end as a deposit for a venue for an event the following year, the double-entry journals would be as follows.

On payment of the venue hire fee

Debit: Venue hire £1,000
Credit: Bank £1,000

To make the adjustment at the year end

Debit: Prepayments £1,000
Credit: Venue hire £1,000

In cases where you know that you're dealing with a prepayment when you first make the entry for the transaction, you could create a journal as follows.

Debit: Prepayments £1,000
Credit: Bank £1,000

In the following year, no payment will need to be made, but the accounts should reflect the cost of the venue, and so a journal will need to be made to recognise the cost in the year in which the event happens, as follows.

Credit: Prepayments £1,000
Debit: Venue hire £1,000

These journals are essentially moving the cost in the accounts from the year in which they were paid to the year in which they were actually incurred (i.e. the accruals concept).

Conversely, you will sometimes receive income in advance, for example a grant paid early but with a clear condition that it cannot be spent until the next year, or fees received in advance of an activity that are refundable if the activity cannot go ahead. Although you will have the money in the bank, your charity is not yet legally entitled to it, and there may be occasions where it needs to be repaid. Amounts received in advance are often called **deferred income**, and a typical double-entry journal, for example for a £5,000 grant received in advance, would be as follows.

Credit: Deferred income £5,000
Debit: Bank £5,000

And then in the following year, the grant would be recognised and the deferred income released, which would be recorded as follows.

Debit: Deferred income £5,000
Credit: Grant income £5,000

In this case, the journals are moving the income from the year in which it was received into the year to which it relates to under the accruals concept.

The amount to calculate for a prepayment or an accrual is not always straightforward – there may not be a bill with the precise amount. In cases such as these, estimates can be made. For example, if you haven't received the final quarter's telephone bill, you can make an estimate for an accrued telephone expense based on the previous quarter. And sometimes bills may need to be apportioned over a period of a year – for example, if your annual insurance covers your charity for nine months after the year end. A prepayment could be calculated as nine twelfths of the annual bill paid.

The examples of estimated prepayments, accruals and deferred income discussed in this section will probably only be required when you are preparing your annual accounts, and your auditor or independent examiner will likely be able to assist. Prepayments form part of the current assets of your charity, whereas accruals and deferred income will be classed as current liabilities where they fall due within 12 months. Some adjustments may not be required because of the concept of **materiality**, which is discussed in chapter 14. However, if your charity is preparing accruals accounts at year end, it is much less work if you keep your accounting system up to date at all times, with debtors and creditors properly recorded as explained above.

Fixed assets

R&P (or cash) accounting does not really account for the value of **fixed assets**, apart from showing the cost to purchase them as a payment. Fixed assets are those items that your charity uses to carry out its work, generally for a period of more than 12 months. They are split into four categories under the SORP (see chapter 14):

- **Tangible assets** include buildings, vehicles and equipment used in your charity's operational work.

- Investment assets, such as shares in an **endowment fund**, are held purely to generate an income to support your charity's work.
- **Heritage assets** are relevant to some charities and include things like paintings owned by an art gallery or artefacts in a museum.
- **Intangible assets** can arise, for example, in instances where your charity acquires some form of valuable intellectual property.

Accruals accounting requires the cost of an asset to be spread over the years in which it is used – this is generally known as **depreciation**.

As an example, let's say a charity purchased some computer equipment to carry out its work at a cost of £1,500. The trustees expect the equipment to last about three years and have no value at the end. If the charity were using R&P accounting, all that would appear in the accounts would be a one-off payment of £1,500 when the computer equipment was purchased. This would mean the charity had a high cost when the equipment was originally bought, but no cost at all in subsequent years, even though it was using the equipment to carry out its work. This might not be an issue for the charity, and it would be able to explain any high costs in a particular year as being down to the purchase of assets.

In contrast, using accruals accounting requires the cost to be recognised over the period the computer equipment is used – the £1,500 must be spread across the three years of the equipment's expected **useful life**. The first double entry reflects the initial purchase of the computer equipment, but, instead of being an expense for the year, it is **capitalised** as a fixed asset, as follows.

Debit: Fixed assets – computer equipment £1,500

Credit: Bank £1,500

This shows that the charity owns the asset – in essence the money at the bank has been swapped for another resource that the charity can use.

A second entry – probably made at the end of the year, when the accounts are being prepared – is for a depreciation charge to reflect the use of the computer equipment for the year. There are several depreciation methods available, perhaps the simplest being **straight line depreciation**. This method allocates the cost evenly over the useful life of the asset, so in this case the charity will charge one-third (£500) of the computer equipment's cost each year, as follows.

Debit: Depreciation charge (an expenditure account) £500

Credit: Fixed assets: accumulated depreciation – computer equipment £500

This has the effect of adding a cost to the accounts of £500 to represent the use of the computer equipment incurred. It also reduces the balance of the asset by £500 to £1,000, reflecting the fact that it is being used up. The same depreciation entry is repeated at the end of the second year and then again at the end of the final year. Each year reflects a cost of using the equipment (and the **accumulated depreciation** reduces the value of the asset). At the end of the three years, the computer equipment has been fully used, for accounting reasons, and there will be no further entries to show its use. The equipment can still be used in the charity, but it will no longer be necessary to reflect a cost of that use in the accounts.

This is a fairly simple example of fixed assets and depreciation to demonstrate the principles involved. There are more complex methods of calculating depreciation – for example, it can be carried out monthly rather than annually if a charity wants very accurate monthly accounts. Or you can use the **reducing balance method**, where a higher depreciation is charged in the earlier years, indicating how quickly the value of the asset decreases. But, as with other areas of accruals accounting, the trustees can use their judgement as to the method used, as long as it is applied consistently. Depreciation is also part of a much broader issue of **impairment** of fixed assets, and this will be covered further in chapter 14.

As the treasurer or finance officer, you will want to be able to identify the assets of your charity. It is quite normal to have a policy to treat something as a fixed asset only above a certain amount, perhaps £250 or £500 for a small charity; this is known as a **capitalisation limit**. You can write off the cost of all equipment purchased under this limit, when the purchase is made, so the full cost is treated as expenditure in the accounts. This gives the same effect as in R&P accounts. Any items above the capitalisation limit should be added to a **fixed asset register**. This acts as a record of all items your charity owns and helps the trustees to safeguard the assets as there is a full inventory. But it is also a document that can be used to record the purchase price of each asset, the date of purchase and how long it is expected to be used for. Each year the annual depreciation can be added, providing a record for the accounts.

Balance sheet

Debtors, creditors, prepayments, accruals and fixed assets all arise because of accruals accounting – they represent the balances owned, owed to and owed by a charity and they form the **balance sheet**, along with the balances on the various **restricted** and **unrestricted funds**. The format of the balance sheet for annual reporting is explained in more detail in chapter 14.

This chapter has introduced the approaches of R&P (cash-based) and accruals accounting as formats you can follow to maintain your charity's accounting records. As has been noted throughout this chapter, further details on the specific task of annual reporting under both the R&P and accruals (SORP-compliant accounts) approaches are detailed in chapters 13 and 14 respectively. A book of this size can only give an overview of accruals accounting; however, there are many general accounting texts available that, although they won't necessarily cover charity accounting, will cover accruals accounting concepts in more depth.

5 Risks and financial controls

Risk is usually thought of as a situation involving exposure to danger, loss or harm, or the possible negative impact of uncertain events. All **charities** face some degree of risk in carrying out their charitable activities – for example, loss of **donors** or key staff, cyberattacks, event takings being mislaid or even changes in government policy.

The responsibility of **trustees**, who are tasked with safeguarding the **assets** and resources of their charity, is to both identify potential risks and put steps in place to mitigate those risks that cannot be avoided. It is worth noting that, in some cases, uncertainty may result in a better result than expected, such as receiving additional funding or being able to support more beneficiaries; this is still risk to be managed. As the **treasurer** or **finance officer**, your role may specifically involve considering those risks that could result in financial loss to your charity and putting in place controls to prevent them.

Not considering any risk properly, regardless of whether it is financial in nature, could result in financial loss to a charity. The negative publicity of something going wrong can have a severe impact on funding and the confidence of supporters. In fact, cases of adverse incidents at high-profile charities, and even more local stories of treasurers embezzling money from their organisation, affect the public perception of trust in the whole sector. However, a book of this size cannot cover all risks; therefore, this chapter describes the more usual risks that a small or medium-sized charity may face – from both internal and external sources – and gives suggestions on how to assess and manage them. It then considers the types of financial control that can be adopted to prevent or reduce those risks.

Risks

Good risk management is an important part of effective **governance** (see chapter 2). It means that charities can carry out their services or projects, maximise their **fundraising** activities, and make informed decisions about opportunities and future planning knowing that risks have been considered. Importantly, it means trustees should be in a position to act quickly and with confidence when faced with an adverse situation. Larger charities (defined in the Charities **SORP** as those with annual income over £500,000) are required to include a risk management statement in their **trustees' annual report** (see chapter 12) to demonstrate that they have identified and addressed risks. One approach to risk management can be described in the following steps: identifying the risks your charity faces, assessing the severity and impact of those risks, and taking steps to manage them.

Identifying risks

There are various approaches to identifying the risks that your charity faces, and some trustees may follow a common tool used in business, called a PESTLE analysis. This framework involves considering all risks that may arise from political, economic, social, technological, legal and environmental perspectives. But such tools only act as a prompt to make identifying the risks more manageable. It is up to the trustees to identify those risks specific to their charity. A helpful approach to follow is that given in CCEW's guidance (CC26 – see the further reading, on page 313), which describes the five main categories of risk that a charity may face:

- *Operational risks* are those uncertainties your charity faces in the course of its normal activities. This is a wide-ranging area and depends on the specific activities of the charity, but it includes the risks involved in service provision, beneficiaries, employment and the charity's assets. Some examples include the risk of beneficiaries not being subject to appropriate safeguarding measures, a sudden increase in the number of beneficiaries, facilities not being fit for purpose, or staff not being appropriately recruited or trained.
- *External risks* are of two kinds. The first are risks that your charity experiences as a result of outside sources. An example is a change in local demographics or government policy, perhaps in relation to funding, or new legislation that prevents your charity from operating or introduces a change to charity tax legislation. You cannot necessarily influence those risks. The second kind of external risk relates to how the outside world perceives your charity, and this is an area you can influence. It includes the risk of adverse publicity and challenges in relationships with key stakeholders, such as **funders** and supporters.
- *Governance risks* relate to the overall control, structure and management of your charity. Examples include the risk that the trustees do not have the requisite skills and experience to manage the charity, that conflicts of interest are not dealt with appropriately or that the management structure prevents the charity working

effectively. For you as the treasurer or finance officer, a particular risk to consider here surrounds payments and benefits to trustees (see page 27).

- *Financial risks* are often thought of as the risk of losing money, such as theft or fraud, but financial risk is much wider than that. It includes risks surrounding funding – for example, the risk that a major funding source is withdrawn or that services are priced incorrectly, or that you receive much more money than expected. It involves financial planning – for example, the risk that cash flow issues mean suppliers cannot be paid, that there is no budgetary control or that **reserves** are inadequate. And it also involves security of financial assets, such as bank accounts and **investments**. The second part of this chapter looks at financial controls that can be used to address some of these risks.
- *Compliance risks* are those that arise from not knowing or following relevant legislation, even if unintentionally. As well as charity law and tax law, this includes, for example, data protection, employment regulations, and health and safety laws. Non-compliance with laws can lead to fines, reputational damage, and other serious consequences for your charity and trustees.

It is worth noting that even charities which have comprehensively covered the risks described above may not have considered the risks of something such as the COVID-19 pandemic and its impact. The lockdown restrictions forced many charities to cease their normal activities, which affected their means of income generation and use of premises and, for many, drastically affected their finances. Identifying the risk of such a serious event occurring and planning for it is known as 'disaster recovery planning'. Disasters also include scenarios such as fire or flood, or serious incidents involving your charity's computer systems. Your trustees should place a high priority on the impact on your beneficiaries if such a major event occurred, and consider how the charity could react and adapt to deliver its activities.

Assessing risks

Simply knowing a risk exists is not enough; it needs to be assessed to appraise how it affects your charity. This can be a very subjective exercise that requires a degree of judgement from the trustees to assess both how likely the risk is to happen and the negative impact it might cause if it did materialise. There are no right or wrong answers to these questions. Trustees may want to consider the views of staff, examine past events or experience at your charity, and draw from the local community or the sector in which your charity operates.

One method often used for quantifying this assessment uses a sliding scale – perhaps ranked from 1 to 4. For example, the likelihood of a risk happening can be assessed from highly unlikely (1) to very likely (4). And the impact on your charity of each risk happening can be quantified from little impact (1) to severe impact (4). Multiplying these rankings together (likelihood × impact) results in a risk rating, in this case from 1 to 16. If a risk is given the rating of 1, it means it is unlikely to happen and, if it does, it will have a minimal impact on the charity. On the other hand, a risk rated as 16 is highly likely to happen and will have an extreme impact if it does. Figure 5.1 shows this tool as a risk map. There are more complicated ways to measure risk, such as larger scales and more involved calculations, but the main purpose of all these methods is to highlight where action needs to be taken.

Likelihood of risk happening		**Impact on the charity if the risk were to happen** Little impact 1	Moderate impact 2	Major impact 3	Severe impact 4
Highly unlikely	1	1	2	3	4
Possible	2	2	4	6	8
Probable	3	3	6	9	12
Very likely	4	4	8	12	16

Interpreting the score:

1–3	Minor risk
4–8	Moderate or major risk
9–16	Extreme or catastrophic risk

Fig. 5.1 An example of a risk map that can be used in assessing risks

Managing risks

Once risks have been identified and assessed, the next question is how to deal with them. There are three broad options: avoiding the risk, mitigating the risk in some way or accepting that it may happen. Avoiding a risk tends to mean just that: not taking up an activity that gives rise to the risk or perhaps changing a process that gives rise to the risk. However, even if a risk has been identified as highly likely to happen, it is often not possible to avoid it completely, although it may be feasible to mitigate the risk and bring it to a more acceptable level. Common ways to mitigate risk are by taking out insurance, sharing the risk by outsourcing the activity that carries the risk to a third party, or working in partnership with another organisation to share the impact of the risk by pooling resources. The final strategy, accepting the risk, does not simply mean ignoring the risk, but instead adopting policies, procedures and controls that enable the risk to be managed, even if it can't be directly mitigated.

It may be helpful to consider an example to examine how these three strategies work in practice.

Risk example

A charity is offered some funding to deliver a new project that falls within its charitable aims but will take up a significant amount of staff time and require additional skills that the charity doesn't have. If the project is successful, it could lead to a fantastic new resource for the beneficiaries. But, if it fails, it will damage the reputation of the charity and could lead to withdrawal of other funders and staff leaving.

The risk of not being able to deliver the project has been identified as operational. The risk has been rated as significant: the likelihood of the project failing has been identified as probable (3) and the impact on the charity of the project's failure as severe (4). This gives a risk rating of 12 – on the higher end of the risk scale (extreme or catastrophic). What strategies could the trustees adopt in deciding whether to accept the funding?

- *Avoidance*: The trustees may consider that, despite the potential benefits the project may have, they do not have the resources and experience available to fulfil the terms of the contract, and so the risk of the project failing is too high. To protect the charity, its resources and beneficiaries, the trustees will decline the funding. Although a charity turning down funding which meets its charitable aims may seem unusual, if the trustees have significant concerns that the project is not achievable, this is the best course of action.
- *Mitigation*: The trustees may consider that the potential benefit of the funding and project is too good an opportunity to turn down. However, they know that they cannot fulfil the project with their current staffing levels. There is a similar charity operating locally, and between them they have the resources to fulfil the project. The trustees would need to confirm this is possible with both the funder and the other charity, and draw up an appropriate partnership agreement to determine the terms of the project, but this option lessens the risk significantly. In fact, with the partnership in place, the trustees consider the likelihood of non-delivery of the project to be 1 (highly unlikely). The impact if the project cannot be delivered remains at 4 (severe), but now the overall risk rating is only

4. By mitigation, the trustees have reduced the risk to a satisfactory level and can accept the funding.

- *Acceptance*: The trustees believe the funding and project are a positive way forward for the charity, but they are aware of the possible shortage in staff resources and lack of skills. The trustees can divert resources from other work in the short term, obtain training to provide existing staff with the skills needed and have a recruitment drive. They will need to review their charity's existing policies and controls but are confident they can deliver the project. With this approach, the trustees consider the likelihood rating of not being able to deliver the project as 2 (possible). The impact on the charity of the project failing remains at 4 (severe), but now the overall risk rating is 8 (moderate). With this choice, the trustees have made the decision to accept the risk as there are appropriate measures in place to manage the risk of non-delivery.

This example demonstrates how understanding the risks involved with a specific course of action can help to inform decision-making. It may not be a straightforward decision and there may be many possibilities to consider in detail. After examining the options, the outcomes of such decisions depend not only on what can be achieved but also on the risk appetite (the willingness to accept risk) of the trustees making the decision. This highlights that there is not one correct way to address risk and that there are several feasible outcomes for a particular situation.

You may hear the term **risk register** in the context of recording risks. In essence, this refers to the tool used for recording those risks that have been identified, and documenting the assessment made and the steps to be taken to mitigate each risk. Although commercial risk register tools are available, simply recording the information in a document – either digitally (more usual) or on paper – is sufficient. The important point is to refer to the information on a regular basis.

Risk management is not a one-off exercise. As activities and processes evolve, the associated risks change. Any new project involves some degree of risk assessment, and it is advisable to have a cyclical approach to monitoring all risks and actions to mitigate them. The results of a risk assessment should be communicated appropriately to staff and/or volunteers, and training should be provided where necessary to ensure any actions put in place to mitigate risks are both understood and capable of being followed.

Financial controls

Financial risk, as introduced in the previous section, covers a broad spectrum of areas, such as loss or misuse of charity funds, security of bank accounts, financial planning and funding considerations. The way to mitigate the risks in all of these areas is with financial controls.

Financial controls are policies and procedures that minimise the risk of financial loss from theft, fraud, human error, unforeseeable circumstances and even bad management decisions. Sometimes you may see them described as internal controls or **internal financial controls**. They do not eliminate financial risk entirely, but they reduce it and act as an early warning sign to trustees to help them identify an issue and take action. Financial controls do not need to be complicated to be effective, but they must be followed. CCEW guidance on internal financial controls (CC8) includes a link to a checklist that you can use to review the controls you have in place against good practice.

Charities customarily use various controls to monitor their financial activities – to make sure things are going to plan or are as expected, and to flag anything that does not look quite right or may need to be investigated. Budgetary control is a good example. Trustees should set a realistic **budget** (estimates of income and expenditure) for the year. Chapter 6 looks at budgeting and other financial planning tools that can help you manage and monitor financial performance.

As a treasurer or finance officer, you will be expected to monitor the actual income and expenditure against the budget on a regular basis to enable the trustees to see whether things are going to plan and ask questions where there are differences. If income is lower than projected, is there a reason? For example, will some funding be received later than expected, was a fundraising event poorly attended or is there another reason for a drop in income that needs to be investigated further? On the other hand, if costs are higher than expected, has the additional spending been discussed and approved? It is recommended that this degree of monitoring is carried out individually across each **fund** – **restricted** and **general funds**. Charities may fail to realise they are in serious difficulty if they consider their results as a whole. For example, a negative balance on the general fund may be masked due to a **surplus** on a restricted fund.

Other common financial controls act as preventative measures – to stop things going wrong in the first place. Examples include controls to stop unauthorised spending or access to the charity bank account, or to provide assurance that all income due to the charity is accurately recorded and banked quickly. As tasks are usually carried out online – such as emailed invoices and online banking – it is also essential to take steps to protect against the threat of cybercrime.

Apart from the risk of fraud, errors can happen – or, if no one asks to see the books, it is easy to get behind and make mistakes. It therefore makes sense that, when taking on the role of treasurer or finance officer, you ensure there are procedures in place to keep everything on track.

The following subsection considers the general topic of honesty, and then the remainder of this chapter explains some practical options that a small or medium-sized charity with minimal or no staff can put in place as preventative financial controls.

Honesty

Sadly, charity fraud or theft happens more often than might be imagined. When it does happen, the impact on the charity and those involved can be great. Even trustees completely innocent of carrying out the fraud or theft will be questioned as to why better controls were not in place to prevent it from happening. Charities tend to be vulnerable to financial crime because of their voluntary nature and position of trust, making them a target for people who want to divert charity funds for their own gain. This can be from external sources, such as someone using your charity profile to raise funds illegally or an email scam pretending to be from a supplier and requesting you to change your record of their bank details. But often it results from one person within a charity having free rein over the charity's bank account or cash tins, and from other trustees placing too much trust in that person.

As the treasurer or finance officer, you will be that person in a position of trust, sometimes with unchecked access to the entire finances of your charity. It might be that the role you have taken on already comes with good controls in place; however, sometimes, especially for small charities, it will not. To protect yourself, as well as your charity, one of your first tasks as treasurer or finance officer should be to review what controls are in place and make sure they are suitable and comply with good practices such as those set out in this chapter.

Even with all checks in place, no system can be absolutely secure. It is good practice to ensure that trustees and staff, particularly those involved in the finances of a charity, are honest and dependable. References should always be taken for staff as part of recruitment procedures (see chapter 11). Not all charities, especially the smaller ones, take references for trustees, although it is becoming common practice for some charities. If someone relatively new to the charity volunteers to be the treasurer, especially where they would have sole control of the cash and banking records, it is probably a sensible idea to ask about their background and experience and take a reference.

As discussed in chapter 2, it is also good practice to require a new trustee to self-disclose any previous criminal activity, and some trustees may be asked to undertake DBS checks (Disclosure and Barring Service, for England and Wales; Northern Ireland also uses DBS checks but via Access NI) or PVG checks (Protecting Vulnerable Groups, for Scotland). However, these checks may not be required unless your charity is working with children or vulnerable adults. In any case, such checks are of no use unless the trustees have a clear policy as to how the results will be considered.

Some treasurers may feel affronted that they have been asked for a reference or to undertake checks, as there is an assumption that honesty is fundamental to volunteering in a charity and that this makes such independent verifications unnecessary. But it is unlikely that anyone with treasurer experience would object, as they are likely to appreciate the need for diligence.

Security of bank accounts, credit cards and cash

Your charity will need at least one bank account. For older charities which have not updated their bank accounts recently, this will often still be managed in paper form, using a cheque book and a paying-in book (to make deposits at the bank), and with the regular receipt of bank statements. However, many charities have made the move to online banking, and most new charities are likely to start off with an online bank account. Online banking can be much more efficient to operate but can have challenges from a control point of view, the most common issue being that some accounts do not allow for **dual authorisation** – where two people are needed to either countersign a cheque or authorise an online payment (dual authorisation is explained more fully later in this chapter, on page 98). The importance of dual authorisation is demonstrated throughout the controls discussed in this chapter. Whichever way your charity bank account is managed, there are some important controls to put in place to ensure the security of your charity's financial assets.

Controls to ensure your bank account is fit for purpose

Ensuring your bank account is fit for purpose includes making sure your charity holds its account with a reputable bank and that it allows dual authorisation. Most high street banks offer charity-specific bank accounts, often with no fees if the bank balance is under a certain amount. There are also charity-specialist banks available. Some hints and tips on opening a charity bank account are provided in the 'Additional notes' section of this book (see page 300).

It is worth noting that under the Financial Services Compensation Scheme, deposits in UK bank accounts are protected up to £85,000 if the bank or building society fails. The £85,000 refers to the institution and not the account; therefore, if the total of your accounts with one bank is regularly over this amount, it may be worth holding a **deposit account** with a different bank, or even investing your funds in another way to bring in **investment income**.

Controls to ensure your bank mandate is up to date

Your bank mandate should reflect your current list of trustees (and anyone else authorised to deal with the bank). Banks usually require all trustees to be named on the bank mandate, but not all trustees have to be bank signatories (i.e. be able to sign a cheque or authorise a payment). Banks should be informed when trustees change, and this is particularly important for those trustees who are signatories. You should be aware that banks often take several weeks to update mandates, so having three or four signatories can be beneficial to meet your banking needs in periods when signatories change. There is a risk, especially on bank accounts that are not used very often, that if trustees are not updated regularly, your charity will find itself without the means to access its bank account, unless you can contact the previous signatories.

If your charity employs staff, it may be sensible for your **charity co-ordinator** and/or finance officer to have signatory access to the bank account to be able to make or approve payments. But care should be taken that an appropriate authorisation procedure is set up (see page 98). As well as adding new trustees and signatories to the mandate, you should remove the details of anyone leaving your charity as soon as possible to prevent unauthorised access to your charity's funds.

Controls to prevent unauthorised access to your bank account

Only authorised persons should have access to your bank account. This includes not only who can access the bank account itself but also the security surrounding cheque books and bank cards linked to the account. It is usual for an online payment to need two signatories – one person to set the payment up and one to authorise – or for charity cheques to require two signatures. In case of a signatory being unavailable, it is practical to have an alternate, hence the three or four signatories recommended in the previous section.

For online banking, signatories should use their own individual login details, and these should never be shared. Anyone with a bank login is responsible for keeping those details and passwords secure. They should also be aware of computer security, such as not leaving bank access open on a computer terminal used by others and identifying potential bogus phishing emails pretending to be from banks.

It is becoming more common to access banking apps on tablets or phones. In fact, some trustees may not have a computer at home and rely on mobile devices for their personal banking. If, as a charity, you are going to allow the use of a banking app, it would be appropriate to request that any device it is installed on has strong security access controls. This refers not only to the banking apps themselves, which often have biometric sign-ins if enabled on the device, but also to opening the phone or tablet itself.

Where cheque books are used, they should be locked away and accessed only by the signatories or those with authorised access. Under no circumstances should cheques be signed (even by just one signatory) in advance of the details being added, such as the payee and amount.

Controls to prevent unauthorised access to your debit and credit cards

Your charity may be eligible for a business credit or debit card, which approved staff members or trustees can use to pay for certain items of expenditure. With debit cards, the payment is taken straight from your charity's bank account, and with credit cards, you will receive a monthly statement with a balance to pay at a later date. However, in both cases, at point of purchase the payment is made unilaterally – there is no second person authorising the payment. For this reason, there should be a clear policy on who can use a debit or credit card on behalf of your charity, and procedures should be followed when payments are made (see page 96 for more information on payments). Credit and debit cards should preferably be kept in a secure location when not in use, as it is very easy for someone to use them online or for small amounts using contactless technology without needing second-level security, such as the PIN number. More than one person (and perhaps even the trustees) should approve any applications for additional credit cards.

In practice, nowadays so many online purchases have to be paid for by card that it is very hard to run a charity without a credit or debit card. But their above-mentioned limitations – principally the lack of dual authorisation – makes it easy for them to be abused by dishonest staff or trustees or unintentionally used inappropriately through a misunderstanding of what is a valid expense for the charity. Improper use of credit or debit cards can result in charity fraud – for example, people charging personal expenses to the charity or even drawing cash for purposes unconnected to the charity. Sometimes the culprit is the treasurer or finance officer.

When anyone makes a purchase on a credit or debit card, the treasurer or finance officer still needs a copy of the receipt to verify the payment, and this must be filed with your charity's **accounting records** so it can be reviewed by your charity's **auditor** or **independent examiner** at year end. It can help to have an agreement with your bank limiting the maximum payment allowed on a card.

However, waiting for a year-end review is not sufficient to prevent fraud. In order to ensure that improper card payments are spotted promptly, it is vital that expenditure on credit and debit cards is checked every month by someone other than the cardholder. It is likely that you will check a credit card statement when it is received for payment and ask another trustee to approve the payment before it is made. However, in the case of a debit card, where payments are charged directly to the charity's bank account, that additional check is not made. This means that if the treasurer holds the payment card, another trustee should be regularly monitoring the bank statement. It may be better for the treasurer *not* to be a cardholder, so they can take responsibility for scrutinising card use by others.

Controls to ensure the security of your petty cash

If your charity holds petty cash – for example, to meet everyday spending needs such as buying milk or stamps – or holds regular balances of cash from **donations** or fundraising events, there should be proper controls to ensure its security. Controls over making cash payments and receiving cash income are covered in the next section. Financial controls over the security of the cash itself include keeping the cash held to a small amount and storing it in a locked petty cash tin within a locked drawer or safe. You should have a written record of the cash balance at all times, with an entry made when cash is deposited in the tin or used to make a payment. The balance of the cash should be counted regularly, preferably by two people or someone different from the person who holds the petty cash, and checked back against the record. Any differences should be investigated to ensure there has been no unauthorised use of the funds.

Payments

Payments made by your charity should be in line with your charitable aims and, where appropriate, in line with any restrictions imposed by funders (see page 36 for information on restricted funds). Your role as treasurer or finance officer will be to avoid unauthorised expenditure.

This means payments that are not in line with the charitable activities of your charity and/or with expenditure that the trustees have authorised. Therefore, there need to be clear and robust procedures in place for approving and making day-to-day payments.

Controls to ensure payments are in line with your charitable aims and any restrictions

People responsible for making payments must be aware of the parameters of your charity's spending, and no one should be able to make a payment on your charity's behalf without some form of authorisation. In a small charity with no staff and minimal spending, it may be that all of the trustees agree the payments to be made. When the frequency of **transactions** increases, this is not practical, and if running the day-to-day operations of the charity is delegated to staff, they also need to know what they can spend.

In fact, expenditure should be controlled before the payment stage is reached – staff and trustees need to understand what expenditure they can commit their charity to. Financial planning will act as a guide to what type of spending can be made. This can include details of expenditure outlined in successful funding applications or set out in the trustee-approved budget. Any large one-off items, or anything that is not covered within the budget, can then be put to the trustees for additional approval. Ongoing commitments (such as for a rental agreement or IT support) and any requests for pay rises or new contracts of employment should require formal trustee approval.

If your charity has multiple staff members, you should define who can commit the charity to expenditure, perhaps with all spending requests coming through a central point. Where clear written and briefed guidance is in place, it is possible to sanction disciplinary action if a member of staff deliberately incurs expenditure outside these rules.

Of course, such controls need to be reasonable: it is often appropriate to delegate authority to individuals to agree expenditure up to certain levels where it falls within agreed budgets. But this does not mean staff are free to spend whatever they wish provided the budget isn't exceeded: at all times a charity needs to avoid wasteful expenditure.

Controls to ensure your charity is receiving the best value for money

Trustees are required to act with care and diligence over charity funds, which includes ensuring the cost and quality of goods or services are appropriate. For small purchases, this may be as simple as only using a recommended list of suppliers. However, for larger items, it may involve shopping around. It is good practice to put any large services out to tender. In practice, this means obtaining quotes from a few different suppliers. At least three quotes allows for a suitable comparison; with only two quotes that are wide apart, it may not be possible to tell if a supplier has misunderstood the brief. The lowest cost is not always the best option, so it is helpful to have a criteria list to use to carry out a thorough comparison and record the decision reached. There are all sorts of situations where you might find a tendering process useful, depending on the activities of your charity, but a common one is for the provision of **audit** or **independent examination** services.

Dual authorisation

Dual authorisation means that at least two people are required in order to make a payment on behalf of a charity. It is a basic requirement expected by the **charity regulators** (for example, as set out in CC8, CCEW's guidance on financial controls; see the further reading, on page 313), but it is also often imposed by funders as a condition on awarding **grants**. However, the actual arrangements of how it is carried out may differ between charities, the types of payment made and any requirements from the banking provider.

Most bank accounts designed for charities will always require more than one signatory per payment, regardless of value – for example, two people to sign a cheque or, for online banking, one person to set up the payment and a second to approve it before it is released (though, as noted above, it may be necessary to use debit or credit cards for smaller items). In a charity with no staff, the signatories will always be two trustees. However, as previously mentioned, it is sensible to have at least three trustees named as authorised signatories in case someone isn't available. Where a charity has staff, it will probably be practical to have at least one staff member as a signatory (in addition to the trustee signatories), and often two, with a payments policy in place.

An example of a payments policy for a charity which has a small staff team and online banking could be that all payments up to £500 are set up by one senior staff member and approved by another, whereas payments over £500 are set up by a senior staff member and approved by a trustee. However, you should check whether there is a requirement in your **governing document** that states 'all payments must be authorised by two trustees' – if this is the case, you must keep to it. This requirement may become cumbersome in the event of your charity growing, and a change to your governing document may need to be considered.

It is best practice that all payroll payments are approved by a trustee. In some cases, these may be set up by someone in the charity, but many charities pay salaries by **BACS**, especially when using a payroll outsourcing service. This is often the largest single area of expenditure each month, so it does require careful approval and at least one trustee should sign the transfer mandate – further details on employment are given in chapter 11.

In some instances, it may be necessary for a staff member or trustee to make a payment using their personal finances and claim this back from your charity as an expense. This is perfectly acceptable, but it is recommended to have an 'expense claim form' for individuals to complete, so you can keep track of payments. The claim form should fully list the purchases on behalf of the charity and have related receipts attached. It should be signed by the claimant and approved by a senior staff member or trustee before payment is made.

It is important to note that the person approving the bank payment, or the second signatory on a cheque, is not there just to add their name; they are a vital check, not only against potential fraud but also for accuracy. As mentioned above, pre-signing cheques should be avoided, and simply signing a cheque or marking an online payment as approved with no real thought offers no protection at all. If you are authorising the payment, you should be considering:

- Have you seen the bill or invoice and is it as expected?
- Is the payment in line with what the trustees have approved and the budget?
- Do you know which fund the payment is being made from and is it appropriate?
- Are all the details on the payment accurate – the amount, payee and bank account details? This is especially important for online payments (see the section below on cybercrime on page 108).
- Have you already authorised a payment for the same item? Some frauds rely on making payments twice and then diverting the second payment. If you are not the only signatory approving payments, this may mean checking back over other payments.
- Are salary payments in line with the payslips or payroll reports, and are they being sent to the correct employees at the level of pay expected? It may be that expenses are included in the salary payments, or someone has worked extra hours, but it is always worth checking, as payroll fraud, such as setting up a fictitious employee or making unauthorised pay rises, does happen.

- If the cheque is for petty cash, has the previous petty cash been spent appropriately? And is the top-up amount being asked for reasonable? If your charity regularly takes out petty cash to reimburse expenses paid by employees or trustees, are expense claims checked and could there be a better way for the system to work without the need for regular cash transactions?

Income

Although often overlooked, it is just as important to have controls over income as it is for payments. There are two main risks: charity funds being diverted elsewhere and accepting funding that is not appropriate for your charity. Trustees should be aware that they should not simply accept any income offered to their charity without appreciating any implications it brings. There may be ethical decisions to make over how the money is raised or the actual source of the funding. Or funding may be offered with obligations that your charity cannot meet, perhaps because they don't align with your charity's aims or may cost your charity too much to deliver (see the section on acceptance of gifts on page 143).

For charities whose income only relies on grant or **contract** income, the situation is fairly straightforward: as long as the trustees approve applications in line with best practice (as set out in chapters 6 and 7) and ensure each grant or piece of contract funding has actually been received, the main issue is controlling the expenditure. However, when funded by other income streams, charities can be particularly vulnerable, especially to the possibility of donations or fundraising money going astray. Therefore, you will need further controls to be adopted to ensure your charity receives all money meant for it.

Controls to ensure your charity receives donations paid directly to your bank in full

Although you may not know when or how a donation will be made, there should be procedures in place to minimise any loss. Requesting donations to be paid directly into your charity's bank account by bank transfer or through donation websites and applications may minimise the risk of funds being diverted. However, you will need to ensure all bank details sent out and donation links are accurate and work. A serious case of fraud could involve a dishonest staff member, treasurer or other trustee opening an additional bank account in your charity's name that only they can access, and no trustee or auditor knows about, and diverting money meant for your charity through that account.

Some donors will contact your charity when they make a donation, or perhaps if they do not receive a thank-you letter or receipt. This can be a good check against what has been received. Not all donors will expect such a communication, though, especially if they assume your charity is saving administrative costs by not sending such receipts. Additionally, a dishonest employee or trustee could go as far as creating a fake acknowledgement. Therefore, this is not an absolute check.

Controls to ensure your charity banks donation cheques in full

It is still popular for some charities to receive cheques in the post. Ideally, post should be opened by two people working as a team to open and record any cheque donations. If it is not practical to have two people opening the post, perhaps try to vary the person and make spot checks. The record of cheque donations will be helpful as supporting documentation for your banking records as well as a reminder of where to send thank-you letters. Banking should be carried out regularly. There could be a risk if the donor has not written your charity's name in full as it would not be too difficult for someone deceitful to alter the payee name and pay the cheque into a personal account, so you should regularly match the income in your bank to the list of cheques received.

Also, make sure that anyone who is preparing appeal letters or applying to grant-making charities is only permitted to use your charity's official address when stating where cheques should be sent. Otherwise, there is a risk of someone asking for cheques to be sent to a personal address and those cheques then being banked into an account not under your charity's control. If your charity has no premises of its own, it will be impossible to give an official address. In this situation, the address used on appeals should be that of a trustee with impeccable standards of organisation who will carefully log and bank cheques promptly. Avoid using anyone with a shared letterbox.

Controls to ensure your charity receives cash donations in full

Cash donations remain common for some charities – for example, collections at religious services or community events, or cash donation tins in public places or on shop counters for spare change. Cash poses the greatest risk for diversion of funds. As well as ensuring security of cash tins and making sure they are emptied regularly to minimise the risk of theft there should be strict procedures over counting and banking cash. Whenever cash is counted and recorded, at least two people should be present to verify the amount. For on-the-day collections, try to ensure that the money is within sight of at least two independent people from the moment it is given until it is counted and signed for. Collecting boxes should have a seal, and a clear rule that there must be two people present when the seal is removed and the box opened. Banking of all cash donations should be done as soon as possible, with the receipts showing in the bank reconciled back to the count records.

Controls to ensure your charity receives fundraising income in full

Charities often receive the bulk of their income from fundraising activities rather than ad hoc donations. The receipt of income from these activities – direct to the bank, by cheque or by cash – will follow the same procedures as for any other donations. However, when the income is in response to a particular event, there may be additional information you can use as a guide to when and what income should be expected. For example, using the number of sponsorship forms or tickets, you should be able to calculate how much is due to your charity and follow up any money that is slow to come in or is less than expected. Many fundraising events now rely entirely on online ticket sales, which reduces the risk of ticket income not reaching the charity. But it is vital to ensure that whoever sets up the online platform does so on the basis that revenue goes directly into the charity's own bank account.

Controls to ensure your charity receives other income in full

Some charities may charge a **fee** for their services or carry out other activities to make their income more sustainable (see chapter 6). If your charity does undertake such activities, you should follow a businesslike approach and ensure invoices or similar are sent out quickly, with non-payment always being followed up. Many off-the-shelf accounting packages have in-built solutions to make this process straightforward. Some treasurers or finance officers may feel uncomfortable following up late payers, especially for fees for services; it can be helpful in this instance to have a scheme in place to help users who are genuinely having difficulty meeting the fees. You should also be aware of grants or contracts that are paid in instalments, or on submission of a monitoring form or invoice, and make sure any necessary paperwork is submitted on time.

Verifying the books

Controls over payments and income are necessary to protect your charity's funds, but it is also necessary to have controls in place over recording transactions. **Bookkeeping** procedures (see chapter 4) are only useful if they mean that the books and accounts properly record all income due to the charity and all expenditure agreed by the trustees. The annual scrutiny of your year-end accounts by an auditor or independent examiner (see chapter 15) will provide some comfort that this is happening. However, auditors and examiners do not set out to detect minor frauds and do not check each transaction. Instead, they consider the processes and controls in place, examine how they are working and test a few transactions. It is down to the trustees to ensure they have proper checks in place, and to the treasurer or finance officer to be confident that the books are accurate.

Simple checks, such as bank and cash reconciliations, can be made throughout the year, perhaps at each month end. These can help you to pick up problems in the books, whether caused by fraud or the occasional mistake, and mean any issues can be addressed sooner rather than later. As well as detecting and preventing potential financial losses, such checks will improve the quality of your financial information, making it more reliable as a basis for managing your charity and decision-making.

Bank reconciliation

A bank reconciliation is the most important check you can make on the books. It could be carried out every time a bank statement is received or at each month end. A bank reconciliation does not prove everything in the books is correct (there still may be errors over where transactions have been allocated), but it does provide a strong confirmation that what has physically gone through your bank corresponds to the entries in your accounts. A bank reconciliation will be needed for each account your charity holds.

The term ‘reconciliation’ is used because the balance in the books may not exactly equal the balance on the bank statement – there may be reconciling items. There tend to be two main types of reconciling item: an uncleared payment and an uncleared lodgement (deposit).

An uncleared (or unpresented) cheque occurs when a cheque has been written but not yet cashed by the payee. For example, you have written a cheque for £200 to an activity provider on 28 March, but they do not pay it into their bank until 12 April. Your books on 31 March would include this payment, but the bank balance on the same date would not – it would be £200 higher as the money had not been paid out of the bank. With online banking, the issue of uncleared payments tends to be reduced; however, it can still happen if you have set up a payment for a future date, or if there has been a time interval between setting up and authorising a payment, but it has already been reflected in the books.

On the other side, an uncleared lodgement is a deposit of income that you have already entered in the books but that has not been paid into or cleared by the bank yet. For example, you have included the income from a coffee morning in the books but have not yet been able to visit the bank and physically deposit the cash. In this case, your books will show a higher balance than your bank statement.

If you use accounting software which automatically brings in bank transactions, as long as you allocate every item of income and expenditure, the reconciliation is effectively carried out on an ongoing basis and the bank balance in the accounting software is always equal to the bank statement balance. But you should always check they are actually the same to ensure nothing has been missed or allocated to the wrong account.

If the software doesn't bring in transactions automatically, or you keep a manual cash book, you need a means of marking in your books when each item has cleared the bank – often a tick against the entry in the books and the corresponding item on the bank statement (accounting software often has a function for this). Any unticked entry in either the books or the bank statement will be a reconciling item. Using the total of all the uncleared cheques and uncleared lodgements, and the balance on the bank statement, you should be able to reconcile back to the balance in the books, as shown in figure 5.2. Note, if you do not keep a running balance for the bank in your cash book (see chapter 4), it may require a bit more work to determine what your books show as the bank balance.

Bank reconciliation: current account 31 December

Balance on bank statement at 31 December			£ 1,908.11
Less uncleared cheques			
	001105	£ 35.76	
	001107	£ 120.00	
		£ 155.76	–£ 155.76
Plus uncleared deposits			
	075	£ 225.00	£ 225.00
Expected balance in books			£ 1,977.35
Actual balance in books			£ 1,977.35

Fig. 5.2 Example of a bank reconciliation

If the expected balance from the calculation ties up to the bank statement, this is a good confirmation that all entries are included. Bank reconciliations should balance to the penny. Any discrepancies between the two should be followed up. One way to find the potential errors is to calculate the amount of the discrepancy and look for that amount in the books. Any difference will result from one or more of the following:

- A payment or receipt has been marked as cleared in error and it has not actually gone through the bank.
- A payment or receipt has not been marked as cleared but it has already gone through the bank.
- An item on the bank statement has been completely missed from the books (this is especially common with automatic bank entries, such as charges and interest, transfers, and standing orders and direct debits).
- An item has been entered into the books more than once and marked as cleared against the single item in the bank statement.
- An item has been entered the wrong way round in the books – for example, a receipt entered as a payment or vice versa (in this case the discrepancy on the reconciliation will be twice the amount of the item).
- An item has been entered incorrectly in the books – for example, £32.60 entered as £32.90, or perhaps a transposition error of £25.70 entered as £27.50 (a transposition error can often be identified as the cause where the discrepancy divides by nine – the difference between these two numbers is £1.80, which divides by nine).
- An item has been allocated to the wrong account in the books (if you have more than one bank account).
- There is a calculation error in adding up the balance in the books.

Sometimes the discrepancies can be found without too much trouble, but sometimes, especially if the reconciliations are not made frequently, you may look back over months of transactions and find there are several errors.

Petty cash reconciliation

When it comes to petty cash, the main control is to verify the balance in the books with the physical cash held. Physical cash should be counted regularly (as noted earlier in this chapter), and the counted balance checked back to that recorded in the books. If the counted balance is less than that in the books, it is likely a cash payment has been missed – is this an oversight and a receipt has been missed, or has someone taken petty cash without authority? On the other hand, if the counted cash is higher than in the books, it could be that someone has made donations or popped spare change in the tin without making a record. This is not good practice, as it reduces the control you have over the petty cash – all donations should be recorded.

Income, expenditure and fund account reconciliations

Unlike with your bank and cash accounts, it is not possible to reconcile the income, expenditure and fund balances recorded in your books with anything physical. The main test that can be carried out is one of reasonableness; for example, does the income you are showing in the books correspond to what you are expecting? Or is the balance on the outreach fund where you thought it would be? This is where budgets help – you can compare the actual results in the books to the budget you have set. If there is a large difference, can you explain it? It may be that something has cost more than expected or that income is less than you have budgeted, but it may also be worth checking in the books that items have been allocated to the right account and fund.

If your charity has multiple funds, it is particularly important to regularly check that items have been allocated to the correct fund, otherwise restricted funds may be used for the wrong purposes (see chapter 3). Generally, mistakes with one-off expenses are easy to identify, but you may need to carefully consider whether correct allocation has been made for someone's salary to a particular fund. If misallocation occurs over a number of months, the balance on the fund could be significantly misstated, so it is helpful if you can pick up these errors at an early stage.

Controls over subgroups' records

Some charities have projects or subgroups (such as lunch clubs or flower funds) that handle their own money and books on a day-to-day basis but are legally part of the main charity. All the risks and controls noted in this chapter apply equally to the subgroups. Therefore, as a treasurer or finance officer responsible for the charity as a whole, it is important that you ensure the same controls are implemented throughout any subgroup.

The accounts from the subgroups will need to be included with those of the main charity to produce the year-end accounts. At year end, you may want to give each subgroup treasurer a form to return to you – see figure 5.3 for an example. These figures can then be included into the books of the main charity, treating the subgroup as a separate fund and creating an additional bank account or petty cash account in the charity's books for the amounts held by the subgroup. If the main charity provides financial support to the subgroup – line (3) – or if proceeds are transferred from the subgroup to the main charity – line (6) – then, although these are seen as receipts or payments from the perspective of the subgroup, they need to be recorded as **inter-fund transfers** in the accounts of the charity as a whole in order to ensure that income or expenditure is not counted twice.

Once a subgroup has been operating for more than a year, a crucial but simple check is to be sure that the opening balance of the second year agrees with the closing balance from the previous year (refer to chapters 4 and 12–15 for transfers between accounts and year-end reporting). However, it is best practice to review the subgroup's books and figures on a more regular basis than only at year end, both to check that controls and procedures are being followed and to ensure there are no surprises at year end.

For trading subsidiaries that are separate legal entities of the charity, the results for the year may need to be included into group accounts through an accounting process known as **consolidation** (see chapter 10).

NAME OF CHARITY

Name of subgroup: ....

Year ending: ....

(1)	Balance of funds at start of year: (cash in hand + bank)	£...........	
(2)	Receipts from external sources:	£...........	(give details)
(3)	Contributions from main charity:	£...........	
(4)	Total receipts:	£...........	(2)+(3)
(5)	Payments made to external sources:	£...........	
(6)	Proceeds transferred to main charity:	£...........	
(7)	Total payments:	£...........	(5)+(6)
(8)	Balance of funds at end of year: (cash in hand + bank)	£...........	
(9)	Check calculation:	£...........	(1)+(4)−(7)

If lines (8) and (9) are not equal, there is an error in your books – please explain.

I confirm that records have been kept of the above items, which can be made available to the charity's auditor or independent examiner on request.

Signed (subgroup leader) ....

Fig. 5.3 A form that could be used for a subgroup to submit records to the overall treasurer or finance officer

Cybercrime

Adopting strong financial controls can help to reduce the risk your charity faces from unintentional errors and fraudulent activities, especially from internal perpetrators. However, with the increasing use of digital technology, charities are at an escalating risk of malicious cyberactivity – normally instigated by external fraudsters. The methods fraudsters use change all the time, often in line with working practices or global conditions. For example, the COVID-19 pandemic saw a spike in purchase fraud relating to personal protective equipment and a rise in email impersonation fraud, as home-working practices became commonplace.

As the treasurer or finance officer, being aware of some of the cybercrime practices may help you to prevent your charity from falling victim to such scams. The National Cyber Security Centre (NCSC) (www.ncsc.gov.uk) is a good source of guidance around the various threats that organisations face and of tools that you can adopt to help reduce the risk. It is not possible to cover all forms of cybercrime in this book, and they constantly evolve, but some risks to consider include malware and ransomware, impersonation fraud and phishing attacks:

- *Malware* is software that finds its way into computer systems and records. It is designed to disrupt and damage, or gain unauthorised access to, your data and systems.
- *Ransomware attacks* involve malicious software blocking access to your data and systems unless a sum of money is paid. Many charities hold sensitive data relating to their beneficiaries and therefore can be targets for such attacks.
- *Impersonation fraud* involves a criminal pretending to be a trusted person or organisation. This could involve taking over the email account of a staff member or trustee and asking for payments to be made to a particular account, or a payment diversion fraud, whereby a legitimate payment to a supplier is targeted. An example of this is where you receive an email looking as though it comes from a supplier but asking for a legitimate payment be made into a particular account. This account is controlled by the fraudster rather than the intended recipient.
- *Phishing* is an attack that attempts to steal sensitive data by deception. It is usually carried out using malicious mass emails which appear to be from a reputable company, such as a bank or retailer. The email asks the recipients to provide sensitive information, such as bank details and passwords, or encourages them to click on a link that installs malware. Although some phishing attacks are easy to spot,

some are very clever and can have devastating results, including identity theft or the ability for the attacker to gain a foothold in an organisation.

Although cyberattacks are sophisticated, some simple controls such as those listed below will reduce the risks involved. If the trustees, or you as the treasurer or finance officer, are not confident in the robustness of your IT controls, there are IT professionals who can review systems and recommend good practices. There is a list of suppliers on the NCSC website (www.ncsc.gov.uk/section/products-services/verify-suppliers), and it is likely that there will be small IT services firms locally that can help.

Controls over backing up data

All essential records that your charity holds on a computer should be backed up. Then, if the data is targeted by malware or a ransomware attack, this will reduce the risk of it being lost. The data should be backed up to an external source – perhaps a removable external hard drive, other computer or USB stick. The external source should be stored securely when not in use, and not be permanently connected to the device with the original data. Cloud storage means your data can be held in an external location, but check providers' security measures. Most accounting software providers say you do not need to back up your data because of the security measures built into their products, and therefore they do not have the facility to take back-ups. However, any reports or data you export from the system can be backed up. Having a daily back-up schedule will keep your back-ups current.

Controls to prevent virus attacks

All computers and laptops should have appropriate antivirus software installed, and IT updates should be carried out on a regular basis. Anyone using your IT should be aware of the risks from downloading links from websites and emails – these can introduce malware into your charity's systems. Making sure your firewall is switched on can help, as this will provide a buffer if someone tries to download or access a link that may be harmful.

Controls over passwords and access

Implementing controls over passwords and access is especially important for personal smartphones and tablets that are also used for the charity's business, including with banking apps, as smartphones and tablets are particularly vulnerable to loss or theft. Use the highest level of security possible – many devices now incorporate fingerprint or facial recognition to access them. It may also be possible to add tracking functions to devices and to remotely lock or wipe them, when necessary, to prevent unauthorised access. For all IT systems, including web-based applications for accounting software, use two-factor authentication where available. This generally involves sending a code to a trusted device before access is allowed. All passwords should be strong, not shared and not left written down in an obvious place.

Controls to avoid phishing attacks and impersonation fraud

All staff and trustees should be made aware of the risk of emails and texts from scammers. Any email asking for bank details or other sensitive information should be treated with the highest degree of caution. Check the full address of the sender before clicking on any links and delete and block any unsolicited emails. Poor spelling or grammar and low-quality versions of logos should raise concerns – especially if they are out of context with the usual emails you would receive. For example, **HMRC** would never send a text or email detailing a tax refund or Gift Aid claim (see chapter 10), or asking you to provide bank details. If you do receive an email from a supplier asking you to change their bank details, check it is genuine by calling them. The same applies to an email from a trustee or staff member requesting a payment to be made or authorised that seems odd. It is much better to confirm by speaking to the person directly than risking the charity's funds.

This chapter has highlighted that a charity will always face risks but that, as the treasurer or finance officer, you can take actions and put in place processes to help manage some specific finance risks. Many of the controls listed above are simple to implement but must be followed to be effective. It may be tempting to override controls by taking shortcuts, such as not fully checking a payment you are authorising, but this could put your charity at risk, and it would not be considered as acting in the best interests of your charity or managing its resources responsibly.

6 Financial management essentials

Treasurers and **finance officers** keep the books and wider **accounting records** of a **charity** as they provide an accurate **financial record** of what has happened to the charity over a period of time. This information can be used to manage the charity, both for ongoing financial monitoring and as a basis on which to make informed decisions. The current financial data is also a good starting point for forward financial planning.

This chapter looks at some of the terms and approaches used in financial planning and management – such as the differences between a strategic plan, a **budget** and a forecast, and when a cash flow may be needed. It considers what makes good regular management reporting and how this can be used to improve resilience and provide the information needed for decision-making. Finally, the chapter introduces the topics of income and cost management, including overhead allocation.

Financial planning

The **trustees** have **collective responsibility** to ensure their charity is financially robust enough to operate in line with its purposes and meet the needs of its beneficiaries. Financial planning enables the trustees to evaluate the cost of running the service the charity provides and the resources that may be needed, and therefore informs decision-making about what is achievable currently and in the future. As the treasurer or finance officer, you will probably take the lead in the financial planning for your charity – preparing, interpreting and communicating plans to the trustees as a whole for decision-making. There are different levels of planning, mainly determined by the time period they relate to: from the longer-term strategic plan to the shorter-term budgets, cash flows and forecasts.

Strategic plan

A strategic plan maps out the direction of your charity. It is not just a financial document; it should set out the aims of your charity, how they can be achieved and the resources needed. It may also include analysis of your charity's strengths and the challenges and opportunities it may face in delivering its purposes. A strategic plan should articulate your charity's vision and incorporate the practical steps towards how that will be reached. Larger charities are required to set out details of their strategy in the **trustees' annual report** (see chapter 12).

It is helpful to think of strategy in different layers. The top layer is the **charitable purposes** themselves, as these ultimately determine what your charity is set up to achieve. This layer is often described as the vision and mission of the charity, and it concerns the long-term view. The second layer forms the medium-term plans and priorities, usually over the next three to five years. The third layer looks at the more immediate short term, considering the tasks for the year ahead, and will inform the more detailed financial planning found in annual budgets (see the next section). Financial planning tends to focus on the third layer but is very much informed by the second layer (medium-term priorities), particularly in terms of issues such as **reserves policy** (see chapter 3) and **investment** policy (see the section on **investment income** on page 129).

As part of your charity's financial planning, there will need to be some evaluation of the expenditure needed to carry out its work and a plan of where the funding will come from to meet that spending. Although these figures need to be based on some robust assumptions and make sense, they cannot be completely accurate, as they involve predicting and estimating future costs. Where your charity has been operating for several years, it may be easier to determine the expected costs, as they can be based on what it actually costs to run the organisation. For a new charity, or even new projects, it can be more problematic, and assumptions will need to be made about the types of cost and their size.

Sometimes it is helpful to include scenario planning in your strategic plan. This can help you to answer 'What if?' questions – for example, what happens if expected funding is not received? Scenario planning can reflect what can be achieved with different levels of funding. Even with this analysis, it is likely that the strategic plan will remain a high-level document, with the income and costs not broken down in any detail, that will be used as a guide to the direction of the charity. However, it is necessary to have a more comprehensive view of the income and costs that your charity expects to incur, and this is determined in the budget.

Budgets

The term 'budget' can be taken to mean different things. For some, it can mean an agreed level of expenditure that can be incurred by the budget holder without having to obtain further approval (for example, a budget of

£500 to spend on an event). Or it could be taken to mean a target (for example, the budget income from a **fundraising** event is £1,000). For the purposes of using a budget as a tool in financial planning, it is a detailed estimate of the income and expenditure for a period of time in the future – generally the next year.

In smaller charities, it will often be the treasurer who prepares the budget. However, in charities with staff, the finance officer will likely prepare it, with input from other staff. A budget should be presented to the trustees for approval. This approval does not mean the trustees are giving authorisations for all the expenditure shown in the budget to be spent without further discussion. Nor does it mean that the amounts of expenditure have to be spent in full by the end of the budget period. This is in contrast to some public sector departments, where it is necessary to fully spend a budget otherwise the money has to be given back. In most charities, any underspend on the budget will simply be carried over to the following period (unless there is a time-limited **restricted fund**); avoiding unnecessary expenditure means that more resources are left for future work.

In a well-run charity, towards the end of the financial year the treasurer or finance officer will prepare the draft budget for the following year. It will show for each line of income how much the charity reasonably expects to receive in the next year, and for each line of expenditure an estimate of the costs. The budget will look similar to an income and expenditure (or R&P) account, but, instead of being based on actual figures, it will show estimates for the future. If there are restricted funds, you will need a budget for each **fund**.

Preparing a budget is a methodical process. Sometimes, the budget is just assumed to be the current year's figures with a small increase for **inflation**. If you use this approach, care should be taken over which inflation rate you use. For example, you could use a percentage increase across all of your costs – perhaps 5% to 10% to cover known increases in salaries or rent – or perhaps you could link the increase to the Consumer Price Index. There is no particular rate you need to use, but it should be reasonable based on current trends. Otherwise, where prices are rising rapidly or suddenly, you may find an existing budget is not sufficient to meet the actual costs incurred and that funding no longer covers the costs of delivering its associated activities. This can be a particular problem where funding is applied for significantly in advance of the start date of a project (usual for large **funders** with a lengthy application and decision process), where multi-year funding has been agreed on a budget without allowing enough inflation in later years, or with funders that tend to **grant** the same amount each year without considering inflation in costs.

However, budgeting only by looking at actual costs and adding an inflationary element does not really allow you to take stock of what your charity wants to achieve. Sometimes **zero-based budgeting** techniques, where you start each budget afresh (from zero), may allow for more meaningful and critical thinking about your finances.

Whichever approach you use, a good starting point is to take each line of income and expenditure in turn and calculate an estimate for the following year. Some lines may be easier to calculate than others. For example, rent may be a known monthly or quarterly amount, and utilities and administration costs may be based on the current actual costs, increased for potential inflationary rises. Salaries can generally be calculated quite accurately as long as you know the various staff posts and pay scales. You may need to add extra for inflationary rises and staff moving up the pay scale. Remember to add employer contributions for National Insurance and pension payments to the gross salaries (see chapter 11) where applicable. You may need to budget not only for existing staff but also for potential new posts to carry out the services going forward.

Some lines may be harder to predict than others. This is generally the case for certain costs – such as project costs, which may depend on the amount of funding your charity has available – and for income lines. At the time of making the budget, you may already be aware of some grants that will be in place for the year, so these can be added to the budget with certainty. You may also be able to estimate with a reasonable degree of accuracy the **fees** you will charge for any services. But grants that are pending, fundraising income and potential **donations** are much harder to predict accurately. It is important to highlight these uncertainties in the budget, perhaps by adding notes to explain that there may be doubt over the actual amounts received, or where there is a funder decision pending.

If you are preparing a multi-fund budget, you will need to include **inter-fund transfers** (see page 46). There is no set way to present fund transfers in budgets, and it will depend on your charity's particular circumstances. An option could be to have separate lines in your budget to reflect the various transfers between funds. An example could be a line to show contributions from restricted funds to the main fund to cover overheads or a central management fee that is charged. Another example could be a budget line to reflect a flow out of the main **unrestricted fund** into a restricted fund where the money will be needed to support a budgeted **deficit** in the particular restricted fund. You may need other lines to show transfers between different restricted funds where there are combined activities. The important point for the budget is to make these expected transfers clearly identifiable and have an accurate estimate of each fund balance after considering all income and costs (see page 131).

Budgets are based on estimates; therefore, it is best to be clear about the assumptions you have made. This can be helpful where the budget needs to be revised or for decision-making on whether an activity can go ahead. Your assumptions, and consequently the budget itself, can be optimistic or pessimistic (i.e. cautious). An optimistic budget tends to assume good levels of income and modest costs. This can lead to corrective action being needed if the income is not as high as predicted or the cost of something has been understated. A pessimistic budget tends to be the other way around, generally overstating costs and justifying the need for higher funds. Although this predicts the worst-case scenario, it can cause anxiety over whether services or projects can be delivered. When presenting a budget, you should be clear which approach the assumptions take and that the expenditure levels for any worst-case costs do not form targets for approved expenditure.

For some charities, it may be practical to work out the cost side of the budget first. This is especially useful if your charity is providing an ongoing service to beneficiaries and cutting that service would be problematic. If you can estimate the costs of running that service, you will have a starting point for determining the amount of funding you need to have available. On the income side, you will be able to add the known grants and fees to the budget and any difference will be the target for other fundraising opportunities. Scenario planning, mentioned earlier, will allow you to consider what cuts may be needed to services if the other fundraising is unsuccessful. Alternatively, you may find it more useful to estimate the income side of the budget first. This then affects what your charity can afford to carry out in the year, and so project costs can be budgeted accordingly.

Note that budget statements do not have to balance. There are three possibilities:

- Where the *expected income is equal to the expected expenditure*, you have a balanced budget. You can carry out the planned activities over the course of the year, and there will be no change to the funds held.
- In situations where funds are already held to be spent in the following year, it is possible to prepare a *deficit budget*. In this case, the planned expenditure is greater than the planned income in the year.

- If the unrestricted funds in your charity are lower than the required **reserves**, as in your reserves policy (see chapter 3), you will need to build reserves. In this case, it is essential to prepare a *surplus budget*, where planned income is greater than expected expenditure. The **surplus** made at the end of the year then forms part of your reserves.

As the treasurer or finance officer, you may find it works best to present a draft budget to the trustees first – based on all assumptions made – even if it shows a large surplus or deficit. If the trustees believe the surplus or deficit is unacceptable, decisions can be made on an informed basis as to what expenditure to cut, or where there may be possibilities to raise extra funds or even commit to using existing reserves. The budget should provoke discussion and decision-making; it is not only a tick-box exercise that a budget has been prepared.

As discussed in chapter 4, accounts can be prepared on a cash (**R&P**) basis or **accrual** basis. Likewise, a budget can also be created on a cash or accruals basis – it is generally best to use the same approach as in the charity's final accounts. The main difference would be for capital items. In an accruals-based budget, the cost of capital items will be spread over several years with a provision for **depreciation** each year. In contrast, on the cash basis, the full cost of a capital item is shown in the budget for the year when the purchase is made, with no cost in later years. In some cases, especially with larger capital items, it may be better to treat capital items independently of the main budget and show a separate capital budget.

Forecasts

Once you have a budget, you can use a forecast to predict your charity's future financial outcomes as more things become certain. A budget is prepared before the start of the financial year, and as time passes, things that were budgeted for will actually occur, and assumptions about other income and expenditure in the future will become more definite. You should not adjust your budget for these changes, as that would reduce the effectiveness of the budget as a monitoring tool. But you can prepare a forecast of your expected position at the end of the financial year.

You can prepare a forecast using a mixture of the actual income and expenditure for the months that have already passed, and your budget for the remaining months. But these budget figures can be amended for any known income or expenditure that is expected to happen. The forecasted result for the year may therefore be different from the budgeted result –

for example, adjusting for a new grant that has been awarded but was not considered in the budget, or including a rise in utility bills that was not predicted. The forecasted position is likely to be much more accurate than the budget. It will change each month as more of the **transactions** happen or more assumptions become certain. Towards the final months of the financial year, your forecasted position will become more and more like the actual results of the year.

Cash flows

A budget and forecast look at the expected income and expenditure over the whole year. They do not consider the timing of that income and expenditure and, crucially, whether there is sufficient money on hand at any time to meet expenditure needs. If your charity cannot pay its bills, like any other organisation, it will become insolvent. Given the uncertainty of charity income, especially if you have minimal reserves in your charity's bank account, you may need to manage your cash flows carefully. For example, if fundraising and **donated income** tend to be seasonal, there may be times when there is no income coming into the bank but expenses still need to be paid. And some grants or **contract** income may be payable in arrears, meaning your charity may need to pay for expenses and salaries before the funds are claimed back. In cases like these, preparing a cash flow may be useful.

A cash flow looks at the actual flows of cash expected into and out of the bank. It is usually prepared monthly; however, if there are concerns, it can be prepared on a weekly or even daily basis. It is usually easier to prepare a cash flow for each bank account separately. If funds from different bank accounts are combined, it will not be easy to see whether a bank account is predicted to go overdrawn. If you do make one combined cash flow covering all bank accounts, you will need to add in predicted transfers between bank accounts where necessary.

A cash flow that looks at the movements into and out of the bank over the year ahead is often referred to as a **cash flow forecast** – a key **management accounting** tool. This should not be confused with a **statement of cash flows**, which is something that larger charities are required to prepare as part of their **annual accounts** (see chapter 14). A cash flow forecast is generally presented in a table with different columns for each month, although it may be presented graphically to illustrate the peaks and troughs of available cash. You can create a cash flow statement on paper, but it is generally helpful to use a spreadsheet package; it is not something that can be automatically generated from an accounting system as it looks forward. Figures from the past year may help in predicting the timing of income being received or bills being paid, but the actual amounts in the cash flow need to tie back to the budget.

To create a monthly cash flow forecast from your budget for the year ahead, draw up a spreadsheet with 14 columns (for a simple example with an April to March financial year, see figure 6.1). The first column is for the type of income or expenditure (using those in your budget), the next 12 columns can be labelled with each month of the financial year, and the final column will be the totals. For each income line in the budget, you can allocate the amount of monetary receipts expected in each month. For example, if a £25,000 grant is receivable in April in full, add £25,000 to the April income. If the grant is paid in instalments, add those to the expected months of the receipts instead. If you know when a fundraising event will be held, add the expected receipts from it to the relevant month. It may be that you need to use past knowledge or a bit of guesswork to allocate some of the income. And if all else fails, it is possible to simply divide the total income estimated in your budget by 12 and allocate the result equally.

The same exercise then needs to be carried out with each line of expenditure, entering the actual payments to be made. The timing of some costs will be easier to predict – those that must be paid monthly or in line with when a particular activity is planned. At the end of the exercise, it is important to check that the income and expenditure across all months are totalled in the final column. This column should equal the budget. This means you have considered the timing of the cash flows associated with the full budget.

At the bottom of each monthly column, you can make a simple calculation to add together all the receipts and subtract from this all the payments. This will give the net cash flow in or out of your bank each month. A positive figure means you will have a surplus of cash that month, but a negative figure means you are predicting you will spend more than you will bring in and therefore need to have cash available from somewhere else to fund the spending.

However, this is only considering the flows in each month. There will be a cumulative effect. Therefore, it is necessary to add the expected bank balance at the start of the year and add in the monthly net flows across the months (as shown in the bottom two rows of figure 6.1). If this cumulative figure remains positive, you should have enough cash available to meet your bills. But this comes with a large caveat: all of this money must be available to use with none specifically tied up in restricted funds. As noted in chapter 3, it is important to ensure any restricted funds are only used for the purposes intended. Therefore, in using existing money to support periods of negative cash flow, trustees must ensure they are not breaching

Cash flow forecast

	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Total
	£	£	£	£	£	£	£	£	£	£	£	£	£
Receipts													
Grant income	25,000			5,500			3,000				2,000		35,500
Fees charged		500	500	500	500	500	500	500	500	500	500	250	5,250
Fundraising					3,500				1,500				5,000
Total receipts	25,000	500	500	6,000	4,000	500	3,500	500	2,000	500	2,500	250	45,750
Payments													
Wages	1,200	2,100	2,100	3,200	3,200	3,200	3,200	3,200	3,200	3,200	3,200	3,200	34,200
HMRC and pension	200	200	300	300	450	450	450	450	450	450	450	450	4,600
Hall rent		125	125	125	125	125	125	125	125	125	225	75	1,425
Activity costs			200	350		400	500		400			400	2,250
Consumables	80	120	75	200	50	250	125	150	75	80	200	200	1,605
Phone and IT costs	50	50	50	75	75	75	75	75	75	75	75	75	825
Insurance		550											550
Fundraising costs				520	55				130				705
Governance								400			125		525
Total payments	1,530	3,145	2,850	4,770	3,955	4,500	4,475	4,400	4,455	3,930	4,275	4,400	46,685
Net cash flow	23,470	–2,645	–2,350	1,230	45	–4,000	–975	–3,900	–2,455	–3,430	–1,775	–4,150	–935
Opening bank	12,560	36,030	33,385	31,035	32,265	32,310	28,310	27,335	23,435	20,980	17,550	15,775	
Closing bank	36,030	33,385	31,035	32,265	32,310	28,310	27,335	23,435	20,980	17,550	15,775	11,625	

Fig. 6.1 An example of a simple cash flow forecast based on assumptions about when money will be received and payments are required to be made

any restricted fund conditions by unintentionally using their contents for another purpose.

If your cash flow forecast shows large negative flows of funds in particular months, the trustees will need to decide whether there are sufficient cash funds elsewhere to support those periods and not jeopardise other activities of the charity. The funds could come from other unrestricted funds of your charity or from a loan (if your charity has the powers to borrow in its **governing document**). If you are able to demonstrate that a grant or contract payable in arrears will result in significant cash flow concerns, the funder may be willing to pay an upfront payment to help manage the project.

If the overall forecasted cash balance is predicted to fall significantly, or even turn negative, this is a serious concern. Your charity will only survive if additional income can be raised, expenditure can be reduced or some form of borrowing is forthcoming. This is where, as the treasurer or finance officer, you must highlight the concern promptly to the trustees so that those hard decisions can be made.

In the example in figure 6.1, in most months the net cash flow is negative. This is because the grant that was received in month 1 is being used up over the year. It is also predicted that the charity will use more cash in the year than it generates as the total net cash flow is a deficit of £935. However, as the charity has unrestricted reserves, represented by the opening bank balance in month 1, the bank balance always stays positive and the deficit in the year can be met. Therefore, this cash flow forecast does not predict any serious issues.

Once you have this cash flow forecast made from your budget, you should update it each month with actual cash flows that have happened. You may be able to predict future flows with more certainty as time passes, in which case the cash flow can be changed accordingly. This is the purpose of a forecast – it provides more accuracy than your initial budget, allowing you to predict your future bank balances more accurately and potentially avoid or manage a major cash flow crisis.

Continuing financial management

Forecasting forms part of your continuing financial management, the regular monitoring of finances and decision-making about income and expenditure. For charities with multiple funds, this may mean on an individual-fund basis. A major part of the role of the treasurer or finance officer is preparing and presenting the financial information at the regular trustee meetings.

Management accounting involves taking the actual figures from your charity's books and presenting them in a form that will be useful for internal decisions. Some treasurers and finance officers will be familiar with 'management accounts' and may use this term in the reports they give. However, in smaller charities, often the term used in the agenda for a trustee meeting is simply the 'treasurer's report' or 'current financial report'. Even if this is the case, what is presented should be more than a simple verbal account.

It can be difficult to take in financial information that you only hear, never mind use it as a basis for decisions or have an awareness of the future impact it may have. So, the first step in creating a useful financial report is to prepare a written document that can be circulated to the trustees in advance of the meeting. This will give all trustees time to digest the information. It will also act as a financial record for your charity, which is often required as part of the **audit** or **independent examination** process, and also as a historical record for the trustees to support their decision-making.

If the information presented in your financial report is a simple list of the actual income received and payments made, together with the bank balance, it does not really provide any basis for decision-making. It could be made more useful if a summary of income and expenditure were provided for each fund, with the balance of each fund highlighted so that the trustees understand what is available to spend, but this still does not really provide any context. It is useful information and good for control purposes, but to be more effective, there needs to be some form of comparison.

Variance analysis

It is possible to compare current and prior years' figures, but often for charities the work carried out in the prior year is not relevant to the current year. In such instances, all you are considering is past information. To provide relevant decision-making information, it is more effective for management accounts to present the current position and compare it against the budget, together with a **variance analysis**.

Variance analysis is the difference between actual and budget figures together with an analysis (or explanation) of why there is a difference. It is often seen as three columns of numbers against each income and expenditure line – the actual figure, the budget figure and the **budget variance**. The budget variance can be an amount in pounds (either over or under), or it can be expressed as a percentage, as this may be easier to interpret. In percentage form, it is calculated as:

Budget Variance (%) = ((Actual – Budget) / Budget) × 100

For example, an event is budgeted to cost £1,350. When all of the invoices have been paid, the total cost is £1,670. Using the calculation, this overspend of £320 represents a 23.7% variance above budget – i.e. ((1,670 – 1,350) / 1,350) × 100 = 23.7.

Note that where the budget figure is zero, this calculation will not work. Anything divided by zero is infinity, and calculators and spreadsheet calculations will give an error.

Using this calculation, a positive variance on the income side is good – you have more income than budgeted. But on the expenditure side, a positive variance means the costs are higher than budgeted. Negative variances are the other way around – less income than expected and underspend on cost lines. Even the addition of a variance figure is not sufficient on its own – for any significant variance, you should determine and explain why it has occurred. Defining what constitutes a 'significant' variance will be different for each charity, and perhaps different between each fund or income and expenditure line, so it is not appropriate just to say that, for example, any difference over 20% should be analysed. Experience with your organisation, and questions from fellow trustees, will help you find the right approach for your charity.

Remember that to compare actual and budget figures in this way for monitoring purposes, you will need the budget lines to accurately reflect those that you use in your books. If you do not do this, you may need to spend significant time extracting the correct actual information to compare it to the budget figures.

Presentation considerations

How much detail should be put into management accounts can be subjective, but they will have no value if the information in them is not meaningful. The information presented must be understood by the reader. Although you may want to show an analysis for each fund, do you need to have all income and cost lines listed separately or could some be amalgamated? For a small charity with simple funds, it may be sufficient just to have one line for income and one for expenditure for each fund. However, this will likely to be too simple and not show enough detail for a charity carrying out more activities where it is necessary to show more detailed costs lines.

As noted in the discussion of budgets above (see page 112), if you operate restricted funds, you will need a budget for each fund and therefore separate 'actual versus budget' analyses for each fund in your management accounts. This could result in an overwhelming amount of information. Not only may some trustees be put off when faced with pages of numbers, but it will also be time-consuming for you to produce a detailed analysis for every set of management accounts.

However, it is not wise to incorporate all funds into one report. Looking at your overall expenditure will not give enough detail for decisions to be made on a specific fund. For example, there may be an underspend on salaries across the budget. This could indicate there is funding available to take on another post. But you would need to know which fund the underspend related to. For example, you may not be able to take on a general administrator if all the salary underspend comes from a specific unfilled post in a restricted fund.

A suitable approach to management accounts may be to provide a summary report on the first page which shows the actual figures in each fund but no budget figures or analysis. This can be supported by a detailed analysis and comparison with the budget for all – or even just some – of the key funds, especially those that need decisions. Any analysis of funds given in the management accounts should include a running total of each fund balance by including the opening position of each fund – not just the income and expenditure in the period. If these brought-forward balances are excluded, there will be no clear picture of what is left available to spend on a particular fund.

Some accounting packages do let you add budgeted figures and pull off standard or tailored reports including budgets, actuals and variances that you can incorporate into the management accounts – this can be a time-saver. If they have been prepared, cash flow forecasts and/or other forecasted information, together with any specific analysis to support a decision that needs to be made, will be useful additions to the management accounts.

Remember that not everyone understands numbers. There could be many columns of figures in a set of management accounts, so make them clear to read, round numbers to the nearest £1, align columns, use clear headings, and make use of coloured fonts or backgrounds to highlight specific columns, rows or important figures. That being said, if you have trustees with particular needs, ask them what works best – too much use of colour can be problematic for trustees who are colour blind, and excessive use of different colours can be challenging for those with dyslexia. Also, bear in mind that trustees who prefer to read documents in hard copy will only benefit from coloured text if they are provided with a printed copy or have use of a colour printer.

Consider alternative approaches – add graphs where they show the information more clearly. For example, a pie chart will visually show the proportions of spending on each item. Bar charts can be useful when comparing actual figures against budget figures, or current and prior year. Add narrative and explanations about any points you want to bring to the trustees' attention.

Frequency of reporting and accounting periods

If possible, it is best to keep management reporting to a uniform period – for example, monthly, bimonthly or quarterly, always working to the end of a month. Keep in mind that it will probably take some time to prepare the management accounts and circulate them to the trustees. It will not always be practical to present management accounts to the end of April at a meeting on 3 May, for example. If you have monthly management meetings, you may not need to do full management accounts every month; they could be prepared on a quarterly basis, with a smaller update in the other months.

The exception to this would be if there were potential financial issues. In this case, more frequent and up-to-date financial information is needed, and some form of crisis planning could be inevitable. This may take the form of weekly cash flow forecasts, identifying costs which can be cut, payments that can be delayed or income that can be generated.

Once you have established a cycle of reporting, you need to decide whether to separate the year into **accounting periods** – for example, providing figures for only the month or quarter in question, or for the year to date. Let's say your charity's accounting year is 1 April to 31 March, and you present quarterly management accounts. At the October meeting, is it best to show figures for the second quarter (July–September) or for the full six months (April–September)? There is no simple answer to this, as it will be influenced by your charity's activities.

If you rely on **trading income** (see chapter 8), having the numbers for each quarter as separate stand-alone numbers, rather than year-to-date figures, may be more meaningful. This will allow profitability comparisons between each quarter (or month), which may provide useful analysis for seasonality factors. However, if you are mainly reporting on grant-funded figures, the year-to-date information may be more important to show usage of each grant over time.

When comparing these accounting periods to your budget, the budget will need to reflect the same period as the actual figures. This can be achieved by allocating the budget across the monthly or quarterly periods on a detailed basis (for example, in a similar way to the section on cash flows on page 117) or by simply taking the relevant proportion of the budget – for example, one-twelfth of the full year's budget for one month, three-twelfths for a quarter and so on. Alternatively, it is possible to compare against the full budget each time you report so you can see your progress against the full budget or other forecasted figures. It is worth noting that funders may want to see mid-year progress reports as well as final reports. Your management accounts can be helpful in providing this information, but often the funding period and a charity's accounting year do not align. Therefore, you may need to combine figures from separate management account reports and even two different accounting years.

Management of income

Having the analysis of your charity's finances in your management accounts provides the information for financial decision-making. But running a charity does not necessarily mean those decisions are about maximising income and minimising expenditure to make a surplus. For a charity, the decisions are more about using the funding you have in the most effective way. Most charities do have to spend money to advance their charitable purposes, so, for example, taking steps to cut expenditure may reduce your charity's effectiveness.

If your charity is struggling to make ends meet, there are always two choices: cut expenditure or increase income. Often the best solution is a bit of both. In contrast, if your charity finds itself in receipt of more money than expected or with costs you were expecting to pay reduced, the decisions are not about making ends meet but about how the funds can be best managed to advance your purposes further. As noted in chapter 3, it is not always acceptable to let reserves become too high. Therefore, if it becomes increasingly difficult to spend all the income you receive, the trustees may need to consider whether your charity's purposes are appropriate or need to be changed (remember, a change to your charity's purposes requires the consent of the relevant **charity regulator** – CCEW, OSCR or CCNI; see page 21 for further discussion).

A charity's spending on its charitable purposes is constrained by the income it is able to generate; therefore, charity fundraising is key to the role of all trustees. Many charities use the term 'fundraising' only to refer to certain types of income generation, and some individuals or charities object to the word completely due to a belief that charities should not need to ask for gifts as making a donation should be a personal choice. But charity fundraising simply means the process of raising enough funds to support the work the charity wants to carry out – whether that is by grants, gifts, selling goods or services, or maximising investment income.

In some charities, there may be a staff member or volunteer who co-ordinates the fundraising, or a trustee may be tasked with the role. This is a completely separate role from the finance officer or treasurer; however, there are links between them, and these are covered further in chapters 7 and 8. In other charities, there may not be a separately identified fundraiser role, and it may be up to all trustees and volunteers to carry out fundraising – but, even in this case, some co-ordination by one person (or perhaps a small team) is probably best.

The following is an introduction to the three main ways a charity can generate income – donations, trading and investment.

Donated income

Money or resources given to a charity are donated income. As explained in chapter 1, this ability to attract gifts – often for nothing in return – is at the heart of being a charity. Donated income includes:

- coins and notes placed in a collection box or plate;
- any gifts from individuals by cheque;
- payments from **donors** directly into a bank – typically through standing orders or direct debits (if applicable);
- gifts from individuals using other electronic means, such as giving platforms, card machines, text messages or QR codes;
- donations as a result of fundraising or sponsorship events;
- payroll giving donations (these will always come via an intermediary body rather than directly from the donor);
- gifts of items or resources for the charity to use or sell;
- grants or donations from grant-making charities;
- donations from a company or other organisation (as long as it is not seeking anything in return);
- grants from local authorities or public sector funding (providing that it is a genuine grant – see the next section, on trading income);
- legacies left in people's wills.

There is no legal distinction between a grant and a donation. 'Donation' tends to be the term used when an individual gives money to a charity, and 'grant' refers to money given by an organisation (such as a trust or foundation), a local authority or the government (although some charitable trusts often call the amounts they give to charity 'donations'). Donations from individuals can attract Gift Aid, which can increase the donation's value by 25% if certain rules are followed. Chapter 10 covers the Gift Aid scheme.

As discussed in chapter 3, whenever a charity receives donated income, the first thing to check is whether there are restrictions attached (see especially page 36). If there are, and the trustees are confident these can be met, the donated income will need to be allocated to a restricted fund and only used for those purposes. Other donations, without any specific conditions attached or where the only condition is that they should be used to carry out the overall aims of the charity, can be earmarked for your unrestricted fund. This allocation is an important factor in managing your charity's income.

There is normally no contractual relationship with a donation or grant; money is given to a charity under the relationship of trust. If the charity misuses that money, the trustees could be in breach of trust and may have to reimburse the funder. However, some grants, especially those from public sector funders, may have pages of conditions attached regarding how the funding is to be used. This is still usually a grant, as the funder is not purchasing anything from the charity – it is setting conditions, and so the funding will likely be a restricted grant.

However, if the funder is purchasing anything from the charity, it will need a contract and the income received will be classed as trading income. Some local authorities describe their funding arrangements as **service level agreements (SLAs)**. In this case, you may need to determine whether the SLA is a grant or contract. Most will be a grant, although restricted to a purpose and a certain service level that must be achieved. For annual accounting purposes (see details on the Charities **SORP** in chapter 14), SLAs are generally described as **performance-related grants**. Contracts and SLAs are covered further in chapters 8 and 9.

Some charities simply accept donations without actively seeking them, but if the work of your charity is worthwhile, why wouldn't you ask people to support it when needed? The link between the finance and fundraising functions is considered in chapter 7. Where a charity relies on grant funding, trustees need to be proactive in seeking funding, planning ahead following a strategy to apply for new funding. As the treasurer or finance officer, you should be alerting trustees to when funding cycles are coming to an end, as this is where gaps in funding may occur. You will also be expected to provide the figures for the financial section of any grant application, usually based on the charity's budget.

Trading income

Many people think there is a rule preventing charities from trading, but some charities derive more of their income from trading than from donations. Trading income is that earned from charging for goods or services. Charities which derive significant amounts of their income from trading often describe themselves as social enterprises (see page 2), but if they are a charity, it is still charitable income following charity law.

Charity trading is divided into:

- **primary-purpose trading**, where the goods or services provided relate directly to the charity's purposes;
- **trading for fundraising purposes**, where the goods or services provided are sold as a means of raising funds.

The differences between the two (along with examples) are covered in detail in chapter 8, and the tax implications of trading income are covered in chapter 9. Trading income can help with the sustainability of a charity because it is actively generated, whereas the decisions on grant awards rest completely outside the control of the charity and its trustees.

Income from primary-purpose trading is usually unrestricted. This means the charity has freedom to use the income to meet its charitable purposes. As the treasurer or finance officer, one of your key concerns from an income management point of view will be the pricing of the activities and services under primary-purpose trading. You will have to bear in mind the **public benefit requirement** of charities (see more in chapter 8) – for example, ensuring the price is not so high that it prevents potential beneficiaries from accessing the service. On the other hand, you must consider the costs of providing the service (see page 130) and make sure your charity has a plan to cover them.

Trading income for fundraising purposes is normally unrestricted, unless (for example) you ask people to buy tickets for or support an event on the basis that the proceeds will be used for a specific purpose. However, there are strict tax limits on trading income from fundraising, and your charity could be liable for corporation tax (see page 170). Pricing is a key financial decision to consider in relation to a fundraising activity. The price should not be too low (so you don't make a profit) or too high (which might put people off), so you need to know your market. A fundraising activity does need to bring in sufficient funds to justify the time and effort involved from all volunteers (and any time or money spent on marketing the activity). However, there are cases where a small surplus may be acceptable if the fundraising activity has directly raised the profile of your charity or increased awareness of your cause.

Investment income

For many smaller charities, the only investment income that will apply is bank interest; however, for charities that hold investments, the income derived from them could be substantial. Indeed, many grant-making charities pay out grants based on the investment income they receive. Investment income includes:

- interest on bank deposits and other investments;
- dividends on shares;
- rents on investment properties (where your charity holds property specifically for investment purposes).

Charities benefit from a number of tax concessions in relation to investment income. For example, bank interest is untaxed and there is no capital gains tax to pay when investments increase in value. If your trustees consider that your charity has funds that are not needed to pay for costs in the immediate future, it can therefore be worth considering whether the funds could be invested in some way to bring in an income.

The question of whether investment income should be allocated to an unrestricted fund or restricted fund relates to the deposits or property on which it is generated. For example, if you receive interest on restricted funding that is among other funds in your charity's bank account, you should use a reasonable basis (such as the proportion of restricted funds to general funds held in the bank account) to allocate a certain amount to the restricted fund. In practice, however, especially where the funder expects that the money will be spent fairly soon, very few funders would specify that a portion of your investment income needs to be allocated back to the restricted fund; therefore, all interest income can often be classed as unrestricted. However, if you hold substantial amounts for a restricted purpose, such as a building appeal, then the interest generated on those funds should also be restricted in the same way.

If you are a smaller charity with limited financial deposits, managing your investment income may be a case of choosing the best bank account that provides a good interest rate. With larger investments, it will probably be wise to seek the advice of a professional investment manager, especially where an **endowment fund** (see page 41) is the main source of your income.

Managing income from an endowment fund depends on the conditions set out for the endowment. The terms of the endowment normally require that income (such as dividends and interest) is allocated to a fund – restricted or unrestricted – so that the income generated can be spent on the charity's purposes. Any capital growth will normally remain in the capital (endowment) fund.

If your endowment investments are providing too much capital growth and not enough income return, or vice versa, there are complex rules surrounding **permanent endowments** outlining how you can apply a **total return** approach, where capital growth and investment are considered together. Any charity in this situation should seek both the regulator's guidance and the advice of their **auditor**, **independent examiner** or charity investment specialist.

Investment management is a major topic in itself and it is only possible to cover it briefly in this book. Trustees must take professional advice on investment management where they do not have the relevant experience, but the treasurer or finance officer should be involved at least to some extent, due to the impact of investments on a charity accounts.

If your charity does hold investments as a source of funding, it is essential to have an investment policy in place that sets out the principles of what your charity will invest in.

Social investments

Some charities make use of **social investments** – for example, making loans to beneficiaries on subsidised terms or supporting other charities with investments that only have to be repaid if a project succeeds. When a charity makes a social investment, it hopes to get some financial return (unlike a grant, where funds are given away completely), but the expected return is less than with a conventional financial investment and there may be a higher **risk** of not getting the capital repaid.

Therefore, social investing requires trustees to have clearly documented policies and evidence that they have debated the risks and returns. The risk of the capital not being repaid must be justified by anticipated outcomes linked to the charity's purposes. That is, it must be shown that in making the investment in the first place, the trustees were acting in line with what the charity was established to do.

Management of costs

As noted previously, managing your charity's costs does not simply mean spending less, as this could reduce your charity's effectiveness in meeting its purposes. However, this is not to say that a charity should not regularly review the costs it incurs and how much it is paying for goods and services. As a treasurer or finance officer, you should understand these costs. For example, are there any unnecessary costs that can be cut, are there better deals available on some of your ongoing costs, and have you considered quotes for larger items of expenditure?

But probably one of the most important tasks of a treasurer or finance officer is to ensure costs are allocated correctly to the various funds. This is to make certain both that you are not in breach of trust with any restricted funds and that you are charging costs appropriately to your charity's various funds and projects – showing the true cost of each activity or project. As explained previously, you cannot use a restricted fund to subsidise deficits elsewhere (see page 36), but you can use an appropriate proportion of your restricted funding to cover general costs that would not have been incurred if you had not run the project covered by the restricted funding. Direct costs are generally easy to identify; the issue normally lies with overheads.

Overheads, often called 'core costs', are the general running costs of your charity. They may include rent, premises and administration costs, but also salaries of core charity staff, such as the **charity co-ordinator**, finance manager and/or administrator. In any case, good financial management should allow you to understand the true cost of delivering a project. For example, how much of your charity co-ordinator's time should be included in the outreach project or what proportion of administration and premises costs should be allocated to the weekly dementia support group? This involves understanding overhead allocation and the concept of **full cost recovery**.

Overhead allocation and full cost recovery

To illustrate the importance of identifying overheads, consider the following example. A charity decides to take on a new project which requires the employment of a new project worker and some direct project costs. But in employing an additional person and setting up a new project, the charity will also incur other costs, such as:

- the charity co-ordinator's time in supervision and training;
- a space in the charity's premises;
- the use and maintenance of computers, telephones and software systems;
- an additional employee in the charity's payroll and HR systems;
- additional transactions from the project delivery which may require additional work and time needed for the charity's bookkeeper, together with the financial management of the project;
- the costs of applying for the funding in the first place, such as time to complete applications.

Individually, these items may not seem significant, but they all add up. If they are not met by the funding for the project, they will have to be paid for by the charity's unrestricted funds.

When you are looking to apply for a grant or bid for a contract, it is important that core costs are considered and that any funding is sufficient to cover the appropriate share of these overheads. When completing a funding application, you may call these costs 'overheads', a 'management fee' or even 'contribution to core costs'. Historically, funders have disliked these terms and preferred to fund purely direct costs. However, times are changing, and there is more understanding that charities need funding for core costs to be sustainable and continue to deliver their charitable purposes. Therefore, any application that includes a reasonable element of overheads, especially where it is explained what it covers, should be looked upon favourably.

Managing the costs of a project to include all necessary overheads is termed full cost recovery. But be aware, even using full cost recovery does not guarantee you will be reimbursed for the full costs of the project. Some funders, especially local authorities, may be short of funding themselves and may not be able to meet the full cost demands of the project. You may then be faced with a choice between doing the work at less than the full cost, subsidising the project from other unrestricted funds or not doing the work at all.

On the other hand, any full cost recovery calculations are based on estimates and the methods you use to apportion overheads. There is no exact or even one universally accepted way of apportioning overheads. This means that changing the costs allocated to a project will make it appear less or more costly. For example, if you estimate that your charity co-ordinator will need to spend half a day per week supervising the project, this will be much more costly than if you estimate that the time needed will be one day a month. This example highlights the need to make reliable estimates and judgements to ensure that you can justify that the costs allocated to a particular project have been made on a reasonable basis.

Personnel costs are usually apportioned based on estimated staff time. This could either be very detailed, looking at individual staff members and hours spent, or a more general percentage applied to the costs of a core staff team. Quite often, administration costs will follow this percentage. For example, if you estimate that the project will require 15% of your bookkeeper's or administrator's time, it is probably reasonable to also include 15% of your accounting software and administration costs. Premises and utility overheads can be allocated based on space, such as a proportion determined by the actual area of space the project takes up. This is easy to assess if a particular project uses a permanent space; however, if it is a shared office space, it may be better to allocate the cost based on the number of people using that space for a specific project. To illustrate, if there are six people in the office and two work solely on a particular project, it may be reasonable to allocate a third of the premises costs to the project.

As the treasurer or finance officer, you will probably need the input of other staff and trustees to make reasonable assumptions about how overheads should be allocated. Then, when these figures are presented to the trustees as a whole, you should be able to make clear any assumptions about how the overheads are allocated to a project and gain the trustees' agreement as to their reasonableness – without overloading the trustees with complicated calculations.

Making sure the funding you receive covers the full cost of project delivery can be challenging, and sometimes impossible. Tendering for contracts can be particularly problematic, as competition between charities and even commercial operators may result in undercutting practices. Good financial management requires you to be clear about the minimum amount of funding you need to carry out a service. If accepting too low a price could leave your charity in financial difficulties and unable to deliver on a contract, a key task of the treasurer or finance officer in supporting your charity could be to help the trustees to say 'no' to an unsuitable project. For this reason, as a treasurer or finance officer, you should be involved in bidding decisions.

In some circumstances, however, it is acceptable to take on a project even where the funding does not cover the full costs. But this must be justified. The project may be crucial in meeting your charity's aims, and there may be other ways to cover the shortfall in funding. For example, other fundraising may be able to cover the overheads, or your beneficiaries may also be paying a small fee for the service which makes the project viable. However, care is needed, and setting prices too low for a contracted service could mean your charity is subsidising an external non-charitable commissioning body and setting unrealistic expectations about funding going forward.

Planning and continuing management of a charity's finances are crucial parts of the role of the treasurer or finance officer, and they involve knowing how to gather the information needed and present it in a meaningful way so that the trustees can use it in their decision-making. Managing the finances of a charity is not necessarily concerned with maximising income and minimising costs, as it often is in a commercial business – instead, bringing in sustainable income, so you can meet your charity's purposes, may be more appropriate. Chapters 7 and 8 look at funding a charity and charity trading in more detail.

7 Finance and fundraising

Charities need sources of funding to carry out their work. Chapter 6 introduced the various types of income that charities typically rely on, and how as a **treasurer** or **finance officer** you will be involved in the financial planning and management of those resources. Although the responsibility for how a charity is funded is a matter for all **trustees**, the implementation of this in practice tends to depend on two key roles – the treasurer (and any bookkeeper or finance officer) and the fundraiser or **fundraising** manager. There may not be a designated fundraiser role within the trustee group, but there will generally be a trustee or staff member who takes the lead on submitting **grant** applications, communicating with **donors** or organising fundraising events.

This chapter considers how the finance and fundraising functions should interact and the importance of being involved as the treasurer or finance officer in fundraising appeals. It introduces the regulatory and ethical aspects of fundraising, such as factors to consider to ensure you are fundraising responsibly and whether all gifts of money should be accepted. It explores involving third parties in charity fundraising and the possibility of having a commercial relationship with a business. As the methods for receiving money evolve with technology, the chapter next considers online giving platforms, cashless ways to accept gifts and cryptoassets. Finally, the chapter concludes by considering the costs of fundraising.

The treasurer's or finance officer's role in fundraising

In some charities, there is an expectation that the treasurer will be the person to complete the grant applications or decide when fundraising needs to be carried out. This tends to be because of the connection to money and **funds**. There is no particular issue with this if the treasurer or finance officer has the capacity to do the work. However, given the other responsibilities of the role, this will probably be too much for one person in all but the smallest of charities. In addition, the skill set needed in a good fundraiser does not necessarily match that of a good treasurer or finance officer. Fundraisers need to be excellent at networking, marketing their charity's work and putting forward a compelling case for support to potential **funders**. Therefore, it would be good practice to have another trustee or staff member responsible for fundraising, possibly heading up a small team.

Whatever the approach, it is crucial that the fundraiser and treasurer communicate well. Otherwise, the outcome can be disastrous for the charity. Fundraisers who simply try to bring in as much funding as possible without considering the implications, such as any restrictions imposed on that funding or whether the charity has the ability to fulfil the terms of it, may cause difficulties for the charity. For example, a funder is not likely to support a charity in the future if it could not deliver on the requirements of a funding agreement, and the adverse effect on the charity's reputation may also deter other funders. Additionally, fundraisers must be able to demonstrate that their charity has good accounting procedures. Funders want to be sure that when funds are received, they will be properly managed. A funder who does not receive clear information on how their money has been spent or is not happy with how it has been accounted for in a charity's accounts is unlikely to provide funding again. It is worth noting that most funders ask for a copy of the charity's latest **annual report and accounts** (see chapters 13 and 14), so poorly prepared accounts can be very damaging for fundraising.

Therefore, good communication between the fundraiser and treasurer, an understanding of each other's role, and a sensible division of responsibilities are important if your charity is to be well run. The following questions set out some areas that may need clarification. Not everything on this list will apply to all charities, and the items will not cover all eventualities. However, they should provide points of discussion to avoid duplication of work and to ensure no areas are missed if one role believes the other is responsible for a specific area:

- *Purpose of gifts*: Is there a simple procedure to ensure the fundraiser knows what to raise money for and when? When funding is received, does the treasurer or finance officer know to which fund every grant or **donation** will relate?
- *New restricted funds*: Is the fundraiser authorised to take on funding that creates a new **restricted fund**, or must this be approved by others? How does the treasurer or finance officer know they need to create a new restricted fund in the **accounting records** (and which expenses will relate to it)?
- *Costing of projects*: When bidding for funds, who determines the level of funding that should be requested (for example, are overheads included)? If the fundraiser applies for and accepts funds without knowing the costs to deliver, there is a **risk** that the funding will not be viable, putting charity funds at risk.

- *Deciding when to refuse a gift*: Every charity needs a policy on ethical fundraising (see page 142) and on when it is right to refuse a gift (see page 143). Sometimes, a gift may give rise to a **conflict of interest** or come with onerous conditions attached that mean it is not in the best interests of the trustees to accept the funding. How are the decisions to accept or refuse a gift made and who takes the lead?
- *Issuing receipts for gifts*: It is good practice to thank donors for gifts. For a grant, this will probably include formal acceptance documents, but for other donations, some form of acknowledgement is also needed. This can be a big task if your charity has a large fundraising appeal or receives lots of individual donations. Who is responsible for making those acknowledgements to donors, and how are they alerted to a donation being received?
- *Deciding how funds should be received*: Should the fundraiser confirm with the treasurer or finance officer how funds should be received – for example, by bank transfer or through a donation platform? What reference should be attached to the **transaction** so that the donation can be identified?
- *Banking income*: If funds are received in cash or by cheque, how are these handled according to your charity's financial controls? Are all cash takings from fundraising events given to the treasurer or finance officer to deal with, or can the fundraiser bank cash independently? If the fundraiser can bank cash themselves, do they know how to properly identify any expenses paid out of the cash before banking?
- *Gifts received directly to the bank account*: If your charity has donors who make regular gifts by standing order directly to its bank account or via online banking, who checks these against the pledges made? How does the treasurer or finance officer identify a particular donation and what it is for? It is likely the treasurer or finance officer will first identify when a new transaction has reached the bank, so they should probably send details to the fundraiser to determine who the donor is and what the funding is for, and a reminder to send an acknowledgement.
- *Gifts received via online funding platforms*: Third-party giving platforms can be convenient ways to collect donations (see page 149), but who is responsible for choosing which platforms to use and agreeing to charges? Who determines the content and promotes awareness (such as through social media) of these platforms, and who looks after the administration side, and monitors and analyses the donations?

- *Other cashless giving*: As more and more people decide not to carry cash, having a way to accept non-cash donations is becoming increasingly useful (see page 151), but who is responsible for implementing a system for accepting such donations and monitoring the funds received?
- *Direct debit donations*: Most high-profile large charities set up direct debit schemes to encourage regular giving. Although rarer among smaller charities due to the processes and bank assurances required, direct debit donations can be effective in bringing in regular known funding. Your charity must request a direct debit payment each month (or as agreed), although there will be an automated system in place with the direct debit provider. Who is responsible for this system at your charity, and how are refunds made following errors or donor complaints?
- *Charities Aid Foundation (CAF) and similar schemes*: In the CAF scheme, a donor can pay into a CAF account (on which CAF can reclaim tax) and direct CAF to donate the funds to a particular charity. Often charities only become aware of such donations through a deposit in their bank. Who follows these gifts up to ensure appropriate acknowledgements are made?
- *Gift Aid claims*: Where eligible, reclaiming tax on Gift Aid donations boosts a donation by 25% (see chapter 10), but it is vital that the claims are made correctly. Who is responsible for ensuring Gift Aid declarations are requested from donors and recorded properly when received? Whose task is it to prepare the tax claims and submit them to **HMRC**? It will probably fall to the treasurer or finance officer to allocate any tax reclaimed on Gift Aid donations received to the appropriate funds in your accounting records, but is it the responsibility of the fundraiser to highlight where a donor has requested their donation be eligible for Gift Aid to the treasurer or finance officer? (Gift Aid is covered further in chapter 10.)
- *VAT considerations*: If your charity's fundraising involves selling goods or services, there may be VAT implications (see chapter 9). Who determines the VAT position of such an activity? Is the fundraiser aware of this, and how do they determine prices to allow for VAT?
- *Funders that require invoices*: Some grant funders require invoicing throughout the funding period. It is likely the treasurer or finance officer will raise these invoices, especially if your charity uses accounting software with an invoicing function. Who is responsible for determining when an invoice should be raised and how much it is for? Have VAT implications been considered? If someone other than the treasurer or finance officer raises an invoice, how is it communicated

to the treasurer or finance officer that a **debtor** must be reflected in the accounts?

- *Cash floats*: If your charity runs fundraising events and needs cash floats (a small amount of cash so that change can be given if someone only has large-denomination notes to pay for items on a stall), what procedures should be followed? Can the fundraiser hold a small petty cash float at all times (this may be sensible if events happen regularly), or should it be banked after each event? Who can withdraw the cash for a float from the bank?
- *Fundraising expenses*: Charity fundraising is not necessarily cost free. Even for a small event, there could be promotional expenses and supplies needed to run it. Who approves the expenses? And, if upfront costs are needed, are funds available to cover these? Fundraisers should keep a note of all expenses so that they can be included correctly in the accounts – they must be shown separately and not netted off the income fundraised during the event or appeal (see page 64).
- *Pledges of support*: In some circumstances, especially in a large fundraising appeal, some donors may pledge support in advance of actually making a gift. It may be only when the full target has been received or pledged, or perhaps on completion of certain milestones in the project, that donors make their payments. A fundraiser may feel that an appeal is complete when the target is reached, but who will then follow up the promises of support? This could be over a considerable period and reminders may be needed before all funds have been received.
- *Maintaining a fundraising database*: If you receive regular donations, or have more than 20 or so separate donors, a good approach may be to maintain a donor database. This can be used to keep track of who has donated what and where Gift Aid declarations are in place, and to provide contact details for donors for further appeals. Who should be responsible for this? Some of the information will form part of your **financial records** (the donation amounts and Gift Aid claims) so will need to be retained and subjected to **audit** or examination. But the donor details will be crucial for the fundraising team. Bear in mind that any personal data (including names, addresses, emails, etc.) are subject to the General Data Protection Regulation (GDPR).
- *Loan finance*: Fundraising does not only involve **donated income** or proceeds from fundraising events. If your charity is involved in a large project, loan finance may be required. How does this fit with the fundraiser's responsibilities or into any fundraising appeal they may be managing? Or is it only for the treasurer or finance officer to

manage? Obviously, all trustees will be involved in any discussion and agreements around taking on loan finance and the capital and interest payments required.

- *Independent fundraising teams*: If anyone is raising money on behalf of your charity as a third party, certain procedures should be followed (see page 144). Sometimes charities set up a subsidiary entity to manage their fundraising semi-independently. In these circumstances, the fundraiser, treasurer and finance officer need to be clear on whether the team is running events on behalf of the charity. If that is the case, all fundraising expenses and income should be incorporated into the charity's accounts. However, if the team is running events independently and then donating the proceeds to the charity, the resulting income will be accounted for as a donation.

The areas listed above highlight the wide-ranging interaction required between the accounting and fundraising functions of a charity. Your charity may have a policy of highlighting the names of donors in your **annual accounts** (though donors who are individuals should generally be anonymous unless they have specifically agreed to be named). Most funders will want to see the annual accounts. Therefore, good communication between the fundraiser, treasurer and finance officer is essential in identifying the appropriate split of income for reporting purposes, making the necessary acknowledgements and meeting funders' requirements. A good relationship between the treasurer, finance officer and fundraiser may be easy to accomplish in your regular trustee meetings, but it can become more complex where there are diverse fundraising needs, or with several fundraisers and no overall fundraising lead.

Regulation and ethics in fundraising

Fundraising tends to be the most public-facing part of a charity's work, and so building good relations with donors and following relevant guidance are essential to get it right. Negative publicity from bad fundraising practices can undermine both your charity itself and the wider sector. The **charity regulators** provide comprehensive guidance for trustees to ensure they understand they are legally responsible for their charity's fundraising practices and take responsibility for its fundraising. See the links in the 'Useful addresses' section on page 319 for more details on guidance from each of the three charity regulators in the UK.

Fundraising regulation

In England, Wales and Northern Ireland, the Fundraising Regulator (FR) is the independent regulator of charitable fundraising. Charities are encouraged to register with the FR to acknowledge their commitment to good fundraising practices and receive advice and guidance. Charities which spend less than £100,000 each year on fundraising costs can currently register with a £50 annual fee. In Scotland, the regulator is the Scottish Fundraising Adjudication Panel. At the time of writing, there is no fee in Scotland. Since 2016, the FR has been responsible for the Code of Fundraising Practice (www.fundraisingregulator.org.uk/code), which sets out the standards that apply to all UK charitable institutions carrying out fundraising and to third-party fundraisers.

The code is designed to be clear and reflect the current laws and regulations about fundraising, which come from various sources and evolve over time. It is set out in a series of standards that it is best practice to follow. All trustees are responsible for ensuring their charity follows these standards and they cover a wide range of areas, such as behaviour when fundraising, protecting donors' data, working with fundraising volunteers and third parties, and the particulars behind certain types of fundraising. This book does not look specifically into fundraising regulation; the purpose of this section is simply to highlight that if you have taken on the role of treasurer or finance officer, you should be aware of the code and how it affects your work. One example of this is your involvement in approving any literature where donors are promised that their gifts will be used in a specific way. You will need to be confident that the systems are in place to record and track such gifts, so they are allocated to the appropriate restricted fund, and that the promise fits with what your charity requires the donation for. Other examples that apply to the role of treasurer or finance officer include guidance on acceptance and refusal of donations, Gift Aid and cash collections, and payment of fundraisers.

The FR operates a complaints service where a member of the public can submit an online report of concerns over a charity's fundraising practices, and the regulator will investigate it (note that for charities registered in Scotland, such complaints need to be made via the Scottish Fundraising Adjudication Panel). Any serious complaints will likely be communicated back to the relevant charity regulator. The Fundraising Preference Service is also managed by the FR; this service helps people end any direct marketing contact with charities which they no longer want to support, and as such you may receive a request from the FR to stop sending materials to a particular named person.

The Chartered Institute of Fundraising, the professional membership body for UK fundraising, released a practical handbook in 2022 (available to download from https://ciof.org.uk/events-and-training/resources/trustees-and-fundraising-a-practical-guide) that sets out the responsibilities of trustees in respect of fundraising practice. The institute's website (www.ciof.org.uk) has useful guidance and resources for charities (including separate guidance for charities registered in Scotland).

How to fundraise ethically

The Code of Fundraising Practice sets out the standards that must be followed. However, standards are not ethics. Ethical fundraising is more of a framework about what ought or ought not to be carried out. Each individual charity is responsible for determining how the standards are applied in the context of its principles. This involves not just looking at the charitable activities of your organisation but also considering potential ethical impacts on all your stakeholders – such as trustees, volunteers, beneficiaries, donors and staff.

For example, the code sets out that 'you must not refuse or return donations, except in exceptional circumstances', and if you do refuse a donation, you must keep a record of why it was refused.[10] There may be legal reasons why the donation cannot be accepted, such as where there are concerns over its legitimacy (for example, if the origin of the funds is questionable or if the Proceeds of Crime Act 2002 should be considered). But there may be ethical reasons too. A common example is whether it is suitable for a cancer charity to fundraise by investing in cigarette and alcohol companies, or if a charity set up to help those with gambling addictions should accept funding from lottery operators. There are no right or wrong answers to these types of decision, but having a framework in place will help trustees to navigate the possibilities and reach a conclusion.

It should be noted, though, that your ethical fundraising framework should be guided by the perspectives of your beneficiaries and wider charity stakeholders rather than the personal views of your trustees. For example, people holding cash collection tins at local supermarkets can be contentious. However, when carried out following the guidelines set out in the code, this can be a successful form of fundraising and promotion of a charity in the local community. Therefore, trustees should not simply disregard this option because they do not like the idea of directly appealing in that way – they must consider the positive effect it could have on the charity and its beneficiaries. Of course, there may be legitimate reasons why the trustees do not use this direct method of fundraising; inviting small cash gifts at the local supermarket may not be as successful as seeking regular monthly giving by direct debit, for example. But the decision has to be made from the point of view of the charity and beneficiaries, not based on the personal choice of the trustees.

How your charity is portrayed in fundraising literature may also involve ethical considerations. What is the right way to represent beneficiaries? Images and narrative must deliver a strong case for support but must not degrade beneficiaries in any way. And your materials should not be misleading. Although, as treasurer or finance officer, producing fundraising literature will not necessarily be within your remit, this is still something to be aware of, especially as you may be required to provide relevant financial data. For example, it can be useful to include in fundraising literature what something costs, such as '£20 could fund a volunteer to attend a first aid course' or '£500 could pay for a trip to the local activity centre'. Some charities even state how much of a donation is spent on charitable activities – for example, '85p in every £1 donated is used to support our outreach work'. However, donors should not be misled to think they are buying something specific (unless a specific restricted fund is intended; see page 36 for more examples), and as the treasurer or finance officer you should be able to justify any of the figures provided.

Acceptance of gifts

As noted above, there may be instances where it is right to decline a gift. Donations that are given with strict conditions, or where the donor dictates who or what the money should be used for, require careful consideration. If those conditions fit with your **charitable purpose** and can be managed in your accounting systems, the donation may be acceptable. But some restrictions may be so tight that it may simply be too much work to justify a restricted fund to carry out the work required under one specific gift. It may also be necessary to consider the Equality Act 2010. For example, a charity could not accept a gift with conditions on the race of beneficiaries unless it was for a project addressing disadvantages experienced by people of a specific racial or ethnic background.

It can be damaging for a charity to accept funds that require it to carry out particular work but do not cover all the costs (see page 131). Unfortunately, sometimes people will accept funds and commit a charity to a new project without it being formally costed. As the treasurer or finance officer, you should make fundraisers aware that any gift that involves specific work should not be accepted until the finances have been approved. It is very easy to forget about extra costs, potential VAT implications and overheads when a large offer of a donation has been made. If it is subsequently discovered that the funding will not cover the costs, the trustees will then be faced with difficult discussions with the funder about how the shortfall will be met or if the scope of the project can be reduced. Your charity will appear much more professional and capable to the funder if these conversations happen before a donation is accepted. Having them afterwards will likely damage your relationship with the funder and potentially your charity's wider reputation.

Third-party fundraising

Charities often enter into agreements with third-party providers of fundraising support. This can take various forms, but three common types to consider for you as a treasurer or finance officer are using volunteers to carry out fundraising on your behalf, employing the services of a **professional fundraiser** and having a commercial relationship with a local business.

In all three of these arrangements, it is essential to have some form of agreement in place to clearly set out the terms and expectations. It is very easy, when involved with a charity you feel passionately about, to believe everyone feels the same way and therefore not contemplate that a formal agreement is needed. But, in order to act in the best interests of their charity and to safeguard its **assets**, trustees and staff must consider what would happen if something went wrong.

The following is not an exhaustive list of where you may find yourself working with a third party to fundraise, but the points highlighted will also be relevant in other situations. The Code of Fundraising Practice sets out useful guidance, and you should always seek professional advice where you are unsure. Note that for any arrangement where a third-party organisation is promoting your charity on its premises, in advertising or by placing content about your charity on its website or social media, you must ensure the information is accurate and not misleading.

Fundraising with volunteers

There are two main ways volunteers can fundraise to support your charity: on behalf of the charity and in aid of it. The distinction is important, as they have different implications for the organisation.

On behalf of your charity

Where volunteers are raising money on behalf of your charity, you must make sure that they have all necessary guidance, information and support to fundraise in line with any standards and ethics applicable to your charity. Any unauthorised or inappropriate fundraising by a volunteer may backfire on your charity, and the trustees may be held responsible. In this type of fundraising, your charity will probably have established, or been involved in setting up, the fundraising event and organised volunteers to take part. This means the volunteers will be under the instruction of your charity. Therefore, in a well-run charity, they will also previously have received the training and equipment they need to carry out the tasks assigned to them. It is important volunteers are aware of the processes your charity requires them to follow in relation to handling donations and that they know they should pay money raised over to your charity quickly. Note that you cannot make payments to volunteers, although you can reimburse reasonable volunteer expenses (see chapter 11).

In aid of your charity

An alternative is volunteers raising money in aid of your charity. For example, in this situation, a volunteer (or group of volunteers) may organise a coffee morning or take part in a challenge event stating that all proceeds will be given to your charity. This often happens where someone is not a formal volunteer with your charity but has some link – they may be a beneficiary or a family member of someone who has been supported by your charity. Quite often, as a treasurer or finance officer, the first you may hear that someone has raised money in aid of your charity is when they contact you with a donation or ask for bank details to pay money into your charity's account.

This type of fundraising is independent from your charity. If you do know a volunteer is going to raise money in aid of your charity, it is important they use the expression that they are raising funds 'in aid of Charity X' to distinguish their fundraising from that controlled by the charity. You must also ensure that volunteers know that they are responsible for all aspects of their fundraising and that your charity will not accept any liability relating to it. However, it is practical for you to supply them with the correct charity name and number, and relevant promotional materials, if you know their intentions in advance. If you are not aware in advance that someone is raising money for your charity, once the donation is received you could send a letter of thanks together with some charity literature and information that the fundraiser could use in the future.

Working with professional fundraisers and consultants

You may employ the services of a **professional fundraiser** (any person or organisation carrying on a fundraising business and charging a fee to raise funds for you) for a variety of reasons. They may look at your overall fundraising strategy and identify target funders to approach or provide ideas about how your charity could raise funds in other ways. Some fundraisers may be appointed for a specific task – such as to complete a funding application or organise a particular fundraising event. It is essential to set out your expectations and remain involved with the process to ensure the fundraiser delivers in line with your charity's purposes and values. In other cases, a charity may prefer to engage a **fundraising consultant** to provide advice on fundraising plans and perhaps to draft appeals – but without them being authorised to approach donors or funders directly.

Whenever a charity takes on the services of an independent adviser or professional fundraiser, it is best practice to carry out some initial research. This may include obtaining quotes from two or three suitable candidates, asking for references to check their experience and qualifications, and considering potential conflicts of interest.

If you work with external professionals, it is important to have a **contract** in place which is clear to understand and proportionate to your charity and the fundraising task in hand. In the case of a professional fundraiser who is authorised to contact supporters directly, this is a legal requirement – for details see the Code of Fundraising Practice (section 7). As well as setting out the details of the parties involved and the expectations, the agreement should also set out how GDPR requirements will be satisfied, confidentiality, timescales, and fees and expenses that will be paid. As the treasurer or finance officer, you will need to be aware of payment amounts and deadlines so that these can be factored into your financial planning. And all trustees have a responsibility to ensure that the professional fundraiser's work is carried out appropriately, responsibly and following any specific guidelines and ethics you have in place.

There are important considerations when paying for the services of a professional fundraiser or consultant. It is worth noting that charities should not expect advice for free, but equally you will want to receive a good service for any fees you pay. You should be confident the external professional can meet your expectations and not damage your charity's reputation in any way. Therefore, any fees you agree to must be proportionate to the income that their work is reasonably expected to generate, and certainly not excessive.

Most professional fundraisers and fundraising consultants will quote their fees on a daily rate and should provide an estimate of how many days of work a particular task will take. You can ask them to monitor this and send updates so you are aware of, and can approve, any additional work to avoid a nasty shock when the final invoice arrives. There can be a misconception that fundraisers will charge using a commission-based approach – for example, asking for 10% of the grant applied for or the income raised at a fundraising event. The FR strongly advises against this in the Code of Fundraising Practice (section 2), and some professional fundraising membership bodies prohibit it. This is because a commission-based approach prioritises personal gain over what may be in the best interests of the charity, going against the value of trust that charitable giving is based on.

Note that professional fundraisers are required to declare (either verbally when approaching a potential donor or in appeal materials) the name of the charity they are raising funds for, the proportion of the funds that that charity will receive, and how the professional fundraiser's payment in connection with the appeal will be calculated, including the amount or estimated amount to be received. Where the professional fundraiser is an organisation, this is the amount due to the organisation, not the individual.

Commercial arrangements

A potentially good source of fundraising for a local charity is partnering with a local business or shop. This may involve the business promoting your charity in its literature or providing in-kind support, advice or fundraising. For example, a business may choose you as its charity of the year and encourage its staff to take part in fundraising events, all proceeds of which will be donated to your charity. This has advantages for both parties. For the charity, it provides an income stream and increased awareness within the local community; for the local business, a commitment to support a local charity may be a selling point for potential customers. There are various ways in which such a commercial arrangement may take place. For example, a local shop may sell items made by your charity, or a factory could donate 50p from every sale of a particular item it makes. When carrier bag charges were introduced (since 2015 effective in all of the UK), some retailers decided to donate the sales of those bags to specific local charities.

If a local business simply donates some funds to your charity without making any claim that it is acting on your behalf, the money can be treated as a donation and no agreement needs to be in place. However, if someone, in the course of carrying out their business, promotes goods or services on the basis that it will make donations to a charitable institution, they are classed as a **commercial participator**. Any such relationship your charity has with a commercial participator requires an agreement to be in place, and your trustees should enter into this kind of partnership with due care. If you find out that a business is making such a link to your charity without your knowledge, you must put an agreement in place or ask them to stop.

Where you do enter into an agreement, you should understand why the business wants to align with your charity and check they are a suitable fit for your charitable purposes. For example, would your beneficiaries find it appropriate for your charity to be associated with a particular product promoted with '£1 of all sales are donated to Charity X'. Are there any conflicts of interest? For example, it would not be appropriate for a trustee, or person connected to a trustee (see page 25), to be selling goods in this way as it could be perceived that the trustee (or their connection) was using the name of the charity to make sales for their own personal benefit.

Once it has been determined that the arrangement is suitable for your charity, a written commercial participator agreement must be adopted which sets out the terms and conditions of the proposed activity. This must include what proportion of sales will be donated to your charity, how this will be calculated and paid to your charity, and any fees the business may charge your charity.

Technology in fundraising

Technology is playing an increasing part in raising donations from individuals. The power of social media and the use of online giving platforms were particularly highlighted during the COVID-19 pandemic, when fundraising activities quickly went viral raising millions (for example, to support NHS charities). For more local charities, embracing such technology can also be extremely rewarding.

Having an online presence is becoming ever more important for any charity, including having a website and one or more social media accounts. The channels you use should be appropriate for what your charity wants to achieve. The common ones, such as Facebook, Twitter and Instagram, have a wide reach, but if your target demographic is younger people, there are new platforms being set up all the time. If you do not have technologically savvy support within your charity, it may be beneficial to take on the services of a digital or marketing consultant. But in any event, when using social media to promote your charity and any fundraising, it goes without saying that the content should be accurate, timely and appropriate to your charity's fundraising – and should link to the ways in which donations can be made.

Online giving platforms

It is possible to host your online donation page through your own website, and most website designers will be able to incorporate this, with the donations to your charity managed through a banking application (for example, PayPal, Stripe or a similar provider). You will need to highlight any fees charged for administration and processing costs by the payment providers on your website so that donors know how much of their donation will actually reach you. Once the donation links are set up, it is important to ensure ongoing maintenance, such as checking that they continue to work. If someone cannot make a donation easily, they will donate elsewhere. Where your charity uses an online donations page on your website, as the treasurer or finance officer, you will need to give input on what data is captured so that you are able to recognise the donations coming into your bank account and what they are for, especially where a restriction is made on a gift. Make sure you ask for the donor's email address so you can respond with a message of thanks, and be sure to ask whether or not they are willing to receive future communications, to ensure you are complying with GDPR.

Third-party online giving platforms are popular alternatives for smaller charities. The more well-known ones (such as GoFundMe and JustGiving) are very user-friendly for both charity and donor. The charity can set up its own fundraising page and add the content it requires. Some platforms provide a button or QR code to add to the charity's own website or social media that will then take potential donors directly to the giving page. Platforms also provide the ability for donors to share that they have donated among their own network, increasing the reach and awareness of your cause.

If individuals fundraise in aid of your charity – such as by taking part in a challenge event and asking for sponsorship from their friends and family to go to your charity – they can link their own fundraising pages to your online giving account. Equally, individuals who want to give one-off or regular donations can look for a charity on an online giving platform and donate that way. This means that individuals not already associated with your charity may find out about your cause and support you.

There will invariably be fees associated with online giving platforms. Given their rise in popularity, there are now a number of platforms so you should do your research to find one that meets your needs at an acceptable cost. There are various types of fee to consider. A charity may need to pay a membership fee. In some cases, this will be a one-off initial set-up fee, or it may be an annual fee or a monthly fee paid by direct debit. Options may be available for a basic package with no fee, but you should check this meets your charity's needs.

There is usually a processing fee for payments. The donor is not charged this fee; however, sometimes they are given the option of paying a small contribution in addition to their donation towards costs. Typically, the processing fee levied on the charity is a standard charge and/or small percentage of the donation. The platform charges this fee to cover the costs of processing the various payments through credit cards, banks and similar. Note that some platforms levy substantial administration charges on the donor unless the donor specifically goes through several steps to opt out. Where they do opt out, the charity sometimes incurs the charges but it may be better for the charity to accept a small processing charge rather than have donors feeling that they have to spend more than they intended once admin charges are added.

Most online giving platforms offer a Gift Aid facility. At the time of making their gift, the donor can make their Gift Aid declaration, and the platform will take care of reclaiming the tax on your behalf. In this situation, there will likely be a small percentage applied to the total amount of the tax reclaimed under Gift Aid to cover the processes involved in making the claim to HMRC.

Your charity will receive payments of donations made via online giving platforms on a regular basis, but the frequency will depend on the platform and the number of donations. The money will come directly to your charity's bank account in a lump sum payment, often combining several donations and Gift Aid claims together, and after deduction of any associated fees. Someone will then be responsible for processing such funding in your charity's accounting records, but this can be a complicated and time-consuming exercise, especially if the donations could belong to several different restricted funds.

To assist with this, the platform providers usually offer a reporting function. This means that, as the treasurer or finance officer, you will need access to the platform to download reports so you can update your charity's accounting records. These reports may include invoices of fees charged, details of payments made into your charity's bank account, and comprehensive data behind all donations and fundraising pages. The reports can contain a large amount of data – often in CSV (table) files with many rows and columns – but they should provide sufficient information for you to pull out total fees charged and identify each donor. Remember that donation income should be reported gross and by specific fund in your accounting records, with the total fees recorded on the expenditure side (see page 64).

Other cashless donations

Charities need to make the donation process easy if they want to maximise their return from individual giving. Many people no longer carry cash with them, so you may need an alternative if you wish to use collection boxes, take donations at an event or even charge **fees**. It is also worth noting that some banks charge fees to charities, and those for banking cash can be quite substantial. There are several avenues available for cashless donating, and they are constantly evolving (some may work better for certain activities than others). As the treasurer or finance officer, it is likely you will need to investigate some options, and you should always bear the financial reporting implications in mind. Some options for cashless giving include:

- *Bank transfer*: This will be the easiest and cheapest option for your charity, as there will not be any additional fees to pay or data collected by a third party to analyse. However, expecting people to have their bank details to hand and give them out at a fundraising event is not ideal. It is open to error and quite cumbersome for the donor in comparison to other methods.
- *Online giving platform*: As previously discussed, this is a convenient way to donate but still means a donor must log on and fill in a number of fields in an application form to make the donation.
- *Text message*: This option has been popular over the years with large charities, especially for one-off events and campaigns (for example, Comic Relief telethons and Disasters Emergency Committee advertising appeals). But charities of all sizes can use this option by signing up with a text-based giving service provider and gaining access to a portal where they can set up a 'text to donate' campaign. You will need to set up a keyword that represents what the donation is for, probably ending in a number that represents the amount of the donation. You will then need the short code which the message is texted to – the platform provider will offer the short code. This will

result in an expression to add to your fundraising material in the following format:

Text KEYWORD5 to SHORT CODE to donate £5.

You will also need wording for a short thank-you message that will be sent back to the donor automatically on receipt of the donation text. The provider will pass on any donations received this way (less fees) to your charity's bank account and should provide reports, which will be similar to those discussed for online giving platforms, to enable you to analyse the donations.

- *Tap-and-pay devices*: There are several options available for simple contactless mobile tap-and-pay devices that link to a smartphone through a Wi-Fi connection, are battery operated and can be used anywhere to take payments. The payments will then be transferred to your charity's bank account, less any fees. They are designed for small businesses, so may not have specific charity functionality (such as being able to provide a Gift Aid declaration or show suggested donation amounts). Nevertheless, they provide a quick and easy way for donors to give a donation of an amount they choose.
- *Contactless charity donation boxes or plates*: These traditional methods of gathering cash donations are being replaced with digital touchscreens (usually freestanding) that can be either a permanent fixture on your charity's premises or portable to take to events. They usually allow you to display content on the screen to promote your charity. The touchscreen allows interaction and provides prompts for differing levels of donation and Gift Aid declarations, and offers contactless technology. As they are specifically designed for the charity sector, they provide data analysis to enable you to track donations.
- *QR codes*: A QR code is a square containing a pattern that donors can read with their smart device. It can be placed anywhere – on your digital media but also printed onto leaflets and even T-shirts. The QR code can then link to various destinations depending on the application provider's options and your charity's preference. For example, it could link to an online giving platform, a text-to-donate app, or a payment-taking application where the donor can input their details and pay directly with their card or smartphone. This means that QR codes can be flexible and reach a wide audience. Charity-specific suppliers may also produce useful data analysis.
- *Micro-donations fundraising apps*: Several online providers allow a charity to sign up and for consumers to nominate a particular charity for small donations. This can involve rounding up the pence in a

particular transaction (for example, rounding up a payment of £9.75 to £10, with the extra 25p going to the charity) or providing cashback on purchases. These are the digital alternative to collection tins at shop checkouts where consumers could deposit their spare change, and so money collected in this way can be added to your accounting records as general donations rather than anything specific. Note that a company receiving funds on behalf of a charity in this way will generally be acting as a professional fundraiser (see page 146) and/or commercial participator (see page 147), so a clear written agreement with the charity is essential.

These are all examples of ways you can encourage your donors and supporters to give to your charity electronically. It is probably worth considering adopting at least one, according to what would best fit the needs of your charity and donors.

Cryptoassets

Recent developments in technology have led to the introduction of cryptoassets. Cryptoassets are built on blockchain, a technology where records of data about past transactions are bound together and shared by a number of computers. No single organisation or individual holds the 'key' to the blockchain, and such transactions are thought of as transparent and secure. Cryptoassets use this technology to create an encrypted digital representation of something of value which can then be used in an exchange transaction between different parties. Cryptocurrencies are the most common example of a cryptoasset (a well-known example being bitcoin). Although blockchain technology is thought to be secure, the value of cryptoassets can change dramatically, suddenly rising or falling, and there are concerns they can easily be misused or stolen.

A very small number of charities are starting to use cryptocurrencies. While CCEW encourages innovation, it warns of significant risks in this regard.[11] Cryptoassets tend to be used for specific reasons – for example, international charities may use them to move currencies across borders where banking services are unregulated. However, some charities are now accepting cryptoassets as donations too.

Where you receive a donation in a cryptocurrency, there are two options. Probably the safest is to immediately convert the cryptocurrency into a traditional currency (i.e. sell it to generate money). Alternatively, you can hold and trade it as you would any currency, avoiding the need to use the banking system. This could be much riskier than traditional banking and

investment due to the volatile nature of the asset and would no doubt need the support of experts in this field.

Non-fungible tokens (NFTs) are another type of digital asset, constructed using blockchain technology. 'Non-fungible' means they are a one-off and cannot be replaced. Digital artwork is an example. Although these are not traded like a currency, they can be sold to the highest bidder and therefore are similar to an actual piece of artwork donated to a charity to sell at a charity auction.

It is possible that the regulators will introduce guidance and even toolkits to help charities manage cryptocurrencies and NFTs. However, while this is being developed and the technology evolves, charities should be aware about three significant risks of digital assets: exposure to volatility in value of the cryptoassets, cybercrime activities and not knowing who the donor is.

Trustees should remember their core duties (see chapter 2) when accepting or investing in cryptocurrencies or NFTs, and not put the charity's assets or reputation at risk. Benefits and risks should be evaluated, professional advice sought and any decisions documented. As the blockchain technology relies on anonymity and secrecy, trustees should consider whether they really know the donor before accepting any gifts of cryptocurrencies. At present such donations do not qualify for Gift Aid, and the exposure to other taxes is not yet known.

Costs of fundraising

If you produce **accruals accounts** in line with the charities **SORP** (see chapter 14), and as good practice even if you do not, there should be transparency about all your fundraising costs, to ensure your charity is not paying more in costs than it generates from fundraising activities themselves. When you are maintaining your charity's accounting records, it is therefore necessary to be able to identify your fundraising costs. They include your outlay for:

- applying for grants;
- actively seeking donations and legacies;
- managing Gift Aid records and claims;
- third-party charity giving providers;
- promotion and advertising where its main purpose is to attract donors;
- investment management (see below).

This list is not exhaustive, but it does illustrate the wide variety of fundraising costs a charity may incur. In some cases, costs will be easy to identify as direct outlay for a fundraising activity – for example, the costs charged by an online giving platform or an advert seeking donations. However, other costs may need to be calculated using estimates – for example, the staff time involved in completing a grant application or managing donor relationships. To calculate these costs, you could estimate the proportion of the relevant staff member's time allocated to the task, and a similar method could be used to estimate the overheads incurred. Refer to page 131 in chapter 6 for further details.

Although managing investments is not thought of as traditional fundraising, it is a method of bringing money into a charity to fund its charitable aims. Therefore, if your charity holds investments to provide a source of income (interest, dividends, etc.), the costs of managing those investments are also treated as fundraising costs. For example, this includes fees for portfolio management, investment advice and, where property is held as an investment, the costs of managing the property, repairs, maintenance and collection of rent.

This chapter has highlighted what, as the treasurer or finance officer, you need to be aware of in the wide-ranging topic of fundraising. You may not be specifically involved in the fundraising at your charity, but it is important to be aware of what is being raised, by what means, what it relates to and how much it costs, so that it can be accounted for correctly and reported appropriately in your charity's accounts. The next chapter looks at the topic of charity trading, including **trading for fundraising purposes**, and how you can assess how worthwhile a fundraising activity is by looking at its return on investment.

8 Charity trading

Donated income is often the main source of a **charity's** funding; however, **trustees** have no real control over what is received as they rely on the generosity of others. Therefore, charities may want to find alternative sources of funding to develop their sustainability. Generally, this means delivering services or goods that they can sell. This could be in the form of providing services for a local authority under **contract** or perhaps selling tickets for an event. In these situations, the charity is *trading*.

This chapter considers the various types of trading a charity can engage in: **primary-purpose trading** and **trading for fundraising purposes**, including running a **charity shop**. It examines some of the costs that you may incur in trading and introduces the concept of measuring return on **investment**, which allows you to evaluate how successful your charity trading opportunities have been (and thereby forecast the potential benefit of similar activities in the future).

Trading income

As outlined in chapter 6, charity income falls into three main categories: gifts (**grants**, **donations** and legacies), trading (selling goods and services) and investments (such as bank interest, rents and share dividends). However, in some cases, this is not clear cut. Something that looks like a grant may actually be a contract (trading), or income from a **fundraising** activity may actually be charity trading rather than donated income. It is important to make these distinctions not only for the sake of classification in your **annual accounts** but also, more crucially, due to the tax implications (see chapter 9).

Understanding the difference between donated and trading income

Donated income is given to a charity on the basis that the **donor** will receive nothing in return, other than the expectation that the funds will be used to further the **charitable purposes**. As explained in chapter 6, the term 'grant' tends to relate to funding received from organisations and the term 'donation' is often used to mean a gift from an individual. Donated income falls under *trust* law, and donations to a charity are not subject to taxes.

On the other hand, **trading income** is that derived from an exchange of goods or services; an individual or organisation pays money to a charity but receives something from it in return. This is essentially a commercial agreement and is covered by *contract* law, and there may be tax implications. Figure 8.1 reflects these different funding channels.

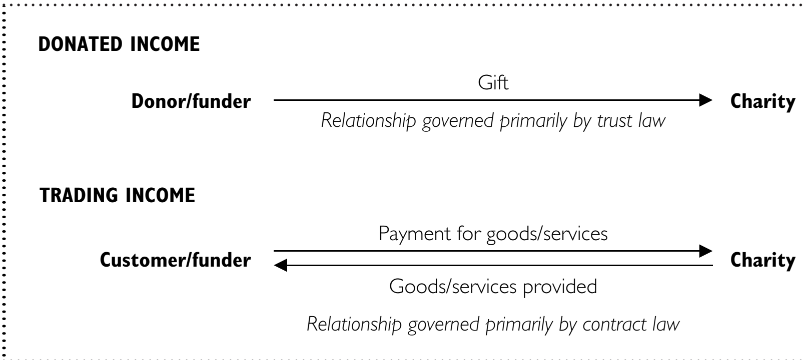

Fig. 8.1 The two main funding channels

As an example, consider a local authority that provides a charity with £50,000 to fund a service. The money could be provided as a grant, with conditions such as what it can be used for, timelines for spending and details of when unspent portions should be returned to the **funder**. However, the local authority is not buying anything specific. In this case, the grant needs to be treated as donated income (possibly restricted) for tax purposes. However, if there were terms in the funding agreement specifying that the funder was purchasing a specified number of places for a **fee** of £50,000, the local authority would not be providing grant funding but would essentially be procuring services. If the services were not up to standard, the funder could in theory sue the charity for breach of contract. But, if the charity completed the work as agreed, it could retain any **surplus**. This would need to be treated as trading income, and there could be tax implications.

Sometimes it is not clear whether funding, particularly from government and local authority sources, is a grant or contract. Although some **SLAs** have pages of conditions, they do not always make it clear whether a grant or contract is intended. Often the funders themselves are not clear, making it very difficult for the charity to determine the type of funding. This not only affects how the money is accounted for – in terms of whether a restriction applies (see figure 8.2) and in which category of income it should be shown in the accounts – but could also lead to huge differences in the VAT position (see chapter 9, especially page 180, for more on VAT).

Getting this wrong could have serious financial consequences for your charity.

As the **treasurer** or **finance officer**, you will need to be clear about the treatment of any grant or contract and advise the trustees of any impact new funding may have on your charity's finances, before the agreement is signed. When it is not obvious, it is perfectly acceptable to go back to the funder and ask them to make clear their intentions and amend the agreement if needed. It is better to delay the project and have clarity than jeopardise the finances of your charity where VAT implications have not been considered, as you might suddenly find out that they apply.

GRANT AND CONTRACT INCOME

TREATMENT OF INCOME	UNRESTRICTED	RESTRICTED
DONATED INCOME	General donations	Grants for a specific purpose are always restricted
TRADING INCOME	Normally unrestricted as the only obligation is to provide the goods/service – the charity can retain any surplus	Only restricted if customers were promised surplus funds would be used for something specific (e.g. an event to raise funds for a specific project)

Fig. 8.2 Accounting for grant and contract income

Trading does not only apply to public sector contracts. Whenever your charity provides goods or services, either in the course of carrying out its activities or by providing access to a fundraising event, and charges the recipient a fee, it is trading. You must consider whether this is primary-purpose trading or trading for fundraising purposes. This distinction is critically important for corporation tax purposes (see page 170).

Primary-purpose trading

This type of trading happens whenever you make a charge or request a fee for goods or services which are provided *directly as part of your charity's purposes*. Some common examples are:

- course fees charged by an educational charity;
- rents charged by a housing charity;

- fees for weddings or funerals charged by a religious charity;
- fees charged by any charity to access its services;
- publications and books sold by a charity where the content relates to the charity's purposes;
- membership fees charged by a charity where the member gets a definite benefit under the charity's purposes (if there is no benefit, the member's subscription is a donation);
- fees charged under contract with the public sector for health- or disability-related services which are delivered as part of a charity's purposes.

Most primary-purpose trading income will be unrestricted, which means the charity will have relative freedom in terms of how it can be used to further the charity's purposes. This can make contract income (which is generally trading income, as explained in the previous subsection) more attractive than a grant. You may find it helpful to use a **designated fund** to manage a certain contract-funded project, but there will be no restriction on how any potential surplus is used. This is unlike what happens with a grant, where any unused funding often must be returned to the funder. Bear in mind that VAT often has to be considered for primary-purpose trading.

Primary-purpose trading does not mean the customer has to be a public sector body procuring services. It covers any fees you directly charge for your charity's activities. For example, a youth club may charge an attendance fee, a welfare charity's beneficiaries may pay for services under a **direct payments** scheme, an arts charity may sell tickets for a performance, or a refuge charity may receive rent from (or on behalf of) its tenants for providing temporary accommodation.

If you engage in primary-purpose trading, it is crucial to consider how to price the goods or service you provide. Since the trade is seeking to advance your charity's purposes, the charges you set should aim to break even, rather than make a profit. And keeping fees low will make your goods or service attractive to more people. However, there is a distinction between whether those buying the goods or service are the funder or the beneficiary using the service. For example, if you are pricing contracts for services to a local authority funder, you will need to ensure all costs are considered (see page 164). But if you are charging a fee directly to people using the service, it is likely you will want this to be set low and be subsidised from your charity's other funding.

As discussed in chapter 1, charities are subject to a **public benefit requirement**, and setting high fees which mean your charity's services can only be used by a limited number of beneficiaries may breach this requirement. The ability to pay should not be a barrier to accessing your charity's services, even if the aims of your charity are unrelated to poverty. You may serve some beneficiaries who are nominated by a funder (such as a local authority setting out conditions on whom its funding covers) and also other beneficiaries. Your trustees will need to decide how the different fees and charges are managed, or whether to raise other funds specially to support beneficiaries not covered by the funder's provisions.

Although carrying out work under a contract is likely to be primary-purpose trading, there are exceptions. For example, if a charity's purposes are to provide services for young people under the age of 18 who have a disability and live in a particular local authority area, then a contract to run a youth club for individuals meeting that criteria would be primary-purpose trading. However, if the charity received a contract to extend those services to young people between the ages of 18 and 25, or to a neighbouring local authority area, that would no longer be primary-purpose trading. Even if the youth club was run in exactly the same way, the fact that it was for young people outside the remit of the charity's purposes would mean that the contract covered trading for fundraising purposes (for more detail see the section just below on trading for fundraising purposes).

There is nothing stopping you from providing a service outside your charitable purposes, but this could significantly affect your tax position (see chapter 9). For a one-off contract this may not be an issue. However, if this became a regular service, it might be beneficial to consider changing your charity's purposes to widen the age or area of benefit, for example.

Trading for fundraising purposes

When you carry out trading other than for the primary reason of meeting your charitable purposes, it is classed as trading for fundraising purposes (sometimes referred to as non-charitable trading income or non-primary-purpose trading). Some examples include:

- selling tickets for a fundraising event;
- selling raffle tickets (not a donation as the buyer receives something for their donation – a chance to win a prize);
- selling charity cards or calendars to raise money;
- providing advertising or sponsorship opportunities in return for payment;
- selling donated goods in a charity shop or jumble sale;

- selling your charity's services in a way that is outside your purposes – for example, renting out rooms to commercial organisations or courses to people outside your charity's beneficiaries.

The income generated is used to deliver your activities, which meet your charitable purposes. As trustees must always act in the best interests of their charity, they must ensure that any trading for fundraising purposes does not pose a significant **risk** to the resources of the charity – for example, if the intended trading could damage the charity's reputation if it failed, put supporters off donating to the cause or lose the charity money (see chapter 5 for more on risk). Although the fundraising activities do not need to be linked to the purposes of your charity, they should be compatible with your charity's general ethos, as discussed in chapter 7, and not adversely affect its reputation. Where there is any risk, you could consider using a **trading subsidiary** to carry out the activity (see page 202).

Trading for fundraising only makes sense if it generates worthwhile funds to support other activities that fall within your charity's purposes. Care must therefore be taken to ensure any costs involved in raising this income do not outweigh the funds generated – they should be profitable activities. As the treasurer or finance officer, you will be required to identify those costs and consider how worthwhile the activity is. You will also need to be aware of whether the activity would produce taxable income (see chapter 9).

In some cases, charities can make sales without the activity being considered trading for tax purposes. Examples include selling charity investments or property and selling donated goods as long as they were given to the charity for that purpose. In addition, there are two forms of trading that have special tax circumstances to be aware of: **ancillary trading** and **trading by beneficiaries**.

Ancillary trading

You may hear the term ancillary trading – an activity carried out that is in addition, but linked, to your primary purpose, to complement your charity's purposes. This is trading for fundraising purposes, but a distinction can be made that is particularly important for corporation tax (see page 170). An example would be a charity that runs an art gallery also running a café. Where the café is solely for the use of those visiting the art gallery, it is classed as ancillary trading. If the café is also open to the general public who are not visitors to the art gallery, then it is trading for fundraising purposes.

Trading by beneficiaries

In some charities, funds are raised by the beneficiaries themselves delivering a service or selling goods that they have produced. Such activities include cafés run by people with learning difficulties in a disability charity or sales of crafts made by young people in a youth charity. The trade itself is for a fundraising purpose rather than primary purpose. However, because the bulk of the work is carried out by the beneficiaries the charity exists to support, there are corporation tax exemptions.

Charity shops

Charity shops are a familiar sight in UK high streets, and many do a roaring trade. There are charity shops raising funds for the very large national charities, and it is becoming more common to see regional and local charities setting up a charity shop – even small and medium-sized charities may run a charity shop or two.

The purpose of a charity shop is usually twofold: to raise money from the sale of donated goods and to raise the profile of the charity in the local area. Although shops can be a sustainable way of raising money for a charity, they are not necessarily simple to run. If, as the treasurer or finance officer, you are involved with a charity that has a shop, or is thinking of setting one up, there are various points to consider from a finance perspective.

You will need to draw up a **budget**, looking at the costs of running a shop compared to the income it is expected to generate, to assess the viability of the idea. Occupying a prime high street space can be costly in terms of rent and rates (although rates relief will probably apply – see page 186) but will provide higher footfall than a more out-of-the-way location. There will be the costs of fit-out and ongoing repairs, and statutory obligations as a retailer, such as insurance, health and safety regulations, and employment laws to consider. Understanding the typical monthly costs will allow you to work out the turnover needed to make the shop profitable.

The main purpose of a charity shop is to raise funds for your charity to use to meet its charitable purposes. A charity cannot use its charitable funds to subsidise an underperforming shop where running the shop is not part of its charitable purposes, so in such cases it is critical to ensure the shop can make a profit to support your charity's work.

If the shop is set up to sell only donated goods, this is not classed as taxable trading. Selling donated goods is treated as realising a donation into cash. This means that no VAT needs to be charged, no corporation tax is paid and Gift Aid can be reclaimed. Note that Gift Aid reclamation is subject to strict procedures; essentially, the charity acts as the donor's agent, and the donor must agree that the charity can keep the proceeds from selling the donated items (see page 195). Donated goods can be cleaned, sorted and repaired before sale, and selling them will still be classed as non-trading income. However, if the charity shop also purchases items to sell, this will be classed as a normal trade – a commercial activity which will attract taxes and may be best managed through a trading subsidiary.

Costs of trading

For you as the treasurer or finance officer, the financial management of trading activities requires a different approach from the management of activities funded by grants or donations. In particular, it is vital to know whether a trading activity is making a profit, breaking even or making a loss. (It is not meaningful to talk about 'profit' or 'loss' for a charity as a whole, as that is not the purpose of a charity, but it is perfectly reasonable, and usually vital, to look at the profit or loss on a specific trading activity.)

It is necessary to identify the costs incurred in each charity trading activity to ensure you are correctly pricing contracts, fees and tickets for events. You may have different pricing objectives for different activities – perhaps to break even when providing counselling services to young people under a contract with a local authority that fits with your charitable aims, and to make a surplus on selling places on a counselling training course to people outside your charity's beneficiaries. However, unless you can establish the cost of providing those services, you will not know what fees to charge, or how much surplus you are actually generating. If a fundraising trade was making a loss, that would be very serious as the activity would be draining your charity's other funds. In order to be effective, trading activities for fundraising purposes usually need to generate a significant return on investment (see the next section) to support your charity's core activities which advance its purposes.

There will be some costs that are easy to directly link to a trading activity – for example:

- the salaries or freelance costs of the people delivering a service or activity;
- expense payments to volunteers or staff involved in delivering a service or event;
- room or venue hire to deliver a service, activity or fundraising event;

- costs of any materials, refreshments or similar used to run an activity;
- payments to entertainment providers and caterers at a fundraising event;
- costs of advertising and selling tickets at a fundraising event;
- rent, rates and utility bills incurred to run a charity shop.

In contrast, other costs may need more consideration and even involve estimating an appropriate amount that relates to the trading activity – for example:

- *The cost of a charity administrator to organise the trading activity*: If half of their role involves administering a contract with the local authority to provide counselling services to young people, then 50% of their salary cost (including employer's costs such as National Insurance and pension contributions) should be included in the cost of delivering that activity.
- *The cost of a charity employee's time to plan a fundraising event*: For example, if it took someone one month to plan an event, then a month of their salary should be included in the cost of that event.
- *The use of a charity's premises to deliver an activity*: If the charity has a space which it uses to deliver training, then a proportion of the rent and any other relevant costs should be included as a cost in delivering that training.
- *Overheads*: An appropriate amount of the regular costs of the charity, such as insurance, telephone and computer costs, should be included in the cost of a trading activity.

Refer to page 130 for more details on how to ensure the costs of delivering a trading activity are fully considered. When you are looking ahead to price contracts, or set fees for services and fundraising activities, many of these costs will be estimates. However, using past experience and budgets and plans (see chapter 5), you should be able to identify a reasonably accurate basis on which to set prices or fees that will cover all costs, depending on the overall aim of the trading activity (see page 159).

Return on investment

When you are looking at trading activities for fundraising purposes, it is a worthwhile exercise to know how profitable a particular activity is and perhaps compare it with different activities that you could choose for raising funds. Many **professional fundraisers**, and charities which have large fundraising costs, use a metric called return on investment (ROI) to measure how successful a particular fundraising campaign has been. ROI is calculated as follows:

ROI = (Proceeds from fundraising / Cost of fundraising) × 100 = X%

where *proceeds from fundraising* is the total amount raised and *cost of fundraising* equals all costs involved in carrying out the fundraising activity. As the treasurer or finance officer, you may be asked to provide data to calculate the ROI, or even be involved in calculating it yourself for the monthly **management accounts** where fundraising is a key activity to be evaluated.

For example, let's say a charity applies for a grant and is successful in securing £10,000. To gather all of the information and complete the application form (including some unsuccessful applications to other funders), the fundraiser for the charity needed three days' work, which is valued at a cost of £750 in total, and input from the **charity co-ordinator** valued at a cost of £250. These costs also include an element for overheads (see page 131). So, in this case:

ROI = (£10,000 / (£750 + £250)) × 100 = 1,000%

This means that for every £1 invested in the grant application, £10 was raised.

The charity also wants to raise funds by holding a fundraising event and sells tickets to a summer garden party. The fundraiser spends one week organising the party, which represents a cost of £1,250 for their time. The catering providers charge £800, hire of the facility is £200, and a further £400 is spent on ticket printing and materials for the event. Therefore, the total cost of the fundraising is £2,650. The ticket price is £50 per head and the charity sells 100 tickets, giving total proceeds of £5,000. The ROI is calculated as follows:

ROI = (£5,000 / £2,650) × 100 = 188.7%

This means that for every £1 invested in the summer garden party, around £1.89 was raised.

Note that it is also possible to calculate ROI based on the net proceeds (after the costs have been deducted, to give a net ROI). In this example, the net proceeds after the expenses were £2,350, which gives a net ROI of 88.7% (i.e. (£2,350 / £2,650) × 100), or £0.89 for every £1 invested.

It is acceptable to calculate ROI using either total proceeds or net proceeds (after deducting expenses), and you can choose which version you prefer. The important point is that if you are going to compare them between different types of activities, or over time, you must use the same basis each time.

In the two examples above, the grant gives a much greater ROI than organising the event, as the costs are significantly less. However, there is always the possibility that grant applications will not be successful, and the fundraising event would do more to raise the profile of the charity in the local community. So, although ROI is a useful measure, it should always be considered in context with other non-financial outcomes of fundraising.

Also, with something like an event where you do not know in advance how many tickets will be sold, remember that if the expenses are fixed, the ROI could vary enormously depending on the level of sales. So, when preparing fundraising plans, it makes sense to allow for a range of outcomes in terms of sales: ideally the event should cover its costs (i.e. have an ROI of over 100% using gross proceeds) even with the lowest level of sales you could reasonably anticipate. Figure 8.3 shows the ROI calculated on gross ticket sales of £50 per head and fixed costs of £2,650 with sales of 50, 75, 100 and 150 tickets.

Tickets sold	**50**	**75**	**100**	**150**
ROI (gross proceeds)	94.3%	141.5%	188.7%	283.0%

Fig. 8.3 Example calculation of ROI over a range

The ROI results show that the event would not be viable for fundraising if only 50 tickets were sold, and even at sales of 75 there could be a question of how worthwhile the event would be. However, if 100 or 150 tickets were sold, it would be a very successful event.

The ROI measure can be used across all trading and fundraising activities and provides a useful comparison tool to aid decision-making.

This chapter has explained the wide variety of types of trading you can carry out either to meet your charitable purposes or as a method to raise funds. As the treasurer or finance officer, you must be able to distinguish which objective any trading meets due to the important tax conditions attached, which are explained in the next chapter.

9 Taxes, rates and reliefs

Not paying tax is sometimes thought of as an advantage of being a **charity**, but charities are not totally exempt from paying taxes. If you employ staff (see chapter 11), or if you trade to generate income or charge **fees** under a **contract** (see chapter 8), there may be taxes to pay and **HMRC** may require you to complete a corporation tax return. However, charities have several tax exemptions and can benefit from certain reliefs.

As the **treasurer** or **finance officer**, it is likely that dealing with any taxes will fall to you; therefore, having an awareness of potential tax implications is essential so you can provide relevant information to inform all of the **trustees**' decision-making. This chapter considers the taxes that you could face as a charity, the situations when a charity may be subject to corporation tax and the exemptions available, the circumstances where VAT will apply, and the potentially complicated issue of VAT recovery and partial exemption. For both taxes, the deadlines for returns and payments are explained. The chapter explores the specific situation of working together with another party and the VAT implications that brings. Finally, the chapter concludes with exemptions available to charities regarding other taxes and business rates.

Introduction to taxes

It is widely thought that charities do not pay taxes, but that is not necessarily true. Figure 9.1 provides a summary of taxes which may be applicable to charities and highlights whether special tax rules exist.

The figure shows that, as the treasurer or finance officer, you cannot just ignore taxes. There are many circumstances where tax needs to be considered, and for a charity the situation can be complex. There will be some charities – those which never employ staff or enter into trading relationships – where tax is never really an issue. But it is the responsibility of the trustees to confirm this is the case and monitor the situation in case it changes.

EXAMPLES OF TAXES WHICH MAY APPLY TO A CHARITY AND POSSIBILITY OF RELIEFS

Tax	No special relief for a charity	Some relief for specific situations	General relief for most charitable work
Employer's National Insurance	✓		
Insurance Premium Tax	✓		
Value-Added Tax (VAT)		✓	
Business rates		✓	
Corporation Tax			✓
Income Tax			✓
Capital Gains Tax			✓
Inheritance Tax			✓

Fig. 9.1 A summary of the main taxes a charity may be subject to, and an indication of where reliefs may apply

Tax law does evolve on a regular basis, particularly regarding thresholds, but this book highlights a few of the key tax issues to be aware of, and this chapter focuses on VAT and corporation tax. Employment taxes, such as National Insurance and PAYE (Pay As You Earn), are covered in chapter 11. You may find your **auditor** or **independent examiner** can provide some advice regarding VAT, but for all complex situations, it will be beneficial to consult a charity-specialist tax adviser.

Registering as a charity with HMRC

Whether or not your charity is subject to the taxes set out in the following sections, it will be worthwhile registering with HMRC. This allows HMRC to recognise your charity for tax purposes and for your charity to access relevant charitable tax reliefs and deal with Gift Aid **donations**. It is best practice to do this as a new charity is set up, but it can be done at any time (see chapter 1 for more information). Your charity may already have an account with HMRC. If so, you will have a Government Gateway login for HMRC online services. Details of the online process for registering with HMRC can be found on page 302.

Corporation tax

Corporation tax is a tax chargeable on business profits, where profits are calculated as sales income less any expenses. In reality, it is not this simple and there are various adjustments needed to determine your profit – i.e. the amount that is subject to corporation tax. Currently the corporation tax rate for small organisations, with annual profits of under £50,000, is 19%.

Charities are not fully exempt from corporation tax, although many will not pay the tax at all due to the various exemptions available. It is worth pointing out that any income donated to a charity, including **grants**, that is used to advance the **charitable purposes** is exempt from corporation tax. On the other hand, a charity running a profitable enterprise to fund its work – for example, a coffee shop – will need to remember that a percentage of the profits made by the coffee shop may need to be paid to HMRC unless an exemption applies (or unless the coffee shop is transferred to a **trading subsidiary** and pays all of its profits to the parent charity as a Gift Aid donation – although if the profits of the coffee shop were small, it could be more cost-effective to pay the corporation tax, rather than incur the costs of running a subsidiary; see page 202 for more information).

Exemptions from corporation tax

The following list sets out the main exemptions and reliefs available to charities in relation to corporation tax. They are all subject to the condition that any profit is retained by the charity to support its charitable purposes and not paid out to other parties (but, as a charity is not allowed to distribute profits to its members or trustees, this condition should never really pose an issue). There are a number of areas where exemptions and reliefs are available to charities:

- *Primary-purpose trading*: Where profit (or **surplus**) arises from the income less expenses incurred in carrying out activities that clearly fall under your charity's purposes, this is classed as **primary-purpose trading** (see chapter 8) and there is no **liability** for corporation tax. This is vital for many service-providing charities; it means that the liability for corporation tax only arises in relation to **trading for fundraising purposes**.
- *Trading carried out mainly by the beneficiaries of the charity*: As noted in chapter 8, where your charity's beneficiaries provide a service or sell goods to raise money, it is classed as trading for fundraising purpose rather than primary purpose trading, but any profits are treated favourably. As the bulk of the work is carried out by the beneficiaries your charity exists to support, there is no corporation tax charge on any profits. Some of the work may be carried out by your charity's staff or volunteers who are not beneficiaries – as long as their involvement is minor, the exemption applies. However, if the

work is only partly (and not mainly) carried out by the beneficiaries, only that part is eligible for the exemption. Therefore, detailed records will need to be maintained.

- *Trading ancillary to your primary purpose*: This is trading which, although not expressly primary purpose in nature, is supplementary to carrying out your charitable purpose. Some examples are provision of a crèche at a college, accommodation for university students, and sale of food and drink to visitors at a theatre charity. All profits from **ancillary trading** are exempt from corporation tax. Note that where those sales – at the theatre, for example – are to the general public and not only the audience, this is classed as non-primary-purpose trading. If it can be proved these sales make up less than 10% of the total sales, they can be included within the ancillary trading exemption, otherwise they will be taxable.
- *Sales of donated goods*: Where charities sell donated goods, even when they are cleaned, sorted and given minor repairs, the profits are exempt from corporation tax. This is because the goods themselves are donations, which are gifted, not traded. The act of the charity selling them is considered to be the realisation of the value of a gift. This exemption applies to donated items sold as a regular activity through a **charity shop** or at a one-off jumble sale (for example).
- *Fundraising events*: Profits from **fundraising** events, provided that supporters know the event is for charity, are exempt from corporation tax so long as the event falls into either of the following categories:
  - small events such as coffee mornings, provided the total takings from such events across the whole charity are less than £1,000 per week;
  - events taking over £1,000 each provided the charity holds no more than 15 events of the same type per year in any one location (if a 16th event is held, all 16 events will be subject to corporation tax).

  Fundraising events meeting either of the above criteria would also be VAT exempt, meaning you would not need to charge VAT on any ticket sales – although you would not be able to reclaim the input VAT either (see page 174).
- *Small-scale trading and fundraising activities*: This useful relief means that, within certain limits, any kind of trading activity, even for fundraising purposes and even if it cannot be described as a fundraising event, is exempt from corporation tax. To comply with this exemption, the total turnover from all of these activities must not exceed the small-scale trading annual turnover limit (see below). (Note that the limit is based on the *turnover* – i.e. the total income from such trading – rather than the profit.)

There are two limits to consider. For all charities with a total annual income from all sources (grants and donations as well as fundraising) of under £32,000, the small-scale annual turnover limit is £8,000. Where a charity's annual income is above £32,000, the limit is up to 25% of that income to a maximum of £80,000. These limits are valid in 2023/24 and subject to change in later years. Examples of small-scale trading exemption limits are shown in figure 9.2.

EXAMPLES OF SMALL-SCALE TRADING EXEMPTION LIMITS

Charity's total income	Maximum trading income from fundraising where no corporation tax payable	
£ 5,000	**£ 5,000**	As up to £8,000 allowed anyway
£ 20,000	**£ 8,000**	As up to £8,000 allowed anyway
£ 32,000	**£ 8,000**	As up to £8,000 allowed and 25% limit
£ 50,000	**£ 12,500**	25% limit
£ 200,000	**£ 50,000**	25% limit
£ 320,000	**£ 80,000**	25% limit
£ 400,000	**£ 80,000**	£80,000 upper limit

Fig. 9.2 Examples of how small-scale trading limits apply at the time of writing

Note that where the turnover from non-charitable trading exceeds the relevant small-scale limit, the whole profit for that activity will be subject to corporation tax. If that applies, it is usually worth the charity establishing a separate subsidiary company to handle non-charitable trading (see page 202). However, some of the other exemptions listed above may also apply.

There is a possibility that HMRC will be lenient where turnover from non-charitable trading exceeds the small-scale limit but where you can demonstrate that, when the events were planned at the start of the year, there was an expectation that the total income of the charity would be higher than it turned out to be, and therefore the limits would not have been breached. For such an appeal to be successful, you will require clear evidence (such as minutes of meetings, approval of **budgets** and prior year results) that the drop in your charity's total income was exceptional.

Registration for corporation tax, returns and payments

Your charity may automatically be registered for corporation tax. This can happen for **charitable companies**, **CIOs** and **SCIOs**. As your charity will be entered into Companies House's records (even CIOs and SCIOs have an entry at Companies House recording their name), this can sometimes automatically trigger the sending out of a tax return for you to complete. Your return will state your charity's ten-digit Unique Taxpayer Reference (UTR) number, which must be used on any corporation tax returns or correspondence.

If you know your charity will be subject to corporation tax for a specific year, you must complete a return and not simply wait until HMRC asks you to. HMRC may have no knowledge that you are making taxable profits, but if you do not pay taxes due on time, you will be liable for substantial non-filing fees and interest on any overdue payments. Therefore, you may need to register with HMRC for corporation tax and you may need the services of an accountant to assist with corporation tax filings.

On the other hand, if you know you do not have any income subject to corporation tax, and HMRC has not requested a tax return, you are not required to complete one. But if you do receive a return, such as one that has been triggered automatically (HMRC sometimes requests returns), it must be completed even if no tax is payable; where the return shows there are no taxable profits, HMRC may not request another for a number of years. Corporation tax returns are due annually based on your financial year end. The return is due 12 months after your charity's year end, although the payment of corporation tax is due 9 months and 1 day after the year end.

VAT

VAT is a sales tax applied to goods and services that are traded. A charity that is charging a fee for services or selling items to raise funds (see chapter 8) is likely to be trading and would therefore need to register for VAT (unless it only has exempt sales, as outlined in the next section). Businesses or charities that are VAT registered must charge VAT on the goods and services they sell but can also reclaim VAT on purchases they have made to generate those sales – for example, goods they have bought to resell or invoices from suppliers of activities at an event, and even VAT charged on utility bills.

There is a misconception that charities do not have to pay VAT on purchases at all, but in fact the rules surrounding VAT mean that often charities end up paying more VAT than other VAT-registered organisations.

This section provides an introduction to the main aspects of VAT for charities. For more detail, see *The Complete Charity VAT Handbook*, also published by DSC (details can be found on page 313).

VAT rates

There are five main categories of VAT that you should be aware of – these apply both to goods and services that you sell, and to goods and services that you buy. Note that the terminology used for VAT is 'supplies' – any goods or services that an organisation sells are called 'supplies'. Supplies can be:

- *Standard rate*: This is used for most supplies unless any of the remaining four categories below apply. The standard rate is currently 20%.
- *Reduced rate*: A few supplies may be subject to a lower rate of VAT (5%). A common one for charities is the supply of energy to charitable non-business premises.
- *Zero-rated*: This means that a supply of goods or services is subject to VAT, but the rate is 0% (this is an important distinction from exempt supplies – see the next item). Some examples of zero-rated supplies are books and publications, children's clothing, most cold food and the sale of donated items (such as clothing sold through charity shops). Even though the customer is charged 0% VAT, the charity can reclaim VAT on purchases relating to this supply.
- *VAT exempt*: Some sales do not have to include VAT, and these do not count towards the **trading income** threshold for VAT registration (see the next section). The VAT exemption covers a wide range of charity services, including those that are educational and health related. Fundraising events exempt from corporation tax are also classed as VAT exempt (see page 170). The drawback with VAT-exempt sales is that the VAT on the purchases used to generate the sales income cannot be reclaimed.
- *Outside the scope of VAT*: This is non-business income and includes grants, donations and **investment income**.

This is a very general summary of the categories. There is a comprehensive list of zero-rated and VAT-exempt items on the HMRC website (see www.gov.uk/guidance/rates-of-vat-on-different-goods-and-services#charities). If it is not easy to identify which VAT category is relevant to the goods or services you provide, it may be better to ask an adviser rather than make a potentially costly mistake.

As the treasurer or finance officer, you need to consider the VAT position of your charity and assess whether you must become VAT registered (based on an assessment of the goods and services you sell in relation to the five categories above) or whether it would be beneficial to voluntarily apply for VAT registration. The following sections will help you to understand what VAT registration would mean for your sales and purchases, and (for all charities) what VAT reliefs you might be able to benefit from.

VAT registration

Thresholds

Only charities that are considered to be trading can become VAT registered, and only where that trading income is over £85,000 in a 12-month rolling period is it compulsory to be VAT registered (£85,000 is the threshold for the 2023/24 tax year and the threshold is reviewed annually; the current threshold can be found at www.gov.uk/vat-charities/registration). If your trading income exceeds this threshold, your trustees are responsible for ensuring that your charity applies to register for VAT.

To make this assessment, consider your charity's total income. For registration purposes, you should look at your last 12 months' total income levels. This is gross income, before taking off any expenses, and is on a rolling 12-month basis. In other words, this does not mean your annual financial year but the last 12 months to the current month.

If your charity's total income is less than the current VAT threshold, registration is not compulsory (although see the following subsection, on voluntary registration). If you conclude that you do not need to register, there is no action to take. You do not need to charge VAT on anything you sell, or submit returns to HMRC, but remember you will have to pay the VAT on suppliers' invoices and include VAT when determining how much something costs. For accounting purposes, you do not need to separate out the VAT element of any purchase – it can be included in the relevant expense account as a cost to your charity.

If your charity's total income is more than the current VAT threshold, you need to consider the breakdown of your income, and in particular the value of your trading income. This means looking at all of your charity's income streams and determining whether they are from donations or trading. In particular, you must be very clear whether a funding agreement is a grant or contract (see chapter 8). All trading income – both primary-purpose trading and trading for fundraising purposes – counts towards the threshold.

If the total of your trading income is below the current threshold, you will still not have to register for VAT. If the total is fairly close to the threshold for the past 12 months, you should monitor the position on a monthly basis to check whether the threshold is exceeded in any 12-month period.

If the element of your income assessed as trading income is over £85,000 and is not exempt (see page 175), the trustees must register the charity with HMRC for VAT purposes. Consider the following examples.

Examples of when VAT registration is necessary

Charity A has a total income of £80,000 a year. This is below the VAT threshold, so the trustees do not need to consider the value of their trading income; however the income is made up, the charity does not have to register for VAT.

Charity B has a total income of £140,000 a year, but £90,000 of this is from grants and donations. The remaining £50,000 is below the VAT threshold; therefore, the charity does not have to register for VAT.

Charity C has a total income of £140,000 a year, but only £20,000 of this is from grants and donations. The remaining £120,000 is assessed as trading income – £100,000 from a contract to provide services and £20,000 from the sale of publications. All this trading income exceeds the threshold and is liable for VAT (see page 175), and therefore the charity must be registered for VAT.

Charity D also has a total income of £140,000 a year, of which £120,000 has been assessed as trading income – a contract to supply health-related services. However, these services have been judged as an exempt supply. In this instance, all the trading income exceeds the VAT threshold, but, because the service is exempt from VAT, the charity does not have to register for VAT (in fact, it is likely it would not be eligible to do so).

There is a very tight timescale of one month to register for VAT once you have exceeded the threshold. You should therefore monitor your charity's income regularly, especially where the amount of trading income is significant and not from an exempt source. If you do happen to find that the threshold was exceeded some time ago, but your charity never registered, you must make a retrospective registration and give the actual date from which your charity should have been registered. This may be several years in the past, which can lead to complex issues such as reinvoicing work to include the VAT or absorbing the VAT element into your charity's finances, which could cause serious cash flow issues.

As an illustration, if for the previous two years your charity had £100,000 of income each year from providing administrative support to third parties but had not registered for VAT, this £200,000 would be treated as a VAT-inclusive amount. This means the £200,000 would be deemed to include the sales price plus the 20% VAT that should have been charged. That gives sales of £166,667 and £33,333 VAT. Therefore, your charity would need to pay £33,333 to HMRC (less any VAT reclaimed on purchases). Retrospective VAT returns would need to be submitted, which would mean extracting a significant amount of information from your charity's books, and your charity would be liable for VAT penalties unless the trustees could persuade HMRC they had a reasonable excuse for not realising the position at the time.

This is complex work and a specialist adviser is probably needed, which could come at a significant cost. However, an expert in VAT with experience of dealing with HMRC will be able to help you navigate what can be a very lengthy and complex process to achieve the best possible outcome. For example, if when you make a retrospective registration it is possible to reinvoice work (more likely to a local authority **funder** rather than to individuals) and reclaim a substantial amount of VAT on your past expenditure, it may be well worthwhile taking on that specialist help.

Voluntary registration

You may decide, or be advised, that you should register for VAT voluntarily, even when your annual trading income is less than £85,000. The main reason to do this is so you can reclaim VAT on your purchases, but often the advice is misguided, coming from someone with business experience who does not fully understand the complex partial exemption rules that apply to charities (see page 183). It may seem appealing being able to reclaim VAT on purchases, especially where this is a significant cost to your charity. However, if most of your charity's income comes from grants or VAT-exempt trading income, the actual amount of VAT that can be reclaimed will be minimal, and the work involved in making those monthly or quarterly VAT claims can be quite substantial. It is only likely to be beneficial to take on voluntary registration where most of your trading income comes from zero-rated sales (see page 175) – for example, if your charity derives a significant portion of its income from charity shops selling donated goods.

If you are advised to apply for voluntary registration, you should estimate the amount of VAT that you would be able to reclaim, as well as what your VAT status might mean for your customers or beneficiaries, before committing your charity to registration.

How to register

It is relatively straightforward to register a charity with HMRC for VAT purposes and involves an online application. If you have registered as a charity with HMRC (see page 302), you can use your Government Gateway ID to log in at www.gov.uk/register-for-vat. If registering for VAT is your first contact with HMRC, you can follow the same link but as one of the first steps you will be required to set up a Government Gateway ID. There is an online form to complete, asking for information about your charity with questions on your turnover (trading income), the nature of your trading and the date when you became liable for VAT (or decided to register voluntarily). Once your application has been approved, you will receive confirmation from HMRC with your charity's VAT registration number. This must be included on all of your charity's invoices.

Records and reporting

Once you are registered for VAT purposes, you will need to keep records of all VAT **transactions** in your books. This involves recording the net and VAT amounts of transactions separately and being able to extract the relevant data for VAT returns. This has to be a fully automatic process under Making Tax Digital (MTD) (a government initiative seeking to improve tax reporting for all organisations), which takes information from your accounting system and sends it directly to HMRC. Most accounting software packages offer this facility. It is possible to use a third-party bridging software from spreadsheet-based accounts to HMRC, but this can be very complex and requires you to keep detailed, accurate spreadsheets.

VAT returns have to be submitted quarterly or monthly and require an analysis of the VAT you have charged and reclaimed as well as your total net sales and purchases. Monthly returns tend to be favoured by organisations which regularly have large amounts of VAT to reclaim as it can help to improve their cash flow. If your organisation tends to pay more VAT than you reclaim, quarterly returns may be more suitable. The VAT return submission and payment deadline is normally one month and seven days after the relevant month end. For example, a quarterly return and payment due for the quarter ended 30 June would need to be submitted and paid by 7 August. Similarly, if you are using monthly returns, the relevant figures for October would need to be submitted by 7 December. If you do not meet the return deadline, a penalty may be due.

If the return results in a payment of VAT (i.e. the VAT you have charged on sales is more than you are recovering on purchases), you will need to ensure you have the funds available to pay by the due date, which means you may need to monitor your charity's cash flow position carefully. If you are due a repayment of VAT (i.e. the VAT you are reclaiming on purchases is more than you have charged on sales), HMRC will generally reimburse your charity, but may hold the amount and set it off against a future payment if it is small.

Impact of VAT on sales

VAT charged on sales is known as 'output VAT'. A major implication of being VAT registered – especially so where it is on a voluntary basis – is that you must charge output VAT on any sales that you make. That means that anything that your charity carries out for trading purposes (such as contracts with local authorities, ticket sales for fundraising events or sales of non-donated goods) will need to include an element for VAT in the total price charged.

If you are VAT registered, you will need to establish which of the rates (zero-rated, reduced or standard – see page 175) apply to any sale of goods or services you make. You must then add the corresponding VAT rate percentage and amount of VAT to all your sales invoices. You may need to apply different rates to different products or services. Accounting software that also has an invoicing function can be helpful in making sure all required information is completed correctly on the invoice.

As mentioned in chapter 8, funding can be received under a contract rather than a grant. Under a contract for services, you will normally need to invoice the funder on a periodic basis. There is scope in these arrangements both to charge VAT in error and, on the other hand, not to account for it when it is due. Where it is unclear whether you need to charge VAT, you should consider whether the funder is receiving a direct benefit or service in return for the funding. If the funder does gain a benefit, is the service liable for VAT or does it qualify for VAT exemption? If it is determined that VAT should apply, you may need to check with the funder that the contract allows VAT to be added or whether the funding agreed already includes the VAT element.

Adding VAT to fees is not usually a problem if the service is being paid for by a local authority. But if the service is being paid for directly by service users, bear in mind that it will be much more costly for your beneficiaries unless your charity has sufficient resources to absorb the VAT element of the price. Consider the following example.

Example of the effect of adding VAT to fees

Charity Z provides a service under contract with a public sector body for £100,000. The service is a standard-rated supply. This means that if the charity wanted to keep the £100,000 income to fund its service, it would need to charge the local authority an additional 20% – totalling £120,000 – with the £20,000 being passed on to HMRC, net of any VAT on purchases related to the supply. A local authority would generally be able to reclaim this VAT and would probably therefore have few concerns with this, but some other public bodies, especially in the health field, are VAT-exempt organisations. In that case, if the funder was only willing to pay £100,000 in total, the contract might need to be negotiated to a point where £100,000 represented the gross amount – invoicing £83,333 with 20% VAT of £16,667, giving a total of £100,000 for the funder to pay, but the charity only receiving £83,333 for the service. Whether the charity could absorb this difference or needs to reduce its service or cut costs to manage on the lower income level is a matter for financial planning, as discussed in chapter 6.

A funder that can reclaim its own VAT on purchases would probably not mind paying this additional VAT. However, if your services were invoiced directly to individuals who had no ability to reclaim VAT, you would have to ensure the VAT-inclusive price was not cost-prohibitive to them in any way. For example, imagine that Charity X wants to charge a fee of £50 for a service to its beneficiaries, who are individuals. The service is subject to standard rate VAT. With VAT added, the price becomes £60. If Charity X absorbs the VAT, so that individuals only pay £50, the price it invoices must be £41.67 (£41.67 plus 20% VAT is £50). Although the amount on one fee is small, when this is multiplied over a period of time, the implications can be significant. If a beneficiary pays for a weekly service at £50 per week plus VAT at £10, they will be paying an additional £520 in VAT per year. If the charity absorbs that VAT, it will receive £433 less in income to deliver the service for that individual over the same period. Charity X will need to weigh up the effect of the costs on individuals against the charity's ability to deliver the service.

It is also worth noting that if you are VAT registered and sell services to a local authority under a contract, then you can reclaim VAT on all purchases related to that contract. However, if the same service is provided under grant funding, you will not be trading, and, as grant income is outside the scope of VAT, no VAT on related purchases can be recovered (known as 'irrecoverable VAT').

Impact of VAT on purchases

VAT on purchases is known as 'input VAT'. You can reclaim this if your charity is VAT registered, but only to the extent where a purchase is deemed as relating to an activity where VAT is charged. It is very unlikely that you will be able to reclaim all your input VAT because usually charities receive some of their income through donations rather than trading. Even if you trade, you might only trade in VAT-exempt goods or services. It is impossible to reclaim VAT on purchases if your charity is not carrying out any trading or if the only trading is VAT exempt.

As noted previously, if you are not VAT registered, when you make a purchase, you will always include any VAT paid in the total cost of the purchase. And in your **accounting records**, there is no need to record the VAT amount separately (see page 176).

Not being able to reclaim VAT can be a big issue for charities that buy services from businesses that charge VAT. Often businesses will quote prices 'exclusive of VAT', as that tends to be the price other businesses need to be aware of. However, a charity that cannot reclaim VAT will need to consider the true cost to the charity, which could be 20% higher than that quoted. For example, a cleaning company might quote a price of £200 per month to a charity, but the actual cost the charity needed to pay, including VAT, would be £240.

This should also be considered when applying for a grant to purchase equipment. For example, you may be quoted a price of £10,000 excluding VAT for some play equipment for your charity. But you will need funding of £12,000 to cover this – the extra £2,000 being the 20% VAT you must pay the supplier, which the supplier then passes on to the government through its VAT returns. It is easy to see how, across the sector, charities pay significant amounts of money to the government in this way.

If your charity is not VAT registered, as the treasurer or finance officer, you cannot simply say to a supplier that they should not charge you VAT as you are a charity – this is not true, although some well-meaning trustees think it is! However, it is worth knowing that there are a few VAT concessions available to charities that may help:

- *Rental of space*: In some cases landlords have the option to charge 20% VAT on rent of a building. However, if a charity is renting that space to carry out its charitable purposes, it can ask the landlord to override that option. An example would be a commercial rent on a charity shop.
- *Advertising costs*: Normally, advertising with a newspaper or online is subject to a 20% VAT charge; however, if the advertisement is placed by a charity, the publisher should charge VAT at 0%.
- *Fuel and power*: Supplies of gas and electricity for non-business purposes, and therefore charitable activities, are subject to a reduced rate of VAT of 5%. (Note, however, that if a charitable building is used substantially for 'business' – i.e. for trading activities – this concession may be lost and VAT at 20% may be payable on gas and electricity supplies.)
- *Goods for people with disabilities*: Some specialist equipment bought by charities for the relief of disability (such as specialist chairs, beds, lifts and wheelchairs) can be supplied free of VAT (zero-rated). The charity concerned will have to provide an exemption certificate or letter to

confirm it fits the criteria, and the retailer is responsible for checking whether the goods are eligible to be sold without VAT.

If your charity is involved with major building work, the VAT rules can be complex, and you should obtain professional VAT advice at an early stage in the work as to whether the building will comply with the criteria for **non-business use**. For the construction of an entirely new building for fully charitable purposes, the building work can be provided with zero-rated VAT. However, if your charity carries out activities in the building funded by fees, care needs to be taken. This can be classed as business use, and once the level exceeds 5% (i.e. if more than 5% of your charity's work is funded by fees or contracts), the concession will be lost and the building work will be charged standard-rated VAT at 20%. Communal residential buildings, such as hospices and residential care homes, do not have to have VAT charged. However, extensions, alterations and renovations to existing buildings will always be charged standard-rated VAT.

There are some schemes available to specific charities. For example, there is a VAT refund scheme for charities carrying out palliative care activities (such as hospices). The scheme enables them to reclaim VAT even though all of their income may be exempt. Search and rescue charities, such as those involved with air ambulances, mountain rescue and medical courier services, are also able to reclaim VAT on all non-business expenditure.

Partial exemption

For most charities that are VAT registered, there will usually be some of their income which is outside the scope of VAT – such as grants and donations. As these are not liable for VAT, the charity cannot claim all VAT back on purchases. This means they are partially exempt.

The accounting required for partial exemption VAT calculations is outside the scope of this book as it is complex and will be unique to each charity, but the general idea is that charities can recover only a portion of their VAT on purchases. If your charity is partially exempt, you will need to analyse your costs very carefully. VAT can be reclaimed on any of your charity's purchases that are directly used for the goods or services that you sell subject to VAT – even if they are charged zero-rated VAT, such as donated goods sold through a charity shop. For any purchases that are directly related to activities funded from an exempt or outside-the-scope source of income (such as a grant – see page 175), no VAT can be reclaimed. And for overheads or other costs that are used for both supplies that are liable to VAT and those that are not, you can make a reasonable apportionment and recover some of the VAT charged.

As you can imagine, these will not be easy calculations to make, and they cannot be made directly from accounting packages. Your auditor or examiner may be able to provide some support, but you will generally need the expertise of an accountant to ensure you are claiming an appropriate amount.

VAT implications of working with another party

Funders often encourage charities to work with other charities and **third sector** organisations to deliver a project. However, this can cause complications with the VAT positions of the parties concerned, so it is vital that as the treasurer or finance officer you are aware of any implications.

Partnership working

Two or more charities can make a bid to a funder to work on a partnership basis to deliver a project. However, usually the funder will require one of the charities to be the **accountable body** – to take the lead responsibility and hold the funding for the whole project, bringing in other charities as needed. Often the lead charity will talk about 'sub-contracting' the work to another charity. This arrangement will potentially give rise to significant VAT implications, as set out in the three scenarios in the following example.

Example of charity partnership working

Charity A receives £150,000 of funding from its local authority to deliver a project and works with Charity B to carry out a third of the work (amounting to £50,000). For the purposes of this example, we will assume that any work invoiced will attract the standard rate of VAT (20%).

Scenario 1: Charity A and Charity B are both VAT registered. If the work is *contract* funded, this is a simple arrangement. Charity B will invoice its work to Charity A at £50,000 plus VAT. Charity A will invoice the funder for £150,000 plus VAT and reclaim the VAT charged by Charity B on its normal VAT return. Both charities will receive the original amount of funding and all VAT will be recovered.

Scenario 2: Charity A and Charity B are both VAT registered. If the work is *grant* funded, this is a more complex arrangement. If Charity A sub-contracts Charity B to carry out its portion of the work, Charity B will need to invoice Charity A £50,000 plus VAT (£10,000). However, as the main work is funded as a grant, Charity A cannot charge VAT to the funder, nor claim back the input VAT on any work relating to it. This means Charity A will only have £90,000 left to complete its work (£150,000 less £50,000 to Charity B and the £10,000 irrecoverable VAT).

In a scenario where the original funding is in the form of a grant, it therefore follows that, regardless of the VAT position of the charities, it would be better for the lead charity to also offer a grant to another partner to carry out the work. If this approach is used, care must be taken to ensure the agreement between the partners does not use words such as 'sub-contracting'. A drawback is that, without a contract, Charity A has much less influence over the work of Charity B if things go wrong – it can ask Charity B to hold the funding as restricted, but, if the grant has conditions on what Charity B must deliver, HMRC could still treat the agreement as a contract for VAT purposes. It is therefore usually necessary to omit such conditions and rely on trust between the parties.

Scenario 3: Charity A is VAT registered but Charity B is not, and the work is *contract* funded. Charity B will invoice £50,000 for the work, but no VAT has to be charged. Charity A will still be able to invoice the funder for the full £150,000 plus VAT. However, Charity B will not be able to reclaim any input VAT on the purchases required for the project. This might be a problem if Charity A had not considered that Charity B was not VAT registered when costing the project and applying for the funding. If, for example, the VAT-eligible purchases for the project that Charity B needed to make amounted to £15,000, they would cost Charity B £18,000. But Charity A has only considered the £15,000 in the budget – resulting in £3,000 of irrecoverable VAT for Charity B and leaving a remaining £32,000 instead of the £35,000 that Charity A budgeted Charity B would need for the rest of the work. This sort of arrangement can be damaging to the finances of small charities.

Charity A could agree for Charity B to invoice the extra amount to Charity A (i.e. £53,000 instead of the intended £50,000). This would help Charity B, but, as no VAT is charged, Charity A could not reclaim the additional £3,000 VAT either, leaving £97,000 for its portion of the work. Either way, the £3,000 is lost as irrecoverable VAT. A possible solution could be that Charity B applies for voluntary VAT registration, but, as discussed above, this has its own complications (see page 178), especially if it is only a one-off situation. Or, potentially, the contract could be drafted in such a way that Charity A makes all purchases of project materials. In situations where significant irrecoverable VAT could arise, it is important this is considered in all budgets and funding applications.

Where such VAT problems arise, it may be possible to have equal partners and no sub-contractor type agreement if the funder is willing to adopt this approach. But unless there were separate agreements (an agreement between Charity A and the funder, and another one between Charity B and the funder), the two charities would still be deemed to be working in partnership and be jointly and severally liable for each other's work – meaning one could be sued if the other failed to deliver. Again, this would need trust between the two partners. If the charities were going to work on future projects together, they could consider a charity merger, but this would take careful consideration and probably benefit from professional advice.

Shared services

Sometimes, charities will work together to create efficiencies. For example, a small charity may not be able to afford its own in-house human resources, finance or IT support, but might be able to do so together with other charities. However, if one charity charged another for these types of service, unless it was very small, the services would be subject to VAT and VAT registration would be needed. This could be a problem for other charities (that are not VAT registered) purchasing the services due to the irrecoverable VAT.

There is a special set-up called a cost-sharing group (CSG), which attracts VAT exemption for cost-sharing arrangements when an entity supplies such services to charity. The exemption applies when two or more charities with exempt (or non-business) activities establish a separate organisation as a CSG to provide themselves with services (such as a finance or IT function). The charities become members of the CSG. The CSG does not need to charge VAT to its members, although there are conditions to be met. This type of arrangement was set up under EU law and could be subject to change due to the UK leaving the EU. The CSG is mentioned here as a possible approach to shared services, but you should seek professional advice as to how this could work for your charity.

Other taxes and business rates relief

Apart from corporation tax and VAT, the other main taxes in the UK are income tax, inheritance tax and capital gains tax. Generally speaking, charities will not be subject to these taxes as long as all of their income is used to further their charitable purposes.

For example, income tax is payable by individuals and corporation tax is payable by companies on **investment** returns, such as interest and dividends. A charity is not subject to those taxes, and can receive gross interest and dividends where those investments and income from them are used in furthering the charity's purposes.

In the same way, selling investments, or selling other **assets** such as property, is not subject to capital gains tax where it is for charitable purposes. And, likewise, although the estate of a deceased person will be subject to inheritance tax, any legacies left to a charity are exempt, which is an incentive for an individual to leave a legacy to a charity. There is no inheritance tax impact on a charity, but it can be worth pointing out to supporters that a given sum left as a bequest to a charity can do more than a similar bequest to a non-charitable organisation or to a relative because there is no inheritance tax charged on bequests to charities.

Business rates relief

Charities are not exempt from paying business rates on properties they occupy, but there is a relief of 80% of the charge if you can demonstrate that your charity is using the space wholly or mainly in a way that is in line with its charitable purposes. Local authorities may have different takes on this measure, with some expecting more than half to be charitable use and others wanting more.

A problem can arise where the premises are for mixed use. For example, a charity shop that sells donated goods will generally get business rates relief even if it sells a small amount of new goods. However, a charity shop that sells only new goods will not receive the rates relief. If a charity rents out office space in its building to non-charity tenants to generate income, the rates relief may be declined.

You will need to apply for the rates relief and often have to pay in full first and then receive a repayment. In some cases, a local authority may be able to offer discretionary relief, which tops the relief up to 100%.

At the time of writing, these reliefs apply in England and Wales, Scotland and Northern Ireland; however, they are subject to change and, in the case of discretionary relief, they are dependent on the local authority, so it is always worth checking what applies where you are based. Note that in Scotland charitable independent schools no longer receive business rates relief from 2022, and some politicians have suggested making similar changes in England and Wales. However, the definition of an independent school is quite precise: most educational charities are still eligible for rates relief.

This chapter has highlighted the complexities in the taxes that your charity may face. It may be that, as the treasurer or finance officer, you will never have to deal with VAT or corporation tax, but you should be aware of when that situation could change. Trustees should always take professional advice when it is in the best interests of their charity.

10 Gift Aid

Gift Aid is the government scheme whereby **charities** can claim an extra 25p for every £1 gifted to them by eligible **donors** (at the current basic rate of income tax). The scheme allows donors to increase the power of their **donations**, giving more to causes they care about. For charities, claiming the Gift Aid tax refund from **HMRC** can boost funding for their cause considerably.

You are not allowed to make Gift Aid tax claims on every donation to your charity, but it will generally be a worthwhile exercise to register for Gift Aid and carry out the necessary work needed to claim any additional funding your charity is due. This chapter sets out which donations are eligible as Gift Aid, including some special circumstances to be aware of. It looks at how to register to reclaim tax paid on a Gift Aid donation, and the administration and record-keeping surrounding the Gift Aid regime. It also examines the Gift Aid Small Donations Scheme (GASDS) and concludes with a discussion of the Gift Aid rules for subsidiary trading companies.

Gift Aid eligibility

Many charities receive much of their income through Gift Aid donations. The benefit of using the Gift Aid scheme is that the donations are topped up by a further 25% from government support (note that, strictly speaking, the term 'Gift Aid' refers to the whole donation and not just the top-up amount). Any organisation recognised as a charity for tax purposes (see page 11) or recognised by HMRC as a community amateur sports club (CASC) can sign up to the Gift Aid scheme.

The principle underpinning the Gift Aid scheme is that a gift from a UK taxpayer is deemed to have been made out of gross income. A charity can reclaim the portion of the income tax that the donor has paid on the income that the gift was made from. Regardless of the donor's personal tax rate, the gift is treated as being made net of basic-rate income tax, currently set at 20%. To work out how much tax to reclaim, you have to **gross up** the gift to find out what the donation would have been before tax was paid.

To gross up for 20% tax, you divide the donation amount by 80% (i.e. 0.8), or alternatively add 25% to the net donation received, as in the following examples.

Gift Aid calculation examples

If someone earns £125 and pays 20% tax, the tax paid is £25 (20% × £125) and they are left with £100.

If the person gives your charity this £100, you can find the gross amount of income by taking the £100 and dividing it by 80% – this gives £125. Therefore, your charity can claim back £125 less the £100 donation already received, so a total of £25. This is the same as 25% of the donation received.

If you are registered to reclaim tax paid on Gift Aid donations, it is worth ensuring you claim on the smaller as well as the larger donations. For example, a one-off gift of £500 would attract a Gift Aid tax refund of an additional £125. However, if you had 20 donors gifting £10 per month, that could lead to an additional £600 of tax being claimable each year.

It is likely that administration of your charity's Gift Aid scheme will fall to you as the **treasurer** or **finance officer**, perhaps with some input from any fundraisers. If you do have a specific fundraiser or **fundraising** team in your charity, it is helpful if they can publicise the Gift Aid scheme among your donors. However, they should be mindful of the conditions that apply to prevent any unauthorised tax being claimed.

Rules for donations

There are strict conditions on the donations that are eligible as Gift Aid:

1. The recipient of the donation must be a charity in UK tax law (including **exempt** or **excepted charities**) or a CASC.
2. The gift must have been received after the organisation was recognised as a charity by HMRC (though it is worth noting that the recognition can often be backdated and you are able to claim for a donation within four years of the end of the financial period you received it).
3. The donation must be a genuine gift – it cannot be a payment for goods or services, or where the donor receives anything but a trivial benefit in return (see point 9).
4. For tax to be reclaimed, the donation must be from an individual – it cannot be from a company (though see page 202, which has information on Corporate Gift Aid).

5 The donor must be a UK taxpayer (paying income or capital gains tax) making a donation out of their post-tax income. The donor must pay enough tax to cover what is being reclaimed by the charity. (Note that although income tax is devolved in Wales and Scotland, a Welsh or Scottish taxpayer is counted as a UK taxpayer for this purpose.)

6 The donor must make a declaration that they wish the donation to be treated as Gift Aid (see figure 10.1 on page 197 for an example declaration).

7 Payment must actually be made and evidence (i.e. a full trail of the money received) of this must be available.

8 The charity must keep accurate records of all donations where tax has been reclaimed on Gift Aid donations and of the completed declarations from donors to confirm their eligibility as UK taxpayers (see point 6). The charity must submit these to HMRC on request.

9 If the donor gets any benefit from their contribution, Gift Aid only applies where the benefit received by the donor (or any **connected person**; see page 25) is less than the permitted benefit level. This means a donation cannot qualify as Gift Aid if the value of the benefit received in return for the donation exceeds the following limits:

- For donations of up to £100, the maximum permitted benefit value is up to 25% of the donation.
- For donations of over £100, the maximum permitted benefit value is £25 plus 5% of the value over £100 up to a maximum total benefit of £2,500. For example, for a donation of £700, the benefit value would be £55 – i.e. £25 plus 5% of £700 less £100).

10 The value of the benefit received by the donor is based on that generally available to a member of the public, or, where such a price is not available, that of a similar item, or the cost to the charity. As an example, if someone donated £20 to a charity and received a charity-branded T-shirt in return that cost the charity £10, their donation could not qualify for Gift Aid, as the value of the benefit (the T-shirt) would exceed 25% of the donation. If, however, they had donated £100, the donation would be eligible as Gift Aid as the benefit would be less than 25% of the donation value.

Special circumstances

The rules above provide the general framework for what is eligible as a Gift Aid donation. It is also worth noting some donations where Gift Aid never applies.

If a person donates to your charity through a payroll giving scheme with their employer, these donations are made from the person's gross income, before tax is paid. Therefore, if your charity receives donations through payroll giving schemes, you cannot claim tax back on them via Gift Aid, as they are not from income which has been subject to income tax.

In many cases, it is clear that the donation meets the Gift Aid rules (for example, if it is from an individual who pays tax and nothing is received in return for the Gift Aid donation) as long as there is a Gift Aid declaration. However, there are some circumstances that are not so clear cut. HMRC provides guidance on some common areas covered below.

Donations from sponsored challenges

Where sponsors of a participant carrying out a challenge event could make a valid Gift Aid declaration (i.e. they are UK taxpayers), then a Gift Aid tax claim can be made on their sponsorship donations. All sponsorship payments are eligible for Gift Aid if the participant pays full participation costs (so receives no benefit). And even if the participant does not pay, the sponsorship is allowed if all sponsors are not connected to the participant (see page 25).

This rule is based on the principle that if the participant is receiving something for the sponsorship (such as travel for an event), then that is not a pure donation. An example would be an overseas challenge event, such as a mountain climb, which costs £2,000 for flights, accommodation and support costs which the charity pays. If the participant only raised £3,000, the benefit they received would exceed the permitted benefit limits, so Gift Aid would not apply. If the charity asked participants to raise £4,000 – half to cover the costs and half as a donation for the charity – then Gift Aid could apply to the donation part as the participant would not have received any benefit.

For smaller-scale events, such as sponsored walks around a local area where there is no cost to enter, as long as the sponsors could make a Gift Aid declaration, then all the sponsorship can be subject to Gift Aid.

Although as a charity you are not expected to verify each and every sponsor's Gift Aid status, you must take reasonable steps to ensure eligibility is set out in the event literature and that evidence is collected in some way – such as by requiring agreement with the eligibility criteria.

Charity membership fees

Gift Aid claims can be made where a charity membership **fee** is for membership only and does not give members use of the charity's services or facilities. However, the membership fee can allow members to take part in activities that form part of your charity's objectives, to view the work of your charity or to receive a newsletter setting out the work of your charity.

Viewing charity property

A person might make a payment to look around a garden that is set up as a charity. In principle, an entry fee is not a gift, as the customer is buying the opportunity to view the garden and so is receiving something in return. However, if you do not charge a fee and simply ask for a voluntary donation, or even add a voluntary donation to the ticket price, then the donation is eligible as Gift Aid. But visitors must have the choice to pay, otherwise it is not a voluntary donation, and the option must be clearly stated at the time of purchase.

There is also a rule saying that even if you charge for admission, the whole amount is eligible as Gift Aid if it leads to admission for at least 12 months (i.e. an annual season ticket). Moreover, even one-off admissions can be eligible as Gift Aid if the person pays at least 10% more than the normal entry fee. For example, if an art gallery normally charges £10 admission, those who are willing to pay £11 or more can declare Gift Aid on the full amount. However, this only applies to museums, galleries, gardens, historic properties and so on – i.e. where the admission just allows people to view something that is already in place. It does not extend to tickets for performances. In all cases Gift Aid declarations are needed from the individual donors.

Charity events

Payments for charity events, such as admission to a jumble sale or a ticket to a fundraising ball, are not eligible as Gift Aid, as again there is something received in return for the ticket. Even where the ticket price is significantly higher than the cost of putting on the event, which is often the case for fundraising events, the payment is not eligible – it is classed as **trading for fundraising purposes** (see chapter 8). Any voluntary donations on top of the ticket price are eligible as Gift Aid subject to the usual declaration being in place. But be aware that if you ask for a minimum donation to attend, this is not eligible, as this is the same as setting a ticket price. If you do ask for a donation to attend the event but do not stipulate any amount, the entire amount can be eligible as Gift Aid; however, people then have the option of attending without making any donation at all. A recent concession, arising from the COVID-19 pandemic but now staying in place, is that where an event is cancelled and the supporter waives their right to a refund, the amount they paid is eligible as Gift Aid subject to a declaration.

Charity auctions

Charity auctions can be a very lucrative opportunity to raise funds and are often included as an additional fundraiser at events such as annual dinners or community fêtes. Proceeds from an auction lot are not in their entirety a donation; the successful bidder will receive something in return, so it is a purchase. However, if a bidder has intentionally paid more than an item's worth to support your charity, part or all of the amount paid may qualify as a donation for Gift Aid if it satisfies rule 9 on page 191.

Where an item is commercially available, the benefit value for Gift Aid purposes is the retail price. For example, say a rugby ball retails for £25. Whether the ball is purchased by your charity, gifted by the shop or given by someone else to be entered in the auction, the benefit value is £25. Therefore, a successful bid would need to be over £100 (£25 is 25% of £100) for the entire £100 to be eligible as Gift Aid under the permitted benefits rule.

If the successful bidder only offered £75, none of the amount would be eligible as Gift Aid, as the value of the ball would exceed the permitted benefit level. However, if, at the start of the auction, the charity told bidders that the ball could be bought locally for £25, the donor could 'buy the benefit'. If their successful bid was £75, it could be treated as the donor having bought the benefit of the purchase price, and thus the balance would be a donation – in this case, £50 (£75 bid less £25 benefit bought) would be a donation eligible as Gift Aid. The excess payment can only be treated as a donation if the item is capable of being purchased separately and the donor is aware of the benefit value (retail cost of the item) at the time they make their successful auction bid, so that they know the excess amount is a donation.

Where the item is not commercially available – for example, the ball is signed by local rugby players – there is no retail price that can be applied.

The benefit value for Gift Aid purposes is then what someone is prepared to pay. Therefore, if the ball sold in the auction for £250, the benefit value would be £250 and no Gift Aid would apply, as the donation would be equal to the benefit received.

Gifting of volunteer expenses

Charities are allowed to pay volunteers (including **trustees**) for reasonable expenses (see chapter 11), perhaps to cover travel so they can carry out a task for the charity. If a volunteer (a UK taxpayer) does not want to receive this repayment, they are able to donate it back to the charity, and it may be eligible as Gift Aid. As with charity events, since the COVID-19 pandemic, HMRC has agreed that a waived payment due from a charity is eligible as Gift Aid going forward. Provided there is clear documentation that the volunteer has submitted a claim for expenses, has clearly said something to the effect of 'I'm happy to donate this to Charity X' and has completed a Gift Aid declaration, the expenses are eligible as Gift Aid. You will need to take care in the accounts, though, to ensure both the volunteer costs and the donation are reflected, as HMRC requires a monetary payment to be recorded.

Retail Gift Aid

If your charity runs a **charity shop**, it could operate a Retail Gift Aid scheme. Any money made by selling items does not qualify as Gift Aid – the person paying for the item is receiving something in return. However, if you can explain to those donating goods that you are acting as an agent to sell goods on their behalf, the donor can agree that the sales proceeds the goods bring in, less any commission charged, can be gifted to your charity as a Gift Aid donation. This must be explained clearly to the donor of the goods through your charity communications, perhaps notices in your shops.

There are slightly different methods of operating the Retail Gift Aid scheme depending on the way the shops are run and structured, but the principles are the same. An individual takes goods to a charity shop. The shop informs the owner that they will act as an agent to sell those goods on the owner's behalf if the owner will give the sales proceeds (minus any commission) to the charity as a Gift Aid donation. The individual completes a Gift Aid declaration to this effect, or, if they are a regular donor, the shop may already have a declaration for them in place. The shop must then identify those goods in some way, either physically or using a recording system, as the sale proceeds need to be linked back to the donor.

Once the goods have been sold, the charity shop must write to the donor to advise them of the net sales proceeds. If the individual does not reply in 21 days to claim those sales proceeds, the shop is then allowed to treat the net sales proceeds as a Gift Aid donation to the charity. The rules allow you to write to the donor just once per year if the amounts involved are fairly small, or even once every three years in some cases.

Standard letters and detailed guidance can be found on HMRC's website.[12] As the treasurer or finance officer, you should ensure that all relevant shop staff receive comprehensive training and that record-keeping is robustly implemented for such claims. In particular, HMRC may want to see the Gift Aid declarations and **accounting records** that track the donated items from the individual donors through to the sales and eventual claims of Gift Aid (where eligible).

Gift Aid tax claims

Gift Aid declarations

If you are going to operate a Gift Aid scheme within your charity, you need to have a properly worded declaration from each individual making donations under the scheme. It must include the surname and one initial, and address (at least house number and postcode) of the donor. It needs to indicate that the donor agrees to tax being reclaimed on their Gift Aid donations and confirms that they have paid (or will pay) the same amount or more in UK income tax (or capital gains tax) in that tax year. The forms should have a description of the gifts to which they apply (e.g. 'all gifts I have made in the last four years and gifts I make in the future') as well as the name and address of your charity.

HMRC does have standard templates that can be used for one-off or ongoing donations on its website (www.gov.uk/claim-gift-aid/gift-aid-declarations), but you are free to tailor the forms to suit your purposes or collect the information in another way, such as digitally, as long as the above information is included. As mentioned, you will also need to ensure you can produce the forms if HMRC requests them. The HMRC template for one-off gifts is shown in figure 10.1.

Charity Gift Aid Declaration – single donation

Boost your donation by 25p of Gift Aid for every £1 you donate

Gift Aid is reclaimed by the charity from the tax you pay for the current tax year. Your address is needed to identify you as a current UK taxpayer.

In order to Gift Aid your donation you must tick the box below:

☐ I want to Gift Aid my donation of £______________ to:

Name of Charity ____

I am a UK taxpayer and understand that if I pay less Income Tax and/or Capital Gains Tax in the current tax year than the amount of Gift Aid claimed on all my donations it is my responsibility to pay any difference.

My Details

Title ____________________ First name or initial(s) ________________________________

Surname ____

Full Home address ____

____

____

Postcode _________________________ Date ___________________________________

Please notify the charity if you:

- want to cancel this declaration
- change your name or home address
- no longer pay sufficient tax on your income and/or capital gains

If you pay Income Tax at the higher or additional rate and want to receive the additional tax relief due to you, you must include all your Gift Aid donations on your Self-Assessment tax return or ask HM Revenue and Customs to adjust your tax code.

Fig. 10.1 HMRC's template Gift Aid declaration Source: www.gov.uk/claim-gift-aid/gift-aid-declarations.

Donors should be aware that it is their responsibility to declare that they pay enough tax in order for your charity to reclaim the tax paid on a Gift Aid donation. Although as a charity you will not be in a position to check this, you should do what you reasonably can to support this. For example, if you have a policy of holding Gift Aid declarations for a significant period of time for the purpose of claiming Gift Aid on ongoing donations, how do you know if the circumstances of the donor have changed? If someone changes employment or retires, they may not pay sufficient tax any more for tax on Gift Aid donations to be legitimately claimed. For this reason, it would be good practice to send renewal Gift Aid declarations to donors on a regular basis. If HMRC did carry out a Gift Aid audit and found a declaration to be inaccurate, your charity could be asked to repay the falsely claimed tax under Gift Aid.

As with all tax records, these forms need to be retained for six years following the year of donation. Online giving sites (see page 149) are able to act as intermediaries, holding the Gift Aid declarations of anyone donating to your charity through the giving platform. They will require your charity's Gift Aid registration details to act on your behalf to make the claims. There are other similar situations where your charity may be linked to a larger membership organisation – for example, for churches, the diocese or national headquarters may operate a Parish Giving Scheme, which acts as an agent and claims Gift Aid on the church's behalf.

How to register and make a tax claim under Gift Aid

If making a Gift Aid tax claim is going to be your first contact with HMRC, you will need to register with HMRC and get recognition as a charity. See page 302 for detailed instructions on how to do this.

Once you have logged into your HMRC online services account, click on the 'Claim tax back on donations' link. There will be a series of short questions to answer about what you are claiming for – for example, Gift Aid or the GASDS (see next section). There will also be questions about your charity and you will be asked to attach your Gift Aid schedule.

Your Gift Aid schedule is your record of all Gift Aid **transactions** in the period you are claiming for. HMRC does give an option to use third-party software, but it also has its own schedule which you can download and complete. The schedule is spreadsheet based and has accompanying guidance and examples of how to fill it in. You are able to download this schedule at any time (www.gov.uk/guidance/schedule-spreadsheet-to-claim-back-tax-on-gift-aid-donations), and you will need to complete it before you make a claim. Therefore, it is best practice to have an ongoing schedule to record the details of all your Gift Aid donations right from the first one. You will then be able to claim periodically.

The HMRC Gift Aid schedule includes fields for the following elements:

- At the top there are boxes for the date of the earliest donation amount on the claim and any over-claimed Gift Aid from previous claims (if applicable).
- Then, for each donation, you must list the name of the donor, their house number and postcode, the donation date and the amount donated.
- There are two columns – 'aggregated donations' and 'sponsored events' – that are not needed for regular donations from individuals:
  - The 'aggregated donations' column is where you can note that small one-off donations from various donors that have been added together (allowed for individual gifts of under £30 under GASDS – see page 201). In this row, you will not have donor details, only a description of the donations in the 'aggregated donations' column, the date collected and the total amount.
  - Where the donations have resulted from a sponsored event, you will need to enter the names of the participants (i.e. the individuals being sponsored), their house numbers and postcodes in the first few columns, and 'Yes' in the 'sponsored event' column. You then enter the total of all Gift Aid-eligible donations from each participant's sponsorship sheet and the donation date. Note that any individual giving £500 or more as sponsorship has to be entered separately as a donor in their own line in the schedule; this means it should be clear on the sponsorship form which sponsors have declared themselves as UK taxpayers and confirmed Gift Aid can be reclaimed. The sponsor sheets themselves are not sent to HMRC, but you must keep these as supporting documentation for your claim.

The schedule is in the OpenDocument Spreadsheet (.ods) format and must be saved as such. There are clear instructions on the spreadsheet concerning how many characters you can enter in each field and restrictions on what can be included. The sheet can be used for up to 1,000 lines of donations and automatically calculates the total amount on which Gift Aid is payable. Remember, the schedule should only include donations that you are confident are eligible as Gift Aid. The amount you will receive will be 25% of the total donation figure noted in the spreadsheet.

Once complete, the schedule must be uploaded to your online claim form and submitted to HMRC. When it has processed the claim, you will receive a letter confirming the amount of tax reclaimed under Gift Aid to be paid to your charity, and this will automatically be transferred to your charity's bank account. Although claims are often processed and paid quickly, HMRC still reserves the right to inspect your charity's records at a later date, and any tax reclaimed under Gift Aid fraudulently, or even in error, will need to be repaid.

It is worth noting that a Gift Aid tax claim can be submitted at any time, and for any number of donations. It is possible to submit a claim for a single donation or claim on a periodic basis, such as monthly, quarterly or annually. As the treasurer or finance officer, you will need to decide how often to claim based on your charity's cash flow and the time available to complete the work. For example, claiming on one large donation is relatively straightforward and will mean your charity benefits quickly from a further inflow of funds when the tax reclaimed under Gift Aid is received. On the other hand, a fundraising appeal may result in many small donations, and it may take time to gather all the data and complete the spreadsheet. However, having a process to record the information required methodically and claim regularly will be better for your charity – especially if you will also claim under the GASDS (see below).

Most small charities find it best to claim on a regular cycle (such as once a quarter, or maybe just once a year if the amounts are relatively small). However, it is best to link your Gift Aid tax claims to your financial year – otherwise, it is difficult to allocate the HMRC tax refunds to the correct years. If you have Gift Aid donations unclaimed at year end, the tax due will need to be shown in your year-end accounts as a **debtor** – see chapter 13 (for **R&P accounts**) or chapter 14 (for **accruals accounts**) as appropriate.

If your charity receives a large number of regular donations, recording them via the HMRC spreadsheet method may be too cumbersome. It may be more practical to use a third-party piece of software or database to help you keep track of donations. HMRC lists such software that is compatible with its systems (see www.gov.uk/government/publications/charities-online-commercial-software-suppliers/charities-online-commercial-software-suppliers). Also note that many of the popular giving platforms reclaim tax on Gift Aid donations on your behalf (see page 149) and as such those donations should not be added onto the Gift Aid schedules you submit to HMRC.

HMRC is fairly generous with its time limits for reclaiming tax under Gift Aid; you can claim for a donation within four years of the end of the financial period it was received. This is very helpful for charities which delay setting up their Gift Aid procedures. However, to take advantage of this, remember that you will need to have the necessary documentation in place for each donation you wish to claim for and be confident that each one is eligible. You will need to be certain it was a true donation (i.e.

check it meets the benefit restrictions outlined in point 9 on page 191), obtain a Gift Aid declaration and ensure the donor has confirmed they were a UK taxpayer in the tax year of the donation.

Gift Aid Small Donations Scheme

For many charities, it is not possible to get all donors to complete Gift Aid declarations even when their donations would be eligible. For a large donation, it would be well worth your charity doing everything it can to make the process easier for the donor and obtaining the declaration. But for some donations this is simply not practical. This is especially the case with cash donations into collection boxes and the increasingly common contactless card donations.

The government has a scheme in place to deal with this, called the Gift Aid Small Donations Scheme. It allows charities to reclaim 25% in tax on small donations, without the need for Gift Aid declarations and without requiring the donors to be identified or actually be a UK taxpayer. However, there are limits.

To be eligible under the GASDS, a donation must be in cash and deposited in your bank individually or as part of a larger banking, or made via contactless card. Each donation from an individual must be under £30. Any contactless card donation must have been made after 6 April 2019. Membership fees are not eligible for the GASDS, and the donor must have received nothing in return, except perhaps a sticker.

There is also a limit on how much you can reclaim under the GASDS: £2,000 in a tax year. This means a maximum of £8,000 in small donations per year is eligible under the GASDS.

However, this is further limited by the total of your actual claims made under the main Gift Aid scheme. HMRC states that donations under the GASDS cannot be more than ten times the amount of your Gift Aid claim. For example, if you claimed for £300 of Gift Aid donations, the small donations claimed through the GASDS would be limited to £3,000, giving rise to £750 in tax reclaimed on small donations (much less than the £2,000 maximum limit). Conversely, if you received £1,000 in Gift Aid donations through the main scheme, small donations of £10,000 would appear to be eligible. But this would exceed the maximum limit of £8,000, and therefore only £2,000 would actually be reclaimable under the GASDS.

In order to benefit from the GASDS, you must have made a full Gift Aid claim in the same tax year as a GASDS and must not have received a penalty for wrongly claiming Gift Aid in the previous two years.

In order to benefit fully, where you have (or expect to have) a significant amount of small donations (at least £8,000) in a particular tax year, it would make sense to ensure you reclaim tax on any Gift Aid donations through the main scheme regularly throughout the tax year, at least up to the value of £800. Then, towards the end of the tax year, if you had £8,000 or more donations qualifying for the GASDS, the full £2,000 would be reclaimable under that scheme. Bear in mind that claims for both the main scheme and the GASDS can be made retrospectively, so it is not necessary to submit the claims before the actual tax year end.

Note that if you do not have any donations eligible as Gift Aid, you cannot claim under the GASDS. There are also more rules, found on HMRC's website (see useful addresses, on page 319) – for example, if you operate community buildings. And, as for all Gift Aid, you do need to keep records, such as the total amount of cash donations collected, the date of the collection, when the money was paid into the bank, and receipts from the card machine for contactless card donations. Claims under the GASDS are entered into the Gift Aid schedule (see page 198) in one line using the 'aggregate donations' column.

Gift Aid and the GASDS do require your charity to keep accurate records of donations, which may be time-consuming and inevitably will fall to you in some way in your role as treasurer or finance officer. However, if you can ensure robust systems are in place to gather the information required, depending on the level of the donations your charity receives, the possibility of an additional 25% boost can be very welcome.

Corporate Gift Aid

Corporate Gift Aid works differently from Gift Aid by individuals. In this case, instead of a charity reclaiming tax on Gift Aid donations, a company which donates to a charity is entitled to tax relief on that donation. This encourages companies to donate to charities, often their own charitable foundations, as it reduces their corporation tax liability. However, this also means that wherever a company is wholly owned by a charity, it can use the Corporate Gift Aid scheme to make a donation to its parent charity and reduce its corporation tax liability to nil.

Some charities operate a **trading subsidiary** to carry out activities that make a profit to fund their wider activities (refer to chapter 8 for more on charity trading). This could be to protect the charity's resources from any **risks** raised by the trading activity, or because any profits made on the activity would be subject to corporation tax (see page 170). For these reasons, some trustees consider setting up a separate legal entity as a trading subsidiary to generate income for their charity.

The trading subsidiary must be owned and controlled by the charity. It is not a charity and is usually established as a registered company limited by shares, with all the shares held by the charity (rather than as a company limited by guarantee, as used for **non-profit** organisations). Trading subsidiaries are often thought of as social enterprises (see chapter 1) because they are designed to generate profits to feed back to the charity. Some charities like to use the **CIC** form to demonstrate that community purpose. Figure 10.2 shows this relationship pictorially.

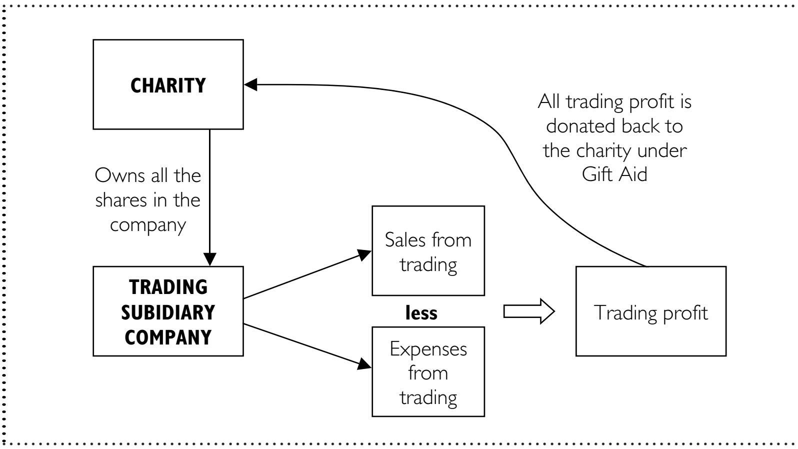

Fig. 10.2 A charity and its trading subsidiary

The important factor is that funds can be passed back to the charity. There are various ways to do this – for example, a dividend to the shareholder (the charity), interest and repayments of capital for any loans, rental agreements for premises, or charges for use of shared resources. The most tax-efficient way for a charity to receive funds, however, is where the trading subsidiary gifts any profits made to the charity under the Corporate Gift Aid scheme. This should be done before the subsidiary pays corporation tax, which then eliminates the tax charge completely.

With Corporate Gift Aid there is no tax paid or reclaimed (unlike in the process explained above for individual Gift Aid). The company just pays the gross amount of the donation to the charity, and the charity records it as a donation from a company.

However, there are some rules to follow in the trading subsidiary. The subsidiary must calculate how much it should donate to your charity to reduce its tax liability to nil, and the payment to your charity must be made within nine months of the end of the subsidiary company's year end. There must be a physical payment of money by the company to the charity, and this must be identifiable as such in the books and bank accounts of both entities. As already discussed, the charity and subsidiary company are separate entities and should have their own separate books and bank accounts anyway (see page 106), but the movement of money must be clear and not simply recorded as an 'intercompany account' transaction in the books.

Caution may be needed in terms of the cash flow of the subsidiary for the timing of the payment under Corporate Gift Aid as taxable profits and accounting profits are not equal. This is because some items are not deductible for tax purposes, such as **depreciation** (see page 81), but will be deducted from accounting profits. On the other hand, the company can claim capital allowances (currently at 100% of the cost) on fixed asset purchases up to £1 million. To eliminate any tax liability, therefore, the amount donated under Corporate Gift Aid may need to be different from the accounting profit generated from the subsidiary's trading activity. Such issues will need careful consideration and may need the advice of an accountant to ensure appropriate tax and financial planning have been considered.

Considerations in setting up a trading subsidiary

Although the trading subsidiary model provides tax-efficient giving, there are other considerations to take into account if you are considering setting one up. Any legal form of charity can have a subsidiary – for example, the parent charity could be a trust, **charitable company**, association, or **CIO** or **SCIO** (see page 11 for more information on charity types). The trading subsidiary should not provide services which meet the **charitable purposes** or **public benefit requirements** of the charity (see page 6) – those must be carried out by the charity itself. Therefore, the trustees need to be clear which activities are undertaken by your charity and which by the subsidiary. For example, if your charity is set up to offer counselling services to young people, they should be carried out through the charity. The trading subsidiary should not, therefore, sell counselling services to young people, but could offer other services or training (for a fee to raise funds) to those outside the scope of your charity's beneficiaries.

Note that if you personally look after the accounting records of the subsidiary, they must be kept completely separately from those of your charity, as it is a wholly distinct legal entity. This includes day-to-day accounting records, **management accounts** and **annual accounts**. As the subsidiary will be a company, its accounts will need to be submitted to Companies House and annual tax returns must be submitted to HMRC. This is all in addition to the requirements you will already be fulfilling for your charity.

If you are considering setting up a trading subsidiary, as with any decision taken at the board level, the trustees should discuss the advantages and disadvantages and document the reasons for any decision taken. Although they will be specific to each individual charity, some general advantages are that a trading subsidiary will:

- protect the charity's **assets** from any risks of trading;
- enable trading activity that is not possible for the charity under its purposes;
- reduce the tax liability of the charity.

On the other hand, some practical considerations to think about are:

- Where will the resources to set up the trading subsidiary come from?
- What legal structure should you use?
- Who will manage the subsidiary and how will that be carried out?
- If the trading subsidiary would occupy a significant part of the charity's premises, would this lead to any loss of rates relief (see page 186)? Typically, rates relief only applies to charities.

The trading subsidiary will need its own directors and a separate record of minutes of the board meetings. There may be different directors to the charity trustees, although it could be useful to have at least one director who is also a trustee and at least one director who is not a trustee. This is to ensure that, although the trading subsidiary should be operated in the best interests of the charity itself, proper arm's-length negotiations can take place between the trustees and directors when needed.

There should be clear guidelines in place that set out the nature of the relationship between the charity and the trading subsidiary and any shared resources (such as premises, staff and equipment). The charity cannot subsidise the costs of the subsidiary or any losses that it may make, as that would not be under the charity's purposes and, in any case, a charity should not be subsidising a commercial business. Equally, the charity cannot give charitable funds to the subsidiary to cover its start-up costs, so a bank loan may be needed initially. At the year end, depending on total income, the charity may need to prepare **group accounts** and consolidate the figures for the charity and subsidiary (see chapter 14).

As the treasurer or finance officer, it is important you at least have regular sight of the accounts of the subsidiary to assess its profitability or otherwise, and to make absolutely sure that all decisions, especially financial ones, are clearly being made in relation to either the charity or the subsidiary, and not confused between the two. If you are acting as treasurer or finance offer for the subsidiary as well as the charity, you will need two separate accounting systems unless your accounting software allows for multi-company accounting within one system. It is possible to have more than one trading subsidiary, but it is unlikely that this would be suitable for smaller charities due to the additional workload involved.

Unless you have specific knowledge, you should take professional advice before setting up a subsidiary trading entity. The **charity regulators** also provide guidance (see the further reading, on page 313).

This chapter has highlighted the main features of the Gift Aid schemes available to your charity. Being registered for Gift Aid and reminding donors to make a Gift Aid declaration, if they are eligible, can result in increased donations. For most charities, this will be a straightforward process. Where there are more complex situations, as treasurer or finance officer, it may be helpful for you to seek the advice of your **independent examiner** or **auditor**, or another expert.

11 Volunteers and employees

Charities need people to run them – to deliver on their **charitable purposes** and make a difference to their beneficiaries. Many smaller charities are operated entirely by volunteers, but, as a charity grows, there is often the need to take on staff. Managing and looking after the welfare of staff and volunteers is the responsibility of the **trustees**, even where a senior staff member has been appointed to manage this on their behalf. Sometimes charities will seek to appoint a trustee with experience of HR or employment law, but it is often left up to the **treasurer** to pay the volunteers' expenses and employees' wages, even though they may not have any experience of running a payroll.

The scope of this book does not include all issues related to working with and managing volunteers. Nor does it consider the complex employment and health and safety laws, which must be adhered to as soon as a charity recruits its first employee. This chapter looks at the financial implications of working with people, such as reimbursing volunteers, taking on freelance support and paying employees. It also considers some implications of being an employer, such as minimum wage legislation, running a payroll (including reporting to **HMRC** and paying employment taxes) and **auto-enrolment** obligations.

Working with volunteers

Individuals make a choice to volunteer. Someone may offer their time and skills voluntarily to support a cause they believe in or help make a difference to someone's life. The charitable sector relies on this support to carry out its work, and voluntary action is at the heart of being a charity. A charity can offer volunteering opportunities, set out clear expectations for each role, and even insist volunteers go through training and checks for beneficiary safeguarding reasons. But it cannot specify minimum hours or shift patterns or offer payment to volunteers for their services, as any of these would be an indicator of employment. Bear in mind that the trustees are also volunteers (except in the very rare cases where a trustee also has a paid role – see page 27). In some charities, the only volunteers are trustees, while others have a wide pool of volunteers in different roles.

In well-managed charities, there will be policies and agreements in place to cover volunteering. They will make it clear that there is a difference between volunteers and any paid staff. In particular, policies should make clear that volunteer roles and staff roles are not the same and that volunteers are not a replacement for paid staff. It is best to avoid using terms in volunteering agreements that could indicate employment – for example, consider setting out 'expectations', rather than 'requirements' that 'must' or 'have to' be met. You should also not require volunteers to book or apply for time off, and you must not pay fixed payments. (It is fine to have volunteer rotas if you need volunteers to be available at specific times, so long as the participants have genuinely volunteered to serve at the dates and times shown.)

Without clearly defined boundaries between the rights and expectations of staff and volunteers, you could face legal issues. For example, if a volunteer raised an unfair dismissal claim or asserted that they had a right to the minimum wage and holiday pay, this could pose a **risk** to both your charity's finances and its reputation.

A volunteer role description should set out the expectations of the role, the training and supervision that the volunteer can expect to receive, and any health and safety guidelines to be followed. It should also set out what expenses the volunteer can claim and equipment the charity will provide for them to fulfil their role. Volunteers can receive payments but only to reimburse out-of-pocket expenses incurred in carrying out their tasks. Examples of acceptable reimbursements include:

- travel expenses to reach their place of volunteering;
- reasonable food and drink costs;
- any equipment they are asked to purchase to carry out the role;
- any clothing they are asked to purchase for the role – perhaps protective clothing.

As the treasurer or **finance officer**, it is likely you will be involved in making or authorising these payments. It is helpful to have an expense claim form that sets out the requirements for eligible expenditure. For example, you could limit reimbursement of food and drink expenses to a set amount and only allow it if the volunteering was for longer than a certain time. All expenses paid to volunteers should be substantiated with a receipt or at least a clear explanation (for example, in the case of a claim for car mileage, details of the journey should be given). HMRC sets approved mileage rates that organisations can pay their employees and volunteers without the need for it to be classed a benefit and attract tax. At the time of writing these are 45p per mile for a car and 20p for cycling.

Organisations do not have an obligation to pay at these rates, though – they can pay less or not at all. However, you should look after your volunteers. Remember that a volunteer who does not want to claim their expenses can gift them back to your charity, and they will be eligible as Gift Aid if the volunteer is also a taxpayer (see page 195).

It is very important not to pay additional amounts above any expenses claimed, or anything that may constitute a payment for carrying out a role. This includes a flat-rate daily payment to cover out-of-pocket expenses, or vouchers or similar tokens. Further payments such as these could legally be considered to constitute a **contract** of employment, which would then mean the volunteer would be entitled to the National Living Wage (NLW) or National Minimum Wage (NMW) (see page 213).

Freelance staff

It is quite common for charities to pay consultants or freelance staff for work they carry out on behalf of the charity. And many smaller charities, when they realise tasks may be too onerous for volunteers, take on freelance workers to run some of their activities, a common one being **bookkeeping**.

There are many consultants who work in the charity sector and offer their specialist service to charities. For small and medium-sized charities, this is often the most effective way to obtain expert advice. For example, it would be cost-prohibitive for many charities to employ a full-time, or even part-time, fundraiser, yet they may benefit from the services of a specialist fundraiser for a particular project or to help draw up a **fundraising** strategy. The same can be said for HR, legal and accountancy support. Freelance support is not just linked to the administration and support functions in a charity; consultants or freelancers can be appointed to carry out charitable activities, for example a play specialist to run sessions in a children's charity or a music therapist to run sessions in a dementia charity.

Consultants (who may be self-employed or work for a company) and freelancers look after their own tax affairs, training and professional indemnity insurance, and they bring their own equipment to the role you have hired them for. They are not under your direct supervision when working. They will submit bids or quotes for work, and will invoice when the work is complete (do make sure they submit regular invoices and keep them with your records – do not make payments on the basis of some general agreement to pay a certain weekly or monthly fee). They do not get sick pay or holiday pay when not working, and they probably carry out similar tasks for other clients. Your charity should have a contract of engagement with them in place to set out what you require them to do – although this is often provided by the consultant or freelancer. As the treasurer or finance officer, your responsibilities will be ensuring the fees charged are at the agreed rate, checking with a fellow trustee or a staff member that the work has been carried out, and paying or approving the invoice.

However, you must make sure in any situation that the people your charity is engaging are genuinely freelance. There can be large fines and penalties if the actual arrangement you have with them is one of employment. For example, you may be required to pay taxes, employers' National Insurance, holiday pay and pensions if the relationship is deemed to be one of employee and employer. HMRC has a useful tool, 'Check Employment Status for Tax', which can be found at www.tax.service.gov.uk/check-employment-status-for-tax. This can help you to determine whether an arrangement you have with an individual should be classed as employment or self-employment. You can also ask the freelancer to confirm in writing that they will be declaring the income as self-employment and to provide their Unique Taxpayer Reference (UTR) number to prove that they are registered under the government's self-assessment tax scheme.

Employing staff

If your charity requires the ongoing support of paid staff, it will be best to become an employer. There are legal requirements around being an employer, and who the employer is deemed to be depends on the **constitution** of your charity. In a **charitable company** or a **CIO** or **SCIO**, the corporate body itself is the employer; however, in an **unincorporated charity**, the trustees are the employer (see page 8 for more on legal status). In any situation, however, the trustees have the responsibility of ensuring that employees are treated fairly and in line with applicable employment and health and safety legislation.

If your charity already has staff when you take on the role of treasurer or finance officer, it should already be registered as an employer with HMRC. It is likely that you will need to have some involvement in the employee function, and if you are a treasurer you may be named with HMRC as the responsible official concerning employment. In a larger charity, the treasurer may be limited to approving employee pay rates and authorising the monthly payroll for payment while the finance officer deals with the running of the payroll. In a smaller charity, the treasurer role may be much more hands on and responsible for running the payroll (where this is managed in-house). If your charity is new to being an employer, you may also be involved in registering as such with HMRC.

Note that this book does not cover some important employment issues such as recruiting staff, including the right to work in the UK and checks required for safeguarding issues. There is guidance on HMRC's and other employment websites (see www.gov.uk/check-job-applicant-right-to-work), and you should seek professional HR advice where necessary.

Registering as an employer with HMRC

As soon as your charity decides to take on its first member of staff and pay them more than £123 per week (current threshold in 2023/24), it needs to register as an employer with HMRC (note that once you are registered as an employer, all employees must be entered on the payroll regardless of how much they are paid). You can complete this process at www.gov.uk/register-employer by answering some questions and completing an online form. If your charity is already registered with HMRC and has a Government Gateway ID (see page 302), it will use this. If not, you can create an ID for your charity as part of the process.

You cannot register more than two months before you start paying people, but you must be registered before the first pay day. And HMRC states that it can take up to five working days to process an application. Once HMRC has accepted your charity as an employer, it will send out an employer PAYE reference number, which you will need to use in all correspondence and submissions to HMRC. As an example, if you were taking on an employee on 1 September and you wanted to pay them on 30 September, you would need to complete the online application process between 1 August and 23 September (allowing for weekends).

The tax year for employment purposes under PAYE is from 6 April to 5 April, but you are able to register as an employer and take people on at any time during the year. And it is not an issue where the tax year for employment purposes does not coincide with your charity's financial year. HMRC provides a lot of guidance on its own website relating to employment. It also offers employers the opportunity to sign up to a regular employment bulletin to keep abreast of changes in rates and thresholds (for example, relating to tax, National Insurance, the NMW and the NLW), reporting and other employment issues. HMRC also runs webinars for small employers where you can type in questions and have them answered (all of these services can be accessed through www.gov.uk/charities-and-tax).

Once your charity is registered as an employer, the trustees, probably guided by the treasurer or finance officer, need to select a payroll system to use internally, or perhaps enagage a payroll services company to run the payroll for them (see page 215). You should ensure your charity's HMRC online services account shows the 'PAYE for employers' section (if this isn't showing, follow the link 'Get online access to a tax, duty or scheme' to add it), as this will provide you with specific information, such as tax code notices (i.e. information on which tax code to use for an employee) and any balance on your employment taxes account. Once registered as an employer, your charity will also receive correspondence about its pension obligations under auto-enrolment from The Pensions Regulator (TPR) – see the following section.

Pension auto-enrolment

Under the Pensions Act 2008, every employer in the UK must put certain staff into a workplace pension scheme and contribute towards it, even if they only employ one person. This is known as automatic enrolment, or auto-enrolment. TPR (www.thepensionsregulator.gov.uk) offers guidance on the subject, and, as an employer, you will be required to complete its compliance checks – firstly on initial auto-enrolment and then at re-enrolment dates, currently every three years.

The key criteria to note are that anyone aged between 22 and state pension age earning over £10,000 per year (this equates to £833 per month or £192 per week and refers to gross earnings) must be enrolled in a workplace pension. The employee will pay at least a 5% contribution to the scheme (before tax on eligible earnings), and as an employer you must contribute a minimum of 3% to their pension pot. Employees can opt out of the scheme, although this must be voluntary and not engineered by the employer in any way. Additionally, employees who do not meet the criteria can opt in. However, some charities feel these minimum contributions for auto-enrolment are too low and thus offer more generous pension schemes.

For any employer, it is therefore necessary to identify an auto-enrolment pension provider. The government has set up its own scheme, NEST (National Employment Savings Trust), which employers can register with. There are several others that can be found through a simple online search, and you can compare fees and features. If your charity has a pension scheme in place that already meets the auto-enrolment conditions, it does not need to change scheme; your current pensions provider will be able to confirm this.

Using an auto-enrolment pension provider for your workplace pension means that your charity will not have any pension **liabilities** to consider other than the contributions due to the pension scheme provider each time an employee is paid. The payroll software you use will identify the payments needed on behalf of each employee, and the pension provider will inform you of what information they require to be submitted. In some cases, submissions can be made automatically by the payroll software, and in others you will need to submit a report or information through the pension provider's online portal. Different providers require pension information to be submitted in different ways, but all will have support and guidance available. The information will include details of employees, their gross pay and pension contributions, all usually submitted in a specific file format given to you by the pension provider. After you have submitted one or two reports, this is generally not a difficult or onerous task.

However, some charities have other workplace pension schemes in place – known as **defined benefit schemes**. In these cases, the pension fund commits to paying a certain proportion of an employee's salary as a pension for the rest of their life (often with commitments to **inflationary** increases). Depending on how the pension fund is performing, your charity could have significant liabilities to the pension fund over and above any regular contributions paid in. Anyone serving as the trustee of a charity with a defined benefit pension scheme, even if it relates only to past employees, should seek specialist guidance where needed.

Minimum wage and holiday entitlement

All employees must be paid at least the NMW or NLW. Failure to pay staff at these levels will result in significant fines. The rates change annually – generally on 6 April or 1 October – so it is important to keep up to date with the current rates to ensure you do not inadvertently fail to comply. The rates can be found at www.gov.uk/national-minimum-wage-rates.

For the 2023/24 tax year, the rates are as follows:

- the NLW is £10.42 per hour and applies to everyone over the age of 23;
- the NMW for those aged 21 or 22 is £10.18 per hour;
- the NMW for those aged 18 to 20 is £7.49 per hour;
- the NMW for those aged under 18 is £5.28 per hour;
- the NMW for apprentices is £5.28 per hour.

Your charity may have a pay rate linked to a role rather than an individual who takes on the role. If this is the case, the pay rate for the role will need to be at least the amount of the NLW to ensure it meets the requirements regardless of the age of the individual. The legislation behind what is and is not included in the minimum wage calculations is quite complex and can take into account such things as staff being required to pay for their own uniforms, required clothing, tools and equipment, unpaid breaks and required travel times. For example, an employee (who is 24 years old) is paid to work 30 hours a week at the NLW. They receive £312.60 per week (30 × £10.42). If the employer requires them to hire some tools to carry out the work at a cost of £20 per week, the employee only really receives £292.60 per week. For 30 hours, this equates to £9.75 per hour and is under the NLW; therefore, the employer is not complying with the legislation. The ACAS (Advisory, Conciliation and Arbitration Service) website is a good source of support where working arrangements are not straightforward (see www.acas.org.uk/advice).

As well as knowing the above statutory minimum rates of pay, you will need to know about the real living wage (RLW), which is increasingly popular. Although it is not compulsory, many employers are turning to the RLW as a benchmark to ensure their staff receive a fair rate of pay. Indeed, some **funders** now ask on their application forms whether charities pay at the RLW rates. The leading think tank in the UK is the Living Wage Foundation (www.livingwage.org.uk), which updates the RLW regularly based on living costs. In late 2022, it announced a UK-wide RLW of £10.90.

As the treasurer or finance officer, you will be involved in setting and reviewing pay rates, generally on an annual basis. You must ensure that staff are paid at least at the statutory rates noted above and it may be helpful to benchmark pay rates, where you compare your rates against what other similar charities, local small businesses and local authorities are paying. Being a charity does not mean you pay your staff at the lowest possible rate: you need to be able to attract good staff. However, the public does not take a favourable view of charity employees being paid at too high a rate, and charity executives' pay is often a hot topic in the press. Remember that in the vast majority of charities the staff are *not* beneficiaries – paying excessive staff salaries may reduce the funds available for the rest of your charity's work. You will need to carefully consider how to achieve the right balance and settle on pay scales that you can justify. All pay rates should be approved and minuted by the trustees.

Employees also have a legal entitlement to holidays, known as statutory leave entitlement or annual leave. Currently this is 5.6 weeks' paid holiday per year. This equates to 28 days and can include statutory bank holidays. For full-time staff, this is relatively simple to calculate. For part-time staff, it can be calculated pro rata. For example, someone working 2.5 days per week would receive 14 days of annual leave. You can choose to provide more holiday than the statutory minimum.

For sessional staff (i.e. those who do not work regular hours and are perhaps only employed for a few weeks of the year – for example, to run activities in the school holidays), there is the option of paying the holiday entitlement, as usually it would not be practical for those staff to take the time off. This can be paid alongside regular pay or as an additional amount on a periodic basis, perhaps quarterly or annually. However, it cannot be rolled up in the pay rate and should be identifiable on a payslip as holiday pay. But you should bear in mind that this is an extra cost of employment and should be budgeted for when you take on sessional staff. Employment law in this area is quite complex, and where overnight and shift patterns are worked it is advisable to seek professional advice.

HMRC has a useful online calculator to help you work out holiday pay (www.gov.uk/calculate-your-holiday-entitlement). This is especially useful to calculate holiday pay entitlement if someone leaves or joins part way through the year, and for those not on regular contracts of employment.

Running a payroll

Payrolls generally are run on either a weekly or a monthly basis. A charity can have more than one payroll if it manages different employees in different ways. However, for a small charity, where possible, one monthly payroll should be sufficient and more should be avoided due to the work involved in running a payroll. There are essentially six steps each month that are required to run a payroll:

1. Add any new employees, remove leavers and check whether there have been any updates to any employees' tax status. Once an employee is linked to your organisation, HMRC will automatically send you tax code changes and updates to student loan collections or other deductions (these are found in your HMRC online services account under 'PAYE for employers').
2. For staff who are paid hourly, record the hours worked on a timesheet to determine the amounts to be paid. For salaried staff, record any overtime; for both types of staff, record any other additional payments if applicable.
3. Enter the details of each employee's pay into the payroll system.
4. Confirm and run the payroll. This triggers the FPS (Full Payment Submission) and EPS (Employer Payment Submission) reports, which will be sent to HMRC automatically each time you run a payroll. When you run the payroll, you will also receive payroll reports (such as who has been paid, the amount of their gross pay and net pay, and

payroll deductions to be paid to HMRC and pensions providers), which you will need for management purposes. Where your payroll system is integrated with your accounting system, the payroll **journals** will automatically be created.

5 Send payslips to employees. Most payroll systems can send a payslip by email to each employee.

6 Make payments. Employees can be paid at the same time as or after the submissions to HMRC. If you operate only one payroll, it is best to make the payments to all employees on the same date; however, that does not necessarily have to be the case and there may be reasons why staff are paid at different times. Payments to HMRC and pension providers can be paid later (see the next section, on payroll deductions and payments).

The level of involvement you will have as treasurer or finance office will vary depending on how the payroll function is managed in your charity. You may do it all, or you may make certain approvals (such as on hours and rates to be paid) and give final authorisation of the payments to employees, while an outsourced payroll service carries out the majority of the work.

Payroll must be run using online software that is compatible with HMRC and that can send it real-time information (RTI) submissions. The options for RTI software for a small or medium-sized charity are:

- *HMRC's free software, Basic PAYE Tools*: Available at www.gov.uk/basic-paye-tools, this allows you to manage a payroll for up to nine employees. Once you have entered the employees' details, you are able to enter the gross pay for each payroll period for each employee. The software then generates the amounts that you need to pay each employee as well as taxes, National Insurance and deductions, and submits the details to HMRC. It also produces payslips. However, as Basic PAYE Tools does not produce combined reports by employee, you will probably need to take that data and record it in a separate spreadsheet, which you might call 'monthly payroll report', that combines all the information you will need (and provides the supporting documentation) to enter into your charity's books (see chapter 4)
- *Payroll functions in standard accounting packages*: Most of the common cloud-based accounting packages (see page 60) have a payroll function that can be purchased for either a monthly fee or a fee per employee. These are usually intuitive to use and, as well as calculating the amounts due and automatically reporting to HMRC, they produce payslips for employees and useful reports for your charity. They also

tend to input payroll journals directly into your charity's books. You may also find that the software can link directly to your pension provider, or, if not, generate a report that can be uploaded for auto-enrolment purposes.

- *Stand-alone payroll-specific software*: HMRC lists those that comply with its RTI requirements (see www.gov.uk/guidance/find-payroll-software-that-is-recognised-by-hmrc). How these work will depend on the software provider, but, as with the above options, they will offer a facility to enter all of your payroll information, send the required FPS and EPS reports to HMRC each time a payroll is run, and generate payslips for employees and reports to enable you to manage the payments and process the **transactions** into your charity's books.
- *Outsourced payroll services to manage payroll for you*: Local firms of accountants may offer a payroll service, and some larger organisations operate payroll services specifically for the **third sector**. You will still need to supply the outsourcing service with the amounts to be paid and may need to actually make the payments to employees, HMRC and pension providers – although many outsourcing services use **BACS** to carry out this function for the charity. This will be the most expensive option; however, if you are not comfortable with the responsibilities of running a payroll, it may be worth the cost.

Payroll deductions and payments

Whenever you pay an employee, it is likely there will be three main payments to make: a payment to the employee of their net salary, taxes and National Insurance to HMRC, and pension deductions to the workplace pension provider. There will be exceptions – for example, where an employee is paid below the threshold for auto-enrolment or has opted out, or where they are paid below the tax and National Insurance thresholds. And there may be other deductions, such as for student loan collections. This book cannot cover every eventuality, but the following list sets out the main elements of payroll payments you are likely to encounter:

- *Gross pay*: This is the amount that the individual has earned during the pay period. If they are salaried (i.e. receiving monthly pay), the amount will be one-twelfth of their annual salary. Payroll software will automatically calculate this when you enter annual salary information. For hourly paid staff, their gross pay will be the number of hours worked multiplied by the hourly rate. Gross pay for tax purposes will also include any bonuses or holiday pay.

- *Net pay*: This is the amount that the employee will receive. The payroll system calculates it by subtracting all of the deductions (where applicable). This is the amount you should pay the employee and is often referred to as 'take-home pay'.
- *PAYE*: Pay As You Earn is the process of deducting income tax and National Insurance. Income tax is automatically calculated by the payroll software and is based on the individual's tax code. This means that two people earning the same gross amount do not necessarily receive the same take-home pay. PAYE is paid by the employer directly to HMRC under the employer's PAYE reference. The deductions must be paid by the 22nd of the month following the date the employee was paid.
- *National Insurance*: All employees over the age of 16 and under state pension age have National Insurance applied to their earnings (although there are thresholds to be reached before it is due and different categories apply). There is an element paid by the employee (employee's National Insurance), which is deducted from their gross pay. There is also an element paid by the employer (employer's National Insurance), which is based on a percentage of the employee's gross pay (note that for employees under the age of 21, there is no employer's National Insurance liability). This is therefore an additional cost to be borne by the charity. Both elements of National Insurance are paid to HMRC along with the employee's income tax.
- *National Insurance Employment Allowance*: To help small employers, the government has a scheme in place where the first £5,000 (2023/24 rate) of employer's National Insurance (combined for all employees) is effectively waived and the employer does not need to pay it. You must ensure you claim this where eligible (see www.gov.uk/claim-employment-allowance/eligibility) on the payroll software. Generally this means ticking a box in the software each year, and then the software will automatically apply the allowance in determining the payments due to HMRC. Note that it is for the employer's element only; the employee will still incur their deduction.
- *Student loan*: Where an employee has a student loan, they are required to repay it under payroll if they earn above a certain threshold. HMRC will make the employer aware of the fact and the payroll system will calculate the amount automatically. It is deducted from the employee's gross pay and is paid to HMRC along with the PAYE and National Insurance.
- *Pensions*: An employee deduction is applied to eligible employees' gross pay based on the scheme in place (auto-enrolment or other), and an employer element is calculated based on the contribution rates in

place (see page 212). Both amounts are paid to the pension provider by the employer. The payment dates will depend on the pension provider and may be claimed automatically by direct debit.

These are common deductions and payments, but there will be other situations that could arise. HMRC's guidance is useful, and most payroll software providers also offer their own online guidance, training and helplines.

TUPE transfers

Although this book does not set out to cover employment legislation, as the treasurer or finance officer, it will be useful for you to have an awareness of TUPE regulations. TUPE is shorthand for the Transfers of Undertakings (Protection of Employment) Regulations 2006 and its amendments in 2014. Whenever an organisation, or part of it, transfers from one employer to another, or a service transfers to a new provider, TUPE regulations protect employees' rights.

This may happen when a charity restructures in some way. A common example of this is when an unincorporated charity restructures as a CIO or SCIO (*Charitable Incorporated Organisations*, also published in this series, contains detailed information on this process; see page 313 for further details). The CIO or SCIO is a completely new and separate legal entity from the existing charity and therefore becomes a new employer (and must register as such with HMRC – see page 212). Even though the activities and staff of the new CIO or SCIO may be exactly the same as under the original charity, any staff transferred to it must be protected under a TUPE transfer. Breach of these requirements could leave the charity open to claims of unfair dismissal.

The TUPE regulations apply to both the old and new employer and involve planning for the transfer, including informing and consulting all affected employees. On the date of the transfer, employees will automatically move over to the new employer along with their existing terms and conditions, such as levels of pay and holiday entitlement. An employee's length of service must also transfer, which means that if the new employer has to make an employee redundant, any statutory redundancy pay calculations will be from the date the employee was first employed by the old charity. The ACAS website (www.acas.org.uk/handling-a-tupe-transfer-step-by-step) provides a useful step-by-step guide, and it may be necessary to contact an employment law specialist if you need to carry out a TUPE transfer.

On a practical note, as the treasurer or finance officer, you will need to be aware that such a transfer will involve changes to your payroll system. For example, you will need to process everyone as leavers from the old charity, and indeed close down the payroll itself and cease employer status by notifying HMRC that your charity is no longer an employer, if the old charity no longer exists or employs anyone (HMRC provides guidance on its website about these actions: www.gov.uk/stop-employing-staff). On the other side, you will need to register as a new employer with HMRC (where necessary) and add the employees transferring into the new organisation into the new payroll system.

This chapter has set out the main considerations for a treasurer or finance officer when working with volunteers, freelancers and employees. Employment law is complex and although this chapter has provided an overview of payroll processes, there is much more to consider when employing staff. If HR is not an area you are familiar with, it may be necessary to consult the services of an HR professional.

12 Annual financial reporting

All **charities** are required to engage in some form of annual reporting. This normally consists of a narrative report from the **trustees** and a set of **annual accounts**. Good financial reporting is a means of promoting your charity and showing how its resources have been used in delivering its work, yet many charities see this as another compliance requirement to simply be ticked off the list. Sadly, this can be an opportunity missed; an engaging set of charity accounts can really sell a charity to **funders** and supporters.

This chapter looks at the legal requirements regarding annual reporting and the differences that exist depending on the size of the charity, its legal form and variations between the three UK **jurisdictions**. The requirements result in two different accounting methods for charity accounts: either an **R&P** approach or an **accruals**-based approach, considered in more detail in chapters 13 and 14, respectively. Whatever type of accounts you produce, a good **trustees' annual report** is essential; therefore, this chapter next looks at what is required and what it is best practice to include to satisfy the various users of your charity's accounts. Finally, the chapter considers various ways that you, as **treasurer** or **finance officer**, may undertake the annual reporting process, including making the annual return to your **charity regulator**.

Legal reporting requirements

A condition of charitable status is that your organisation must prepare a full set of annual accounts reporting on your income and expenditure for the year, and the balances at year end across all **funds** your charity holds. These accounts should be accompanied by a narrative report from the trustees which sets out certain information about your charity and its achievements in the year. This is called the trustees' annual report. The full document is often called the **annual report and accounts**.

In Scotland and Northern Ireland, any organisation with charitable status must submit its annual report and accounts to OSCR or CCNI, respectively. This is regardless of size or legal status. In England and Wales, the annual report and accounts must normally be sent to CCEW. However, if a charitable organisation has an annual income of less than £25,000, it should prepare the annual report and accounts, but it does not need to send them to CCEW (unless it is constituted as a **CIO**, where no lower limit applies). **Charitable companies** in all jurisdictions, regardless of income level, must also file their annual report and accounts with Companies House.

There are generous timescales for these filings. Under the relevant laws, OSCR and Companies House both require the reports and annual accounts to be submitted by nine months after the year end. This means a charity with a 31 March year end must submit its annual report and accounts before 31 December, or one with a 31 December year end must submit them before the following 30 September. In England and Wales and in Northern Ireland, the law extends this period to ten months for filing with CCEW and CCNI, respectively. All regulators show when accounts have been submitted on the registers they hold – and highlight when they are overdue. Potential funders and supporters can access these records, so a well-organised charity will usually ensure the documents are submitted to the relevant regulator in plenty of time. And often you will need to have your annual report and accounts ready much sooner to present them at your charity's annual general meeting (AGM) or to meet funders' requests. Note that OSCR calculates the nine-month deadline to the day – so if your charity had a year end of 30 June, the nine-month filing deadline would be 30 March the next year (not 31st).

It is important to note that not only must your annual report and accounts be sent to the regulators, and usually to funders as part of a **grant** application, but they must also be made available to anyone on request (as mentioned as a duty of trustees on page 21).

If you are the treasurer, you will normally be responsible for drafting your charity's accounts and organising for them to be externally scrutinised where required (if you are the finance officer, you will likely be heavily involved in this process, but the accounts and their external scrutiny are the responsibility of the trustees). In practice, many charities use their auditor or independent examiner to *help* with the preparation of the accounts (see page 235), but the trustees must remain in charge. The actual approval of the annual accounts, and the writing and approval of the narrative report, is the responsibility of *all* trustees. But, in general, it will be the treasurer or finance officer who drives the whole process.

The legal framework for charity accounting

As noted in previous chapters, the whole ethos of being a charity is based on the principle that funds donated are used to further **charitable purposes** for **public benefit**. The legal framework surrounding charity accounting has been developed based on the need to ensure that trustees demonstrate accountability for resources entrusted to them. Therefore, charity accounting requirements are much more extensive than those for commercial entities. Professional accountants who are not charity specialists may be unaware of the full implications. Therefore, it is crucial for the treasurer or finance officer to have a grasp of the current framework.

Chapter 1 noted that charity regulation is devolved in the UK, and therefore the legislation underpinning charity accounting differs depending on where the charity is based. Although the accounting principles across the different jurisdictions are virtually the same, the legislation referred to in the accounts is specific, and you should ensure your charity is using the correct legal framework. For example, a set of accounts for a charity only registered in Scotland should not refer to the legislation applicable only in England and Wales. The key legislation in each jurisdiction is shown in table 12.1.

In England and Wales, the Charities Act 2011 either directly details what a charity must do in terms of accounting or refers to the Charities (Accounts and Reports) Regulations 2008. The situation is similar in Northern Ireland, with some requirements falling within the 2008 Act itself and other issues covered in the regulations. As explained in chapter 1, not all Northern Irish charities are registered with CCNI yet (see page 12). For those that are, it is compulsory to follow the requirements set out in the Act and regulations; for those awaiting registration, the requirements are recommended as best practice. In Scotland, the 2005 Act points to the specifics of charity accounting as set out in the Charities Accounts (Scotland) Regulations 2006 (as amended). Regardless of where it is based, any UK charity constituted as a charitable company must also consider the requirements of the Companies Act 2006 as applicable legislation.

A common thread across all this legislation is that, in some cases, a charity must prepare its annual accounts using the Charities **SORP**. The SORP is a way of taking the technical UK **accounting standards** and making them applicable to the types of **transaction** and situations that charities can face (see chapter 14 for further details). However, the legislation allows many smaller charities to prepare **R&P accounts**, which do not have to follow the SORP (see chapter 13).

This overview of the legal and accounting framework highlights that in each jurisdiction the rules around charity accounting depend on primary legislation (Acts of Parliament), secondary legislation (regulations issued as statutory instruments) and other standards such as the SORP. As the treasurer or finance officer, you will find it useful to have a basic understanding of these principles, but this book does not cover the full details surrounding every eventuality. If you require further details, information on how to access the relevant legislation can be found in the further reading on page 313.

Table 12.1 The basis of the law on charity accounting

Jurisdiction	Legislation and guidance
England and Wales	Charities Act 2011 (as amended) (Part 8) Charities (Accounts and Reports) Regulations 2008 Charities SORP – see below CCEW's directions and guidance (in some areas these have the force of the law, especially the Directions to Independent Examiners 2021)
Scotland	Charities and Trustee Investment (Scotland) Act 2005 (as amended) Charities Accounts (Scotland) Regulations 2006 (as amended) Charities SORP – see below OSCR guidance (helpful advice but without the force of the law)
Northern Ireland	Charities Act (Northern Ireland) 2008 (as amended) Charities (Accounts and Reports) Regulations (Northern Ireland) 2015 Charities SORP – see below CCNI directions and guidance (in some areas these have the force of the law, especially the Directions to Independent Examiners 2019)
UK-wide	Charitable companies Companies Act 2006 (as amended) The Charities SORP (Statement of Recommended Practice on Accounting and Reporting by Charities) is currently in its second edition (2019). It is published by the regulators but with the approval of the Financial Reporting Council. The SORP, based on an accounting standard (FRS 102), applies to all charities throughout the UK. It is currently in the process of being updated and the new edition is due to be applied from 2025 – refer to chapter 14 for more details. See the further reading on page 313 for details of where to access the SORP and the directions and guidance mentioned above.

Which accounts to prepare: thresholds

Charity legislation, in terms of managing a charity and its accounts on a daily basis, applies equally to charities of all sizes. However, when it comes to annual accounts and reporting, there are thresholds in place designed to simplify the obligations for smaller charities. Table 12.2 sets out the income thresholds to enable you to decide which accounts your charity should prepare. For the purposes of assessing your charity's income, you should consider your charity's gross incoming resources for the year in respect of all **unrestricted** and **restricted funds**. As can be seen, these thresholds are relatively consistent across the jurisdictions.

Table 12.2 Income thresholds for the different types of accounting

Charity type	Annual income level	Accounts to prepare in all jurisdictions, unless specified
Trust, unincorporated charity, or CIO or SCIO	Less than £250,000	Choice: R&P accounts or accruals accounts following the Charities SORP (with some limited simplifications allowed*)
Charitable company	Less than £250,000	Accruals accounts following the charities SORP (with some limited simplifications allowed*)
All charities	£250,000–£500,000	Accruals accounts following the charities SORP (with some limited simplifications allowed*)
All charities	More than £500,000	Accruals accounts following the charities SORP in full

* Some concessions exist in the Charities SORP for charities with an annual income of under £500,000 (see chapter 14).

Any charity with dual registration – for example, where the charity is registered both in England and Wales and in Scotland – must follow the rules for the most strict regime, which tends to be Scotland.

Which accounts to prepare: choice

Table 12.2 shows that, for company charities of any size, and any charity with an annual income of more than £250,000, there is no choice – **accruals accounting** using the SORP is required. Chapter 14 sets out some of the main requirements under this accounting regime.

However, for smaller charities with an annual income of under £250,000, perhaps constituted as a trust, **unincorporated** association, or CIO or SCIO, there is a choice of accounting regimes to follow. You can use **accruals accounts**, but if you do so, you must follow the SORP. Or you can make use of a concession, designed to make things simpler for smaller charities, and use the cash-based accounting regime to prepare R&P accounts. Chapter 13 sets out the main requirements under this accounting regime.

In some cases, having that choice may make things more complicated for charity trustees – in particular for the treasurer or finance officer, who is usually the person left to consider the options. Note, however, that *all* trustees should approve the accounts format. Often, the treasurer may default to the **independent examiner** to decide which accounts to prepare. This is not a problem where the reason has been explained by the examiner and is understood and approved by the trustees. Bear in mind, though, that where the examiner is a professional accountant but without much charity accounting experience, their natural instinct may be to prepare accruals accounts as these are often seen as 'proper' accounts. However, it may be that R&P accounts are more suitable for your charity.

The following sets out some factors to consider when making the choice of whether to prepare R&P or accruals accounts.

R&P accounts are:

- often easier to prepare, as they are based only on the actual cash and bank transactions you receive and pay in the year (you must still keep a record of **debtors**, **creditors** and major **fixed assets** for a year end as a **statement of assets and liabilities** (or **SOAL**) – but this does not form part of your normal books);
- usually easier to understand, as they tend to be shorter, have fewer notes and be more user-friendly for people looking at your accounts;
- representative of the actual cash position of the charity and often align better to **budgets** in a smaller charity (thus highlighting whether there are cash-flow issues);
- cheaper for **independent examination**.

However, R&P accounts are often criticised for not showing a **true and fair view** or not being as professional as accruals accounts, especially as the quality of the accounts may vary between charities.

Accruals accounts are:

- seen as more comprehensive and consistent, as they show a true and fair view (as explained in chapter 14);
- better at showing how an **asset** is used in a charity over several years, by spreading the cost rather than indicating the full amount charged at the time of purchase (see page 81);
- much better at comparing the resources of a charity from year to year, as they are not affected by the timings of payments and receipts;
- commonly perceived as what funders require to allow more meaningful comparisons between charities.

However, accruals accounts can require complex calculations and **disclosures** to follow the provisions set out in the SORP. They also require many **notes to the accounts** that are not generally needed with R&P accounts. Consequently, they can be very long documents. Where they require a professional accountant to independently examine them (see chapter 15), the process tends to be more costly.

If your charity has a large amount of grant funding, particularly from government or local authority sources, you may be influenced to produce accruals accounts, and some funders require them as part of their funding agreement, as they are seen as more professional. In some cases, you may consider accruals accounts to align better with the activities your charity provides, and using them is perfectly acceptable as long as you follow the SORP. However, it should be noted that R&P accounts are allowed by law and are equally as professional when carried out to a good standard. You may choose to prepare accruals accounts if your charity's income level is just under the £250,000 threshold and it is predicted to increase in the future. But, conversely, a charity that has historically prepared accruals accounts may change to the R&P basis if its income has dropped under the threshold and is not likely to increase.

It is clear that where you have the choice between the two approaches, you will need to determine what is best for your charity's particular circumstances. There is no right or wrong decision – both options are equally valid. However, whichever approach is followed, it must be implemented fully. It is not acceptable to follow a hybrid approach – for example, by using R&P accounting but then including **depreciation** or a debtor in your figures (as these are accruals concepts). To help you make the decision and to appreciate what each approach may look like, refer to chapters 13 and 14 for more detail on what is involved in R&P and accruals accounts, respectively.

External scrutiny

Another decision that trustees need to make concerning the annual reporting process is what level of scrutiny is required for the accounts; as with the question of which type of accounts to prepare, this will generally fall to the treasurer or finance officer to investigate. For all charities registered in Scotland and Northern Ireland, there is a requirement for external scrutiny. In England and Wales, there is a concession from this requirement for the smallest charities. However, there are differences in the form this external scrutiny can take, as set out in table 12.3, which shows the minimum requirements for external scrutiny based on income levels and where assets are under £3.26 million. (Refer to the tables by jurisdiction set out in the 'Additional notes' section of the book for more details; see page 299.)

Table 12.3 Income thresholds for different levels of scrutiny of the accounts

	Income levels		
Minimum permitted scrutiny of accounts	*Registered or excepted charities in England and Wales*	*All registered charities in Scotland*	*All registered charities in Northern Ireland*
Approval of accounts by trustees only	£0–£25,000	Not permitted	Not permitted
Independent examination by examiner of charity's choice	£25,000–£250,000	Up to £250,000 and only for R&P accounts	£0–£250,000
Independent examination by professionally qualified accountant	£250,000 to £1 million	Up to £500,000 for all accruals accounts	£250,000–£500,000
Full audit by registered auditor	More than £1 million	£500,000 or more	More than £500,000

Note that where assets are over £3.26 million, a full **audit** is required when income reaches £250,000 in Scotland, and over £250,000 in England and Wales. Asset levels do not apply in Northern Ireland.

As table 12.3 shows, it is important to take care when appointing someone to carry out the external scrutiny of your charity, as the appropriate person depends on your charity's income and the type of accounts prepared (and where applicable if the charity's assets are valued over £3.26 million). Having said that, most small charities will be able to opt for an independent examination rather than a full audit. Although the majority of small charities will have assets under £3.26 million, those that own property may find themselves close to this limit. Chapter 15 considers the external scrutiny requirement in more detail, including who trustees can appoint and the general process that should be followed.

The trustees' annual report

In addition to the annual accounts, all charities must prepare the trustees' annual report (often abbreviated to TAR or called the 'annual report'). For **excepted charities** in England and Wales (see chapter 1), the trustees' report is not compulsory; however, it is best practice to prepare one, as it is very difficult to make sense of accounts which have no annual report alongside them. Although sometimes charities keep these as two separate documents, it makes more sense to combine them into one document – the annual report and accounts. This is because both documents, where required, must be submitted to the regulator, and if someone asks for a copy of your accounts, you must also provide your annual report, and vice versa. The external scrutiny report (where relevant) should also be combined with these documents – as well as providing some assurance on the accounts, it reports on consistency between the annual report and the accounts.

The annual report normally forms the first part of the combined document, as it includes the all-important details of your charity's purposes, **governing document** and trustee names (see page 234 if it would be an issue in your charity to publicise the trustees' names). Your annual report should link to your annual accounts, providing a narrative that explains the figures in the accounts for a more complete understanding. For example, the annual report might describe your charity's activities and point to the relevant note in the accounts where the costs of those activities can be seen. Or the annual report might explain the **fundraising** that your charity has carried out and refer to an income note in the accounts where the scale of those efforts can be appreciated in financial terms.

Although the treasurer or finance officer normally co-ordinates the preparation of the annual accounts, the annual report can be compiled by another trustee or staff member. As the treasurer or finance officer, you will still need to have some input into the report, especially those parts which include finances, **reserves** and funds. When preparing the report, you should have in mind both what must be included and who the users of the accounts are. If you incorporate a focus on the needs of the users unfamiliar with the charity, you will probably end up with a much more meaningful document.

Users of accounts

Charity accounts and reports are not simply a means to meet the legal requirements of being a charity. Although a commercial company may want to disclose the minimum possible in its accounts to avoid giving too much away to its competitors, the opposite is normally true for a charitable organisation. A charity will want to demonstrate what it has been able to achieve with the resources it has been given. Your annual report is a key means of communication with members of your charity, funders and supporters. And, in fact, it is likely that a potential funder will read your annual report and accounts in much greater detail than a regulator will.

Therefore, when you are thinking about who might want to see your accounts, the list could include the charity regulator (where your charity is registered), Companies House, **HMRC**, umbrella bodies, other similar or local charities, beneficiaries and members of the charity, staff and volunteers, funders, supporters, and members of the local community or even the wider public. These could be people who have a past, present or potential future link to your charity.

Some charities feel they want to produce full accounts for the regulators and a smaller summarised version for their supporters – but this results in extra work and can cause complications. Summarised accounts must clearly state that they are a summary and, if possible, include a statement by your **auditor** or independent examiner to state that they are not inconsistent with the full accounts. It could be argued that some people might be put off by the detail and accounting jargon in the detailed accounts and, conversely, feel more comfortable learning about your charity from a plain-language summary. However, it is also possible to make the full accounts more accessible.

You only have to look at the annual reports of some of the largest UK charities to appreciate the resources they invest in reporting. Many have dedicated staff teams working year round to gather data and present it in an attractive, informative and compelling way. A small charity does not have the resources to produce an annual report on the same scale as these large organisations, nor is it expected to do so. And sometimes too much information can be overwhelming and, indeed, some information may be more suited to another report, such as an impact report. But including photographs or other graphics, quotes and stories from members, and setting the report out clearly, will result in a much more engaging document.

Trustees do not have an entirely free rein over what to include in their annual report. There are some legal requirements for what must be included, which helps to bring a degree of standardisation across all charities, as set out in the following section. But these are *minimum* requirements – there is nothing to stop a charity giving more information that it feels will be useful to readers.

What to include in an annual report

The requirements for the annual report are set out in regulations which differ slightly between jurisdictions: in the Charities (Accounts and Reports) Regulations 2008 (for charities in England and Wales), in the Charities Accounts (Scotland) Regulations 2006 (as amended) or in the Charities (Accounts and Reports) Regulations (Northern Ireland) 2015. In each case, the regulations give full details of the annual reporting requirements for charities preparing R&P accounts. For those charities preparing accruals accounts, the regulations in England and Wales also provide requirements for the annual report, but in Scotland and Northern Ireland, the regulations refer to the SORP for annual reporting requirements using accruals accounts. Although it is not possible to cover the full requirements for annual reports in this book, the following five subsections set out the main points that all charities must cover regardless of size and legal form, unless otherwise stated.

The points are grouped together under the five main headings prescribed by the SORP (and even with R&P accounts it is simplest to follow this approach). The annual report must cover the same period as the annual accounts, and therefore you will generally be writing about things that began over a year ago. If there is something that you want to note in your report that is outside the year concerned, this must be made clear – for example, 'After the year end, the trustees received confirmation of a new grant to support the outreach project.'

Reference and administrative details

This section must include the following:

- official and any working names of the charity;
- **registered charity** number (if registered) and company number (if applicable);
- address of the principal office of the charity and registered address (if a charitable company);
- the names of the trustees at the date of approving the report;
- the names of all other trustees who served as a trustee during the financial year;
- the names of **holding trustees** (see page 8) at the date of approval and during the financial year.

There are some exemptions to the requirement to disclose the names of trustees and the address of the principal office where this could put anyone in personal danger (see page 234).

Objectives and activities

Three pieces of information must be included in this section:

- details of the purposes or purposes of the charity, usually the objects as set out in the governing document;
- a description of the main activities that the charity carries out to achieve its purposes;
- for charities in England and Wales and in Northern Ireland, an explanation of how these activities further the charity's purposes for public benefit and a statement to confirm that the trustees have had regard to CCEW's or CCNI's (as appropriate) guidance on public benefit.

Structure, governance and management

Here, you must cover the following:

- how your charity is constituted, including the particulars of your governing document and date of the last amendment;
- how trustees are appointed;
- if day-to-day tasks are delegated to a staff team or to individual trustees or volunteers, how that is managed.

Achievements and performance

This is the main narrative section, where the trustees are free to present the charity's achievements throughout the year. However, in all jurisdictions, there should be a focus on how your charity advanced its purposes for public benefit.

Often, it is best to focus on what has been achieved for the charity's beneficiaries – this should not simply be a list of fundraising achievements and thanks to various individuals. As such, the section should clearly identify who the beneficiaries are – not as individuals, but wider groups – quantifying where the data is available. For example, this could be the number of visitors to a heritage charity who learned about the building, or the number of young people supported by workshops. Even if you cannot give numbers, you need to explain how people will benefit – for example, a charity campaigning on climate issues will want to mention benefits to the whole population (current and future).

Financial review and reserves policy

For a small charity, a couple of sentences are generally sufficient to summarise the financial situation over the year. This often includes the total income or receipts, total expenditure or payments, and the net **surplus** or **deficit** for the year.

The section should include a note of the financial position, or the total funds the charity holds at the year end, together with how this is split between restricted and unrestricted funds. It should also outline the policy your charity has for holding its reserves, and an assessment of the actual reserves compared to the required reserves at the year end, as well as any action that that trustees may need to take. If the trustees do not believe they need to hold reserves, this must be stated together with the reasons behind the decision (see chapter 3).

Any financial uncertainties must be disclosed, along with the reasons behind them and the steps that the trustees are taking to address them. In particular, if any individual fund is in deficit, this must be explained.

Further requirements for larger charities

In each of the sections above, the SORP requires larger charities, defined as those with an annual income of over £500,000, to disclose much more information, including:

- strategies adopted to meet their short- and long-term aims and how the impact of those strategies will be measured;
- the processes used for training and inducting trustees;
- how volunteers contribute to the charity (if applicable);
- **investment** policy and a review of investment performance;
- grant-making policy (if applicable);

- **risks** the charity faces and strategies in place to mitigate those risks;
- plans for the future.

Trustees of smaller charities can also include information on these areas where applicable. They should especially do so where it will provide readers with a more thorough understanding of the charity.

Additional disclosures for charitable companies

Charitable companies must also comply with company law disclosures. Rather than make a second annual report covering those disclosures, it is acceptable to combine everything into one report. But the trustees, who are also the directors in company law, must make sure all relevant disclosures are included to satisfy both regimes.

In general, for a small charitable company, the disclosures required for a directors' report under company law are fairly minimal, and so this will usually be achieved via a trustees' annual report that meets the criteria set out above. However, the report should make clear that the trustees are also the directors of the company, and a statement of the trustees'/directors' responsibilities is usually added.

Making trustees' names public

In exceptional cases, a charity may wish to avoid one or more trustees' names being made public if it could put individuals at risk. For example, if a woman who was a survivor of domestic abuse became a trustee of a charity working in that field, she might be tracked down by a former perpetrator if her name were made public in the charity's annual report. Similar issues might apply in a charity undertaking work which was very unpopular in a particular locality, where threats of violence might be made against its trustees.

In circumstances of this kind, the charity can apply to the relevant regulator (CCEW, OSCR or CCNI) for permission to exclude such information from the annual report (if this is granted, the annual report should explain that the charity has formal authorisation not to show trustees' names). In England and Wales and in Northern Ireland, the request should also ask that the relevant trustees' names are not shown on the online register of charities (OSCR does not yet publish trustee names on the Scottish charity register – but this will change when the Charities (Regulations and Administration) (Scotland) Act 2023 is implemented). Such requests can apply to all trustees of the charity or just some.

If necessary, a request can also be made to omit the charity's address, but this makes it very hard for anyone to contact the charity. It is usually better to have a PO Box address.

If the request to omit trustees' names from the annual report is granted, CCEW authorises it under the Charities (Accounts and Reports) Regulations 2008, reg. 40(4); OSCR under the Charities Accounts (Scotland) Regulations 2006, sch. 2 para. 5 (which refers back to s. 3(4) of the Charities and Trustee Investment (Scotland) Act 2005); and CCNI under the Charities (Accounts and Reports) Regulations (Northern Ireland) 2015, reg. 32(4).

However, there is little point in making such a request for a charitable company, because the details of the directors/trustees will still be available from Companies House (there are very exceptional cases where names can be omitted even from the register of companies, but this is much more complex to achieve). It follows that it is usually better to structure a charity as a CIO or SCIO, or as an unincorporated body, rather than as a charitable company if you wish to be able to avoid disclosing trustees' names.

Annual accounting process

Preparing the annual accounts is the process of taking the information from your books and presenting it as a final document. Chapters 13 and 14 consider the differing forms that those accounts can take, but the process to be followed to arrive at the figures for the accounts is the same. Chapter 4 discussed **closing off** the books (see page 70). When that process is completed, you will have a set of final figures for the year. This is the starting point of the annual accounts.

Most sets of accounts will be created in an electronic document, usually a combination of word-processed and spreadsheet-based files. This makes it easier to amend drafts, and copy and circulate the accounts. In theory, however, there is no issue with a very small charity with no computer access preparing handwritten or typewritten documents.

Except in the case of very small charities in England and Wales (see table 12.3), the accounts will be subject to external scrutiny, and so it is usual to involve the independent examiner or auditor while the accounts are in a draft stage. This means that if you have not already appointed an auditor or examiner, you should do so as soon as possible after your year end. If you leave preparing your accounts until they are almost due for submission, you may find it difficult to locate someone who has availability to examine your accounts in time.

Chapter 15 considers external scrutiny, particularly independent examination; however, there are different ways of dividing up the overall work on the annual report and accounts between people within your charity (normally the treasurer and/or finance officer) and the person providing the external scrutiny (independent examiner or auditor):

- *Approach 1: Auditor or examiner is appointed only to report.* In this situation, the treasurer or finance officer will have produced the final accounts in their entirety. This means the accounts will be in the required form for the size of the charity, comply with applicable regulations, have been approved and signed by the trustees, and have an accompanying annual report. They are then submitted to the auditor or examiner for them to complete their work and include the necessary signed scrutiny report.
- *Approach 2: Auditor or examiner may request amendments and then reports.* As in the first approach, the treasurer or finance officer will have produced the full accounts, but they are in draft form. They have not been approved or signed by the trustees. The auditor or examiner carries out their work; however, where this results in any amendments being needed, the treasurer or finance officer makes these adjustments to the draft accounts. The accounts are then finalised, approved and signed, and the auditor or examiner adds their report.
- *Approach 3: Auditor or examiner completes accounts and then reports.* The treasurer or finance officer may not have the knowledge to prepare the full accounts but is able to produce some of the main reports and provide analysis from their accounting system or spreadsheets. The auditor or examiner uses this information, together with their scrutiny work, to pull together the full set of accounts (so the accounts are finalised externally to the charity). These are then returned to the treasurer or finance officer, along with any explanations, so that the trustees can understand and approve the accounts before the auditor or examiner signs their report.
- *Approach 4: Auditor or examiner produces accounts from the charity's underlying* ***financial records*** *and reports on them.* In charities with limited financial experience, it is often the case that the treasurer makes no attempt to draw up the annual accounts. However, they will have completed all the **bookkeeping**, closed off the books and reached some final figures. This could be in the form of a spreadsheet or reports from accounting software. From these records, the auditor or examiner prepares the accounts. These (externally prepared) accounts are given back to the treasurer, often with explanations or discussions. The trustees must consider and approve the accounts, and, once they

have been signed, the auditor or examiner can sign their scrutiny report.

For you as the treasurer or finance officer, it is probably best to aim for approach 2 or 3. You can use last year's accounts, which will help you to populate the figures. (However, this comes with the caution that simply following what was prepared in previous years has its risks, such as failing to update details in line with new legislation or comply with changing requirements, and missing the chance to stand back and think about whether you are presenting the figures in the most suitable way.) If you are involved in preparing the accounts, the knowledge you can bring about your charity's finances from your role will enable you to have a proper dialogue with the auditor or examiner about any tricky areas in the accounts. The only difference between approach 2 and 3 is who completes the final amendments to the accounts.

If you have good charity accounting knowledge, you may be tempted to go for approach 1. But, as a caution, bear in mind that if the auditor or examiner is unhappy with anything in the accounts and they have already been approved by the trustees, the auditor or examiner may need to issue a **qualified report** (see chapter 15). This is a formal report declaring issues with the accounts, and it could be damaging to your charity. It may be that the trustees fundamentally disagree with the examiner, which could be more of a concern. But if the qualification is for a small matter that both parties would be happier to see resolved, the accounts could be amended and reapproved. Therefore, it may have made more sense to provide draft accounts to the auditor or examiner rather than approved accounts.

Approach 4 is common in smaller charities (where there will usually only be a treasurer, not a finance officer, and where an auditor will not be required). The examiner must not be carrying out any work that constitutes maintaining the charity's **accounting records**; however, if they have been provided with the final figures, they can prepare the accounts from scratch. This should involve a significant amount of dialogue between the examiner and treasurer. The examiner should not be left to complete the accounts with no input from the trustees. For example, the treasurer must advise the examiner on any restricted funds that are not obvious from the accounting records. After all, it is the legal responsibility of the trustees to produce the accounts; they can take help, but they remain responsible for the content. Therefore, where an examiner has prepared the accounts, the trustees must understand how those accounts relate to the accounting records and reflect the decisions they have made as trustees throughout the year, before giving their approval.

Approval of the annual report and accounts

The annual report must be approved by all trustees – even though the draft will probably be the work of one or two people. This means that the content has been agreed as an accurate reflection of the charity's situation and performance over the year by all the trustees. Usually one or two of the trustees, often including the chair, will sign a statement along the following lines at the end of the report:

> This report was approved by the trustees on [date] and is signed on their behalf by [name].
>
> [Name, position]

It is usual for the trustees to approve the annual report at the same time as the accounts (see chapters 13 and 14). You should check your governing document to see whether there are any provisions about how and when this approval should take place. Often trustees think that the annual report and accounts must be approved by everyone present at the AGM. This is rarely the case: under charity law, approval is needed by the trustees at a meeting before the AGM. The approved accounts are then presented to the members and others at the AGM. (However, in a charity with no members beyond the trustees, the trustee meeting to approve the accounts may be combined with an AGM.)

Whether the accounts are approved before or at the AGM, approval of the annual report and accounts should be given by all trustees. This is normally at a meeting where the required number of trustees are present to be quorate and where open discussion can take place to ensure everyone understands the accounts, can ask questions and feel sufficiently informed to give their approval. If your accounts are subject to audit, it is likely your auditor will attend this meeting to present their findings to the trustees and answer any questions. Similarly, you can ask your independent examiner to attend the meeting where the trustees will discuss and approve the accounts.

During the restrictions encountered as a result of the COVID-19 pandemic, where in-person meetings were not possible, trustees were able to hold meetings virtually, including to approve the annual accounts and reports. This option has remained in place, but you should make sure virtual meetings are consistent with the provisions in your governing document. What is most important is that the accounts and report cannot simply be signed as approved by the chair and/or treasurer without the other trustees having any input into the process – that would be a serious breach of charity law.

Annual returns

The final stage in the annual reporting process, once you have completed your annual report, annual accounts and external scrutiny report, is to make the annual return to the appropriate regulator and file the accompanying reports and accounts. These are actually two different requirements but they are usually done at the same time, as the return depends on information in the accounts. Charities (non-CIOs) in England and Wales with an annual income of under £10,000 do not need to complete an annual return, although they must still complete an online update for CCEW, so the process is largely the same. All charities registered in Scotland or Northern Ireland (regardless of size) must submit an annual return and accounts to their regulator. Some trustees make this return as soon as the accounts are ready and approved, but others wait until after their AGM.

The process is essentially the same in all jurisdictions. You will require the login details to access your charity's account on the relevant regulator's website. Once you have logged in, the first step is to check that the main details for your charity are up to date to ensure what is provided on the public record is accurate. It is worth noting that although it is often the treasurer or finance officer who files the return and accounts with the regulator, it is not necessarily part of their role and could fall to another trustee, such as the chair or secretary.

The purpose of the annual return is to provide the regulator with a snapshot of your charity at the time in question, so you will be required to answer questions on the charity's income and spending. The amount of detail and number of questions will vary depending on the size and activity of the charity, but you may need to answer questions on areas such as fundraising, government grants and **contracts**, grant-making and employees. You will also be required to answer questions on transactions with trustees and whether there have been any **serious incidents** that have not yet been reported to the regulator.

Submission of annual report and accounts to a charity regulator

At the end of the annual return process, you will be given the opportunity to upload a PDF of your signed annual report, accounts and external scrutiny report. You should check that the document is complete and that none of the pages have been scanned the wrong way around. If electronic or typed signatures (see page 296) have been used, it is better to just save the original document as a PDF rather than print and scan it. The charity regulators perform some initial checks on the accounts, and so they may be rejected if one of the reports is missing. However, the regulator will not report back on the individual quality and completeness of a set of accounts as a matter of course. As previously noted, OSCR allows until nine months after the year end as the time limit for this submission. For CCEW and CCNI it is ten months.

Submission of annual report and accounts to Companies House

If you are a charitable company, in addition to making your submission to the charity regulator, you must send your trustees' annual report and accounts to Companies House within nine months of the year end. In some cases, your auditor or independent examiner will do this for you. At the time of writing, there is no online facility to submit charity accounts using Companies House's filing software. Therefore, the easiest way to do this is to send a copy of the accounts by post. There is no need to send a covering letter but the company number (and registered charity number) should be on the front page of the document. These should be sent to the relevant Companies House address for your country of **incorporation** (see the useful addresses on page 319).

Confirmation statement

There is also an annual return to submit to Companies House, but this is not usually done at the same time as the accounts filing. This is known as the **confirmation statement**. It is made on or shortly after the annual anniversary of the date of your incorporation. Paper reminder letters are not normally posted out, but an email is often sent once the date for the confirmation statement has been reached (and the company then has just 14 days to respond). Therefore, it is a sensible approach to note this date as an annual action. You must complete the confirmation statement online by accessing your charity's Companies House account. It is a short series of questions to confirm or update information about your charitable company. Currently, it costs £13 each year to file your confirmation statement (but there is no charge to file your accounts).

This chapter has provided an overview of the annual reporting process that all charities need to be aware of. It has outlined the legal requirements based on the size and legal form of a charity and has set out what you should include in a good annual report. It has looked at the annual accounting process that you need to be consider as a treasurer or finance officer. The following two chapters look more closely at the different requirements of R&P accounts and accrurals accounts following the SORP.

13 Receipts and payments accounts

As explained in chapter 12, there are two distinct ways in which a **charity** can present its year-end accounts. The first is **receipts and payments (R&P) accounts**, which are allowed for many smaller charities (see page 225 for the thresholds) and are the focus of this chapter. The other is **accruals accounts**, prepared in accordance with the Charities **SORP** and explained in chapter 14.

See chapter 4 for a technical introduction to the differences between **bookkeeping** on the R&P basis and bookkeeping on the **accruals** basis, and chapter 12 for a comparison of the two approaches from an accounting perspective, the eligibility criteria for using them and the wider reporting requirements regarding the **trustees' annual report** – required whichever type of accounts is presented.

This chapter first recounts and summarises the key considerations when using R&P accounts, including which charities are eligible for the R&P concession (if the **trustees** choose to accept it) and differences between the R&P requirements across the three **jurisdictions**. The bulk of the chapter then provides some typical examples of how R&P accounts may be presented.

Key considerations

The eligibility criteria for R&P accounts, and the advantages and disadvantages of the regime, are discussed in detail in chapter 12 (see especially table 12.2, on page 225). However, as a summary, where a charity has an annual income of under £250,000 and is *not* a **charitable company**, it will generally have the choice to prepare R&P accounts. Additionally, for the avoidance of doubt, charities that are constituted as **CIOs** or **SCIOs** are not subject to company law and therefore also have the possibility of preparing R&P accounts if their annual income is under £250,000.

Some charities will meet the criteria but choose not to take advantage of the concession. In this case, they must follow the requirements under the SORP and prepare accruals accounts, as covered in chapter 14.

Relevant legislation

In England and Wales, section 133 of the Charities Act 2011 allows a charity with an annual income that does not exceed £250,000 to prepare:

- a **R&P account**; and

- a **statement of assets and liabilities**.

For charities in Northern Ireland, section 64(3) of the Charities Act (Northern Ireland) 2008 has the same provision.

In England and Wales and in Northern Ireland, a trustees' annual report is also needed under separate provisions (see chapter 12).

In Scotland, the Charities Accounts (Scotland) Regulations 2006 (as amended) sets out in Regulation 9 that non-company charities with an annual income of under £250,000 can opt to prepare:

- a **R&P account**;
- a **statement of balances** as at the last day of the financial year;
- **notes to the accounts**; and
- an annual report.

These regulations also set out in Schedules 2 and 3 the information that is required to be included in the accounts, notes and reports.

In all three jurisdictions, therefore, it is a choice, not a requirement, to prepare R&P accounts, and trustees are free to prepare accruals accounts under the SORP instead.

Accounting under the receipts and payments regime

One of the reasons that R&P accounts are thought of as a concession is that the **transactions** that are used for the **annual accounts** can be taken straight from your charity's **accounting records** based on the dates that they were paid and received. There is no need to allocate anything to a different financial year – it is always shown in the year when the money was received or paid out. Also, with R&P accounting, there is no need to make an estimate of how much something is worth: every item in the R&P account just records the actual money received or paid out (see page 74 for further discussion of these concepts). **Closing off** the books is covered in chapter 4 (see page 70), and this will result in your final figures for the year.

Under R&P accounting the figures you need to determine are:

- *Receipts*: These must include all the amounts that have been received through the charity's bank and cash accounts (including cash, online giving and other **donation** collection platforms) for the year in question. These should be split into appropriate categories, such as **grants**, donations, **fees** and **fundraising** proceeds. You will also need to separate out receipts for different **funds** if your charity has **restricted funds** (see chapter 3).
- *Payments*: These are all the amounts that have been paid through your charity's bank accounts (including payment cards) or in cash for the year in question. These should be split into appropriate categories, such

as wages, rents, utilities, activity costs and administration (and, as with receipts, payments may need to be separated for different funds).

- *Net **surplus*** (where receipts are greater than payments) *or net **deficit*** (where payments are greater than receipts): Note that some people prefer to use the terms 'excess of receipts over payments' instead of 'surplus', or 'excess of payments over receipts' for 'deficit' – either terminology is acceptable.
- *Cash and bank balances*: You will need to know these both at the start of the year and at the end of the year, from all your bank accounts and petty cash tins.

To check that everything is included, add your net receipts (or subtract your net payments) from your opening cash and bank balances. You should get your closing cash and bank balances:

> *Opening cash and bank* + *Net receipts* (or – Net payments) = *Closing cash and bank*

Timing of receipts and payments

Receipts are accounted for in the R&P account on the date your charity receives them. If a charity with a year end of 31 December 2023 receives a grant of £20,000 on 15 December 2023, it needs to include that £20,000 in its 2023 accounts, even though the grant may be funding payments that will be made throughout 2024. The R&P accounts may then show high net receipts (or a surplus) for the year, which may look confusing.

In reality, the £20,000 will be included in your funds (and cash and bank balances) carried forward to 2024, perhaps as a restricted fund. As it is spent in 2024, your 2024 accounts may then show net payments (or a deficit). R&P accounts are sometimes criticised because they show spikes and troughs like this and do not match receipts to payments as accruals accounts do. But this is where a good trustees' report can enhance your accounts by explaining that funding was received towards the end of the year for a project the following year. And, as will be seen, in the R&P accounts themselves, you can provide a note explaining the funds held at the year end.

On the other hand, you may have provided some services at the end of the year – for example, hiring a room to an external organisation – for which the customer has not yet paid. You cannot recognise that income in R&P accounts as it has not yet been received. But you may have made payments in respect of the work, and so your result for the year may be lower than expected. In this instance, you can list the expected income as a **debtor** in the **statement of assets and liabilities** (or **statement of**

balances in Scotland), which will help readers of the accounts to understand the situation. See page 248 for what this means in practice.

As with your receipts, the timing of payments can also affect the figures in R&P accounts. If you receive a large bill at the end of the year but it is not paid until after the year end, the payment cannot be included in your R&P account. This may mean your charity looks as though it has made a much bigger surplus in the year than it really has. In this instance, you can list the unpaid bill as a **creditor** in the statement of assets and liabilities (or statement of balances), which will help to inform the users of your accounts.

The accounts: R&P basis

Once you have determined your figures for the year, there are two main reports (or **primary statements**) to prepare:

- the R&P account, showing what has come into and gone out of your charity over the year (often described as a 'movements' report);
- the statement of assets and liabilities (or statement of balances in Scotland), showing what is on hand at the end of the year (often described as a 'snapshot' report).

The remainder of this chapter first steps through these two main reports. It then considers the question of notes to the accounts and finally explores options for how you might wish to format your accounts.

Receipts and payments account for the year

In England and Wales and in Northern Ireland, there are no rules about how the R&P account should be presented. It is usual to set out the receipts at the top and payments at the bottom, and show the result of the net receipts or payments for the year. However, you are free to break down those receipts and payments into whatever categories suit your charity and are helpful for your readers. It is sensible to include a comparative column for the previous financial year too. This allows users of the accounts to see any changes between the years, and it will ensure you are consistent in the receipts and payments categories you use from year to year. The **charity regulators** of the three jurisdictions each set out useful guidance (see the further reading, on page 313).

In Scotland, the rules surrounding R&P accounts are more specific. Schedule 3 to the Charities Accounts (Scotland) Regulations 2006 sets out the details and OSCR provides additional useful guidance. In particular, in Scotland it is a requirement to show comparative figures in your R&P account. There are also defined categories of receipts and payments that should be disclosed, as detailed in figure 13.1. Any transfers between the different funds should also be identifiable.

Extract from Schedule 3 of the Charities Accounts (Scotland) Regulations 2006

Information to be shown on the R&P account:

The following receipts in particular, if any, shall be shown separately:

(a) donations;
(b) legacies;
(c) grants;
(d) receipts from fundraising activities;
(e) gross trading receipts;
(f) income from investments other than land and buildings;
(g) rents from land and buildings;
(h) gross receipts from other charitable activities;
(i) proceeds from sale of fixed assets; and
(j) proceeds from sale of investments.

The following payments in particular, if any, shall be shown separately:

(a) expenses for fundraising activities;
(b) gross trading payments;
(c) investment management costs;
(d) payments relating directly to charitable activities, detailing material items;
(e) grants and donations relating directly to charitable activities;
(f) governance costs relating to
    (i) audit or independent examination;
    (ii) preparation of annual accounts; and
    (iii) legal costs associated with constitutional matters or trustee advice;
(g) purchases of fixed assets; and
(h) purchase of investments.

Fig. 13.1 Details of the categories of receipts and payments that should be shown separately in R&P accounts

For charities in all jurisdictions, if you have different funds – such as one or more restricted funds and a **general fund**, which will be **unrestricted** – you will have to decide how they are best shown. If you only have two funds, a separate page for each fund's own R&P account may be sufficient to clearly set out all the information you need. However, if you have many funds, this will mean a set of accounts with multiple R&P accounts, which may become confusing, and it may be hard for readers to understand any transfers between the funds. In this case you could use an R&P account with multiple columns, similar to the format used in accruals accounts (see page 271). However, you must clearly state that the account has been prepared on the R&P basis, and it is normal to have just two columns for the year –

unrestricted and restricted funds – to avoid too much data appearing on one page. If your restricted funds column contains more than one fund, a note explaining the different funds is needed. Figure 13.2 provides an example of an R&P account for a charity with two funds.

MIDSHIRE YOUTH PROJECT CIO

RECEIPTS AND PAYMENTS ACCOUNT FOR THE YEAR ENDED 31 MARCH 2024

	General Fund 2024 £	Outreach Fund 2024 £	Total 2024 £	*Total 2023 £*
Receipts				
Council grant	30,000		**30,000**	*25,000*
Outreach grant		5,000	**5,000**	*0*
Miscellaneous donations	2,540		**2,540**	*3,400*
Gift Aid reclaimed	470		**470**	*660*
Membership fees	700		**700**	*650*
Outreach fundraising event		1,500	**1,500**	*0*
Bank interest	25		**25**	*19*
Total receipts	**33,735**	**6,500**	**40,235**	*29,729*
Payments				
Youth worker salaries	18,500	3,000	**21,500**	*16,500*
Administrator wages	3,000		**3,000**	*2,800*
Hall hire	2,400		**2,400**	*2,300*
Activity costs	4,857	2,500	**7,357**	*4,560*
Insurance	600		**600**	*575*
Publicity and guides	1,360		**1,360**	*860*
Fundraising costs		130	**130**	*0*
Telephone and IT	1,230		**1,230**	*1,190*
Travel expenses		475	**475**	*0*
Trustees travel expenses	234		**234**	*196*
Independent examination	400		**400**	*375*
Total payments	**32,581**	**6,105**	**38,686**	*29,356*
Net receipts less payments	**1,154**	**395**	**1,549**	*373*
Transfers between funds				
Outreach administration	200	–200	**0**	*0*
Opening cash funds	1,868	0	**1,868**	*1,495*
Closing cash funds at 31 March	**3,222**	**195**	**3,417**	*1,868*

Fig. 13.2 An example of a detailed R&P account for a CIO with two funds

In figure 13.2, the different types of receipt and payment are set out in detail. An alternative way to present the information is in a more summarised format, showing the main categories on the R&P account and the more detailed information in notes to the accounts. For example, the R&P account could show the total amount of donations received and the notes would provide a breakdown of those donations. Similarly, you could give the total amount spent on 'charitable activities' in the R&P account and provide a note to the accounts setting out a detailed analysis into categories including wages, utilities, administration and activity costs. A more summarised version of an R&P account is shown in figure 13.3.

HAPPY FAMILIES PROJECT SCIO

RECEIPTS AND PAYMENTS ACCOUNT FOR THE YEAR ENDED 31 MARCH 2024

	Note	**General Fund 2024 £**	**Outdoor Play Fund 2024 £**	**Total 2024 £**	*Total 2023 £*
Receipts					
Donations	2	5,600		**5,600**	*3,000*
Grants	3	30,000	20,000	**50,000**	*40,000*
Trading receipts from activities	4	8,400		**8,400**	*8,800*
Receipts from fundraising activities		7,700		**7,700**	*8,605*
Total receipts		**51,700**	**20,000**	**71,700**	*60,405*
Payments					
Payments for fundraising events		2,030	750	**2,780**	*1,760*
Staff payments to deliver activities	5	33,000	12,000	**45,000**	*35,150*
Other payments to deliver activities	6	13,750	5,555	**19,305**	*17,525*
Governance payments	7	800		**800**	*750*
		49,580	**18,305**	**67,885**	*55,185*
Net receipts less payments		2,120	1,695	**3,815**	*5,220*
Transfers between funds					
Outdoor Play Fund administration		1,200	–1,200	**0**	*0*
Opening cash funds		17,600	0	**17,600**	*12,380*
Closing cash funds at 31 March	8	**20,920**	**495**	**21,415**	*17,600*

Fig. 13.3 An example of a summarised R&P account for a SCIO with two funds

Statement of assets and liabilities, or statement of balances

The second report required in a set of R&P accounts is the statement of assets and liabilities, often known as the **SOAL**. In Scotland, this is known as the statement of balances, but essentially it is the same thing – a list of what your charity owns, what it owes to others and what is owed to the charity. An important distinction between this and a **balance sheet** (as found in accruals accounts) is that a SOAL is not designed to balance. There will be a balancing section between the cash and bank balances to the funds that your charity has declared on the R&P account, but the other **assets** and **liabilities** will be a list only. It is easier to think of the SOAL or statement of balances in two parts: the monetary assets and non-monetary assets and liabilities of your charity.

The monetary side should include cash, bank accounts and very short-term **investments** that your charity can access relatively quickly, such as savings in a **deposit account**. When using cash-based accounting, the total of these monetary assets will equal the funds that your charity has declared at the bottom of the R&P account. Again, the 2006 regulations in Scotland are more prescriptive and expect a reconciliation between the cash balances at the beginning and end of the year with the net receipts or payments shown in the R&P account and split out by fund.

The non-monetary assets and liabilities include amounts you are due to receive (debtors), bills you need to pay (creditors) and equipment, or similar, that your charity owns (**fixed assets**). If you wanted, you could simply list the debtors, creditors and assets your charity had at the end of the year, with no monetary values attached, but this would not provide meaningful information, so it is best to quantify them where you can.

As the **treasurer** or **finance officer**, you will know about any unpaid bills or amounts due to your charity and any purchases of capital items made during the year. However, the fixed assets will also need to include items that your charity purchased in previous years but still uses and items gifted to the charity. If you have an up-to-date **fixed asset register**, this will be relatively straightforward to obtain. Otherwise, you may need to compile a list from scratch. Remember in this section to also include any longer-term investments that your charity holds, along with buildings, furniture and vehicles. And, on the other side, any loans that your charity will need to repay or commitments to other organisations would appear as liabilities.

For some assets and liabilities, the amount to include will be straightforward – the cost paid or to be paid, or the amount due to be received from a debtor. However, the values of older assets and those that were gifted may not be so easy to determine. The 2006 regulations in

Scotland provide some guidance that it may be helpful for charities to apply throughout the UK. They specify that any investments should be stated at market value, and other assets should be listed at cost, unless the trustees consider the current valuation would be lower.

Trustees are required to demonstrate their approval of the accounts by adding a statement to that effect and signing the SOAL or statement of balances. Examples are shown in figures 13.4 and 13.5.

MIDSHIRE YOUTH PROJECT CIO

STATEMENT OF ASSETS AND LIABILITIES AT 31 MARCH 2024

	2024	*2023*
	£	*£*
Monetary assets		
Deposit account	1,025	*1,000*
Current account	2,317	*793*
Cash in hand	75	*75*
Total monetary assets	**3,417**	*1,868*
Represented by funds		
Unrestricted funds		
General Fund	3,222	*1,868*
Restricted funds		
Outreach Fund	195	*0*
Total funds	**3,417**	*1,868*
Non-monetary assets and liabilities		
Fixed assets		
Furniture and equipment	2,500	*2,500*
Office laptop	1,100	*1,200*
Total fixed assets	**3,600**	*3,700*
Debtors		
Gift Aid due	95	*0*
Creditors due within one year		
Independent examination fee	–425	*–400*
Total non-monetary assets	**3,270**	*3,300*

These accounts were approved by the Trustees on [date] and signed on their behalf by:

Name — Name

Treasurer — Chair

Fig. 13.4 An example of a statement of assets and liabilities

HAPPY FAMILIES PROJECT SCIO

STATEMENT OF BALANCES AT 31 MARCH 2024

	Unrestricted 2024 £	**Restricted 2024 £**	**Total 2024 £**	*Total 2023 £*
Cash and bank balances				
At start of the year	17,600	0	17,600	*12,380*
Net receipts	3,320	495	3,815	*5,220*
At end of the year	**20,920**	**495**	**21,415**	*17,600*
Represented by funds	**20,920**	**495**	**21,415**	*17,600*

Other balances (all unrestricted):

	2024 £	*2023 £*
Fixed assets		
Furniture and equipment	4,800	*4,800*
Office laptop	2,250	*2,500*
Debtors		
Gift Aid due	300	*0*
Creditors due within one year		
Independent examination fee	–800	*–750*

These accounts were approved by the Trustees on [date] and signed on their behalf by:

Name — Name
Treasurer — Chair

Fig. 13.5 An example of a statement of balances for a SCIO (note that the 'Net receipts' figure for each fund is the amount *after* allowing for transfers between funds)

Notes to the accounts

In England and Wales and in Northern Ireland, there is no requirement for a set of R&P accounts to contain notes. There is an exception to this for CIOs established in England and Wales. This is because a CIO is a limited liability body, and two specific notes are needed:

- details of any guarantee (legal obligation) given by the CIO, if it is still in force at the year end – for example, if the CIO has agreed to underwrite the costs of a project run by another organisation or

provided a guarantee against a commitment on behalf of a beneficiary, this must be explained;
- details of any debt outstanding at the year end which is a secured charge on an asset of the CIO – for example, if the CIO has a mortgage on the property it owns, this must be made clear.

If neither is applicable to the CIO, it is good practice to include a statement to confirm this. For example:

> The trustees confirm, in accordance with the Charitable Incorporated Organisations (General) Regulations 2012, that at year end the charity did not have any outstanding guarantees to third parties or any debts secured on assets of the CIO.

There is no corresponding requirement for SCIOs, but any charity preparing a well-considered set of R&P accounts should list any commitments or guarantees such as this on the SOAL or statement of balances (as discussed in the previous section) under 'liabilities'.

For charities registered in Scotland, the 2006 regulations specify the following information which should be given as notes to the accounts, along with any other information that may help the reader of the accounts to understand the information they contain:

- the nature and purpose of each fund, including restrictions – this often results in a **funds note** similar to that seen for SORP-compliant accruals accounts (see example in figure 14.3);
- details of grants paid, including numbers, amounts, types of activity supported and whether to an individual or organisation;
- details of any remuneration paid to a charity trustee or **connected person** (if there were no such payments, there must be a statement to confirm that);
- the total amount paid to the trustees in terms of expenses, and the number of trustees receiving expenses (if no expenses were paid, a statement confirming that is needed);
- details of any transactions between a charity trustee and a person connected to them, including the nature of the relationship, the amount of the transaction and if any amount remains outstanding at the year end.

Even for charities registered elsewhere in the UK, including notes such as these would be considered good practice and will enhance the transparency of reporting, particularly around transactions with trustees.

Notes can be a useful addition to accounts, making them clearer and providing more meaningful information or explanations to readers. Although they might not be required, if you are preparing a set of R&P accounts, it may be beneficial to consider adding notes where relevant. CCEW's guidance does indicate that the accounts should make clear which funds are restricted and the balances on them at the year end, and also that payments, including expenses, to trustees should be highlighted. Information such as this is probably best given as a note to the accounts. Also, your charity's **independent examiner** may wish to include further items for the reader's attention in their report if they feel the accounts need additional explanation (see chapter 15). A suitable note added to your R&P accounts may also avoid the independent examiner needing to raise additional issues by making a **qualified report**.

Some charities also include notes to confirm how the accounts have been prepared, the legislation followed and whether or not the charity is subject to VAT. Figure 13.6 provides an example of some notes that could accompany the R&P account in figure 13.2 and the SOAL in figure 13.4. Figure 13.7 provides an example of some of the notes that might accompany the accounts for the SCIO featured in figures 13.3 and 13.5.

MIDSHIRE YOUTH PROJECT CIO

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2024

1 These accounts are prepared on a receipts and payments basis, with all revenue and expenses shown on a cash basis. Non-monetary assets and liabilities are shown as estimates of the value at the end of the year. The charity is not registered for VAT and, accordingly, expenditure includes VAT where appropriate.

2 The CIO has two funds: an unrestricted General Fund and an Outreach Fund. The Outreach Fund is a restricted fund supported mainly by a grant to employ the services of an outreach youth worker to provide activities for young people who are unable to visit our main base. We organised a fundraising event to top up these funds. The conditions of the grant allow a small proportion to cover administration costs. This is reflected in the transfer from the Outreach Fund to the General Fund.

3 The CIO had no outstanding guarantees to third parties nor any debts secured on the assets of the CIO.

4 No remuneration was paid to any trustees during the year. Travel expenses of £234 were paid to 7 trustees (2023: £196,6) to cover costs of attending charity meetings and business.

Fig. 13.6 An example of notes to accompany an R&P account and SOAL

Formatting your R&P accounts

If you are looking to prepare R&P accounts, there are a few options to consider when deciding on the layout and form to use. You may already have a set of R&P accounts from previous years. As long as this meets any relevant current requirements and is in a good format for the readers of your accounts, this document can be rolled forward year on year. But be aware: you should ensure it is updated to take account of any changes that have happened during the year, for example in terms of legislation or layout of the report.

One option, perhaps if this is your charity's first year or you are a new treasurer or finance officer preparing the accounts for the trustees, is a standard accounts pack. All three charity regulators offer an R&P toolkit directly from their respective websites. These are spreadsheet-based standard forms, but you can add in the names of different types of receipt or payment so that they reflect your charity's activities. They all have an accompanying pack of notes to help with completion. The finished reports can be printed as a spreadsheet or PDF document. If you are happy with the layout these provide, they can be a straightforward option, but they may not give the flexibility you require. Also note that your trustees' annual report (see page 229) and your external scrutiny document (see chapter 15) have to be prepared in separate documents, although they can be combined into one document with your accounts for submission to the appropriate regulator and your **funders** and supporters.

Alternatively, your independent examiner may be able to provide you with an accounts format to use. A professional examiner who works with lots of different charities will probably have standard templates that can be tailored to your charity. It is likely they will be in one document containing the trustees' annual report, scrutiny report and accounts; this should result in a professional-looking set of accounts. However, not all small charities take on the services of a professional examiner, and someone carrying out the examination on a voluntary basis for just one charity may not be able to provide such a template.

HAPPY FAMILIES PROJECT SCIO

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2024

1 Accounting Policies

The accounts have been prepared on a receipts and payments basis in accordance with the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006 (as amended).

VAT

The charity is not registered for VAT and, accordingly, expenditure includes VAT where appropriate.

Funds

The charity has one restricted fund that has been set up due to a specific grant for the Outdoor Play project. All payments relating to that fund have been separately identified in the accounts.

	General Fund 2024	**Outdoor Play Fund 2024**	**Total 2024**	*Total 2023*
2 Donations	**£**	**£**	**£**	*£*
Golf club donation	3,000		**3,000**	*0*
Individual donations under £500	2,600		**2,600**	*3,000*
	5,600	**0**	**5,600**	*3,000*
3 Grants				
Local council grant	30,000		**30,000**	*30,000*
The Play Foundation grant		20,000	**20,000**	*0*
The Trigg Trust grant			**0**	*10,000*
	30,000	**20,000**	**50,000**	*40,000*
4 Trading receipts from activities				
Membership fees	1,200		**1,200**	*1,250*
Summer club attendance	3,900		**3,900**	*3,750*
Easter activities	2,500		**2,500**	*2,950*
Drop-in Saturday fees	800		**800**	*850*
	8,400	**0**	**8,400**	*8,800*
5 Staff payments to deliver activities				
Project worker salaries	25,000	12,000	**37,000**	*27,400*
Administrator wages	8,000		**8,000**	*7,750*
	33,000	**12,000**	**45,000**	*35,150*

Fig. 13.7 An example of detailed notes to accompany a summary R&P account and statement of balances

HAPPY FAMILIES PROJECT SCIO

6 Other payments to deliver activities

Venue hire	1,200	1,200	**2,400**	*1,200*
Activity costs	8,500	4,355	**12,855**	*12,560*
Insurance	875		**875**	*850*
Publicity and guides	1,700		**1,700**	*1,550*
Office costs	985		**985**	*850*
Travel expenses	490		**490**	*515*
	13,750	**5,555**	**19,305**	*17,525*

7 Governance payments

	General Fund 2024 £	**Outdoor Play Fund 2024 £**	**Total 2024 £**	*Total 2023 £*
AGM expenses	120		**120**	*130*
Trustee travel	180		**180**	*145*
Independent examination	500		**500**	*475*
	800	0	**800**	*750*

8 Funds

	Opening funds £	**Receipts £**	**Payments £**	**Transfers £**	*Closing funds £*
<u>Unrestricted funds</u>					
General Fund	17,600	51,700	–49,580	1,200	*20,920*
<u>Restricted funds</u>					
Outdoor Play Fund	0	20,000	–18,305	–1,200	*495*
Total funds	**17,600**	**71,700**	**–67,885**	0	*21,415*

<u>Restricted funds</u>

The Outdoor Play Fund is a restricted fund to deliver a project for local children funded by the Play Foundation grant received in the year. The small amount remaining will be spent on an activity in the next year.

<u>Transfers between funds</u>

A transfer of £1,200 was made from the Outdoor Play Fund to general funds to cover the costs of administering the project and in line with the funding agreement.

A set of R&P accounts may include:

- *Trustees' annual report*: As discussed in chapter 12, this provides users with a better understanding of your charity and is required under charity law.
- *Independent examiner's report*: This is covered in chapter 15. It tends to be placed before the accounts, so that the reader can appreciate whether there are any issues with the accounts or to assure them that everything is as it should be.
- *R&P account for the year*: This is required under all three jurisdictions (see examples set out in figures 13.2 and 13.3).
- *SOAL or statement of balances*: As set out in figure 13.4 (England and Wales, and Northern Ireland) and figure 13.5 (Scotland).
- *Notes to the accounts*: These are specifically required under the Scottish regulations for all charities completing R&P accounts. In the other jurisdictions, some notes are required for CIOs, and notes should also be included if they would help with the understanding of the accounts (see examples provided in figures 13.6 and 13.7). However, it is good practice to use notes regardless of the requirements to help the readers of your accounts understand your charity's finances more fully.

Although not strictly required, it may be helpful to provide a title page giving the name of the charity, its registered number (where applicable) and the year of the accounts. In any case, these details must appear at least at the top of a set of R&P accounts.

The vast majority of charities in the UK are classed as small.[13] This means there will be many charities producing R&P accounts. These will range from very small charities with only a few transactions to quite complex ones with staff, hundreds of transactions and multiple funds to account for. Therefore, some may need more sophisticated R&P accounts than others, although all will probably want to be seen as professional. This chapter has set out the requirements for a set of R&P accounts. If your trustees do not want to prepare R&P accounts, or are not eligible to do so, they must prepare accruals accounts, as described in chapter 14.

14 Accruals accounts and the charities SORP

Any **charity** with an annual income of over £250,000 (and below this if it is a **charitable company** – see page 225 for exact details of the thresholds in each UK **jurisdiction**) must prepare its **annual accounts** on the **accruals** basis. Additionally, any other charity may choose to prepare **accruals accounts**, rather than using the concession of **R&P accounts** discussed in chapter 13. Wherever accruals accounts are adopted, they must comply with the **Charities SORP**.

This chapter introduces the SORP and the **accounting standards** and principles it is based upon. It then explores some of the more common concepts that small and medium-sized charities may face when applying the SORP, such as **recognition** of income and **impairment** of **assets**. It next sets out examples of a **statement of financial activities**, a **balance sheet**, a **statement of cash flows** and **notes to the accounts**. Finally, it looks at special considerations for charitable companies and charities with subsidiaries.

Charities SORP

The Charities SORP is developed by a body which consists of the three **charity regulators**. The Financial Reporting Council, which has the responsibility for publishing standards that underpin accounting legislation in the UK, authorises the body to review, consult on and draft revisions to the SORP, acting on recommendations from an expert committee (the SORP Committee). The current SORP is based on the prevailing UK **accounting standard** (for company accounting requirements) known as Financial Reporting Standard 102 (**FRS 102**), which has been effective since 2015 and was last updated in 2019. You will often hear it referred to as the 'FRS 102 SORP' or 'Charities SORP (FRS 102)'. Its full title is:

> *Charities SORP (FRS 102): Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland* (FRS 102)

Accounting standards have developed over the years to harmonise the way organisations across the UK, and more widely, account for **transactions**. In fact, there is a standard known as International Non-Profit Accounting Guidance in development by the project International Financial Reporting for Non-Profit Organisations (www.ifr4npo.org). However, there is no current plan for such standards to be given statutory force in the UK. Although the general-purpose standard FRS 102 is driven by the reporting requirements of commercial, profit-making entities, sector-specific standards, such as the SORP, exist to tailor those standards to a more unique set of needs. They remain, however, based on the same set of concepts, or principles.

Currently, FRS 102 is being considered for revision and, consequently, the SORP Committee – which includes some users and preparers of accounts of all sizes as well as charity umbrella bodies, funding organisations, accountancy firms and academics – is consulting on both the impact this will have on charity accounting and other improvements that may be needed to the SORP. It is likely a revised Charities SORP will be released in late 2024 to take effect for financial years starting on or after 1 January 2025. However, this timescale means that for a charity with a 31 March year end, the first financial year where it will be compulsory to follow the new SORP will be the year ending 31 March 2026.

As the SORP refers to 'recommended' practice, there may be the misconception that it does not need to be followed as it is recommended rather than required. This is not the case, and in fact the SORP is compulsory for any charity producing accruals accounts.

Chapter 4 introduced the concept of **accruals accounting**, which is designed to reflect what is owned and owed by an organisation. Accruals accounts are intended to show a **true and fair view**, which means that the information in the accounts is considered complete, accurate and based on commonly held accounting principles to recognise, measure and present transactions (discussed in detail on page 259). The SORP is just that: a common set of instructions on how transactions should be accounted for, to present a true and fair view of the situation of a charity and enable accounts to be comparable between different organisations.

The Companies Act 2006 requires company accounts to show a true and fair view, which is why all charitable companies, regardless of size, must follow the SORP in preparing their accounts. The accounting regulations under charity law across the three UK jurisdictions also require the accounts of larger non-company charities to show a true and fair view, and the regulations refer directly to the SORP. There could be other situations where you need to complete accruals accounts, perhaps because of a **funder's** request or a requirement in your charity's **governing document**. And smaller non-company charities may wish to voluntarily adopt accruals accounting if the **trustees** consider this is a better way to reflect their finances (see page 226 for suggestions on what to consider when making this choice). In any of these situations, you must follow the SORP.

There are exemptions from this requirement to follow the SORP. For some charities another SORP may be more appropriate. For example, charities which are registered social housing providers or further or higher education institutions have specialist SORPs available for their specific industry.

For smaller non-company charities with an annual income of up to £250,000 (see page 225 for more details), there is also the alternative to prepare the accounts on an R&P basis (as described in chapter 13). As R&P accounts are not designed to show a true and fair view, the SORP is *not* applicable to them: the vast majority of the SORP is concerned solely with accruals accounts. However, even for R&P accounts, some information in the SORP, particularly surrounding the **trustees' annual report**, may be useful. Note that the R&P approach and the accruals/SORP approach are two distinct frameworks – a charity must use one or the other, it is not permissible to mix and match elements of the regimes.

Concepts and principles underpinning the Charities SORP

As noted in chapter 4, the key principle of accruals accounts is that they show the income due to a charity and the expenses and costs incurred. This provides a much clearer understanding of the charity's resources than simply the receipts and payments during the year, but it does mean that trustees need to make estimates and judgements about particular transactions and situations faced. There are no right or wrong answers, but changing those estimates or judgements means different sets of accounts could be produced for the same charity. The methods of making estimates and judgements are normally set out in a charity's **accounting policies**, which are usually summarised in the first note to the accounts (see page 277). Ultimately, the trustees must agree on the accounting policies, but in most cases they will be guided by the recommendations of the **treasurer**, **finance officer** or accountant.

It is worth noting that the judgements, estimates and, ultimately, accounting policies adopted must have some reasonable basis and be consistent. If you were to make a judgement that artificially improved your charity's financial position, the **auditor** or **independent examiner** would have to give a **qualified report** (see chapter 15). Accounting policies are normally based on the guidance in the SORP and influenced by ten accounting concepts and principles, described as 'qualitative characteristics' by FRS 102, which are designed to enable accounts to demonstrate a true and fair view. These concepts and principles are:

- *Understandability*: The information presented in the accounts must be set out in a way which is understandable by the intended readers. This does not mean you can simply omit required information if it seems too complicated, but you may need to provide more than the bare minimum to give a full understanding.
- *Relevance*: Unless specifically required, there is no need to include information that has no relevance to your charity or has no value to the user. For example, there is no need to include accounting policies or notes on situations that are not relevant to your charity; this would simply complicate the accounts and add no value.
- *Materiality*: In accounting terms, an item is described as **material** if its omission, or misstatement, could influence decisions taken based on the accounts. It is based not only on value but also on the nature and circumstances. For example, an item that may be small compared to the whole charity's accounts may be material to a particular **fund**. And certain transactions, such as payments to trustees, are always considered material.
- *Reliability*: Information is considered reliable if it is free from any error or deliberate bias that would make it look different than it actually is. If information that would be useful to the reader is omitted, or presented in such a way to mislead, it is not considered reliable.
- *Substance over form*: In some cases it will be necessary to look at the commercial substance or purpose of a transaction and not merely its legal form in order to determine how it is presented. A typical example is a finance lease for equipment where, although the organisation does not own the equipment, it has the rights to use it, and so the asset can be included in the balance sheet (with the **creditor** for the lease rentals to be paid included on the **liabilities** side of the balance sheet).
- *Prudence*: In essence, acting with prudence means not overstating income or resources, or not understating costs or liabilities, in particular acting with caution where something is uncertain. However, this does not mean you are permitted to make things look financially worse than they are or artificially hold money aside 'just in case'.
- *Completeness*: The accounts should show the whole picture for the entire charity. Neither information nor transactions should be omitted

(subject to the principles of materiality and balance of benefit and cost). This is because an omission may cause the accounts to be misleading or biased.

- *Comparability*: The accounts should be consistent year on year to allow readers to identify trends and so the accounts are comparable to those of other charities. This means using appropriate accounting policies year on year and making **disclosures** where an accounting policy has been changed as well as explaining the effects this has had.
- *Timeliness*: Accounts should be issued promptly and not be out of date. Even though accounts may not need to be submitted to OSCR or Companies House until nine months after year end (ten for CCEW and CCNI), this does not mean you should wait until just before that deadline to prepare them. By then, the information will be out of date for the readers and users of the accounts.
- *Balance between benefit and cost*: This is a judgement call. If providing certain information means your charity would incur a significant cost that far outweighed the usefulness of the information to the reader, the required information can be omitted. However, the reasons for this must be explained.

A final important consideration to ensure the accounts reflect a true and fair view is to appreciate the concept of **going concern**. Charities normally prepare their accounts on the basis of being a going concern. This is an accounting term which means it is probable that an organisation will be able to keep going for the foreseeable future (i.e. that it has resources available to meet its liabilities and obligations as they fall due). The trustees are responsible for making this assessment. In making the assessment, they should take into account all available information about the future for at least, but not limited to, 12 months from the date the accounts are approved.

It can often be an issue for charities to assess whether they are a going concern, especially those relying on annual **grant** applications. This is why **reserves** are so important for charities (see chapter 3). Being able to explain what you hold in reserve and why can form part of this assessment, along with **budgets**, **cash flow forecasts**, and known and potential funding streams. The concept of 'going concern' has become a particular focus of the **audit** community in response to charity failures (due to cash-flow issues causing charities not to be able to meet their liabilities) and in reaction to the repercussions of the COVID-19 pandemic. Whether or not they are subject to an audit or **independent examination**, trustees need to consider whether their charity has the viability to continue for another 12 months and should be prepared to demonstrate the assumptions used on their going concern assessment to their auditor or examiner.

Where it is determined that the charity is *not* a going concern, this has different implications for the accounts and the way they are presented. This is not covered within the scope of this book. If you find yourself in this situation, you should seek the services of a specialist accountant.

The accounts: accruals basis

It is possible to produce accruals accounts at the year end whether you have maintained your **accounting records** on an R&P basis or an accruals basis. However, if you understand the concepts and principles of accruals accounting, it is simpler to maintain your day-to-day accounting records on the accruals basis. Otherwise, large adjustments to your R&P figures may be needed at year end to bring in **debtors**, creditors and **fixed assets**.

The starting point for preparing the annual accounts will be to close off the books for the year and draw up a **trial balance** (see chapter 4). If you use accounting software, a trial balance will automatically be generated, as well as a statement of income and expenditure and balance sheet. However, unless you have a charity-specific accounting package, these will probably not be in the required format for SORP-compliant accounts. In any case, it is very unlikely that these accounts will be the final version. You will usually need to adjust various items to ensure that income and expenditure are properly recognised in accordance with the SORP requirements. And often accountants will finalise the numbers for accounts in spreadsheets outside of computer package. If this is the case, it is usually possible to input the adjustments, once finalised, into the accounting package so that they are included in the correct year. This is recommended so that the system is directly in agreement with the final accounts.

If you are using spreadsheet-based accounting records rather than a computer package, perhaps as a very small charitable company, you will need to extract the balances from each item of income and expenditure and lists of any debtors and creditors to generate the trial balance.

For some charities, at this point the treasurer or finance officer will send the trial balance and any draft accounts to the auditor or independent examiner. This person will then be able to use this information as a basis for the accounts and advise on any adjustments for the trustees to approve before the full accounts are drawn up. (See page 235 for various possible ways to split the work between those within your charity and the external auditor or examiner.)

The adjustments that may be needed for the accounts include those typically associated with accruals accounting – such as those for debtors, **prepayments**, creditors and accrued liabilities – to ensure the accounts reflect what is owed to and owed by your charity for the year. They may also include adjustments for fixed assets to reflect how your charity uses them over time, rather than taking the full cost at the time of purchase. See chapter 4 on typical adjustments under accruals accounting.

But FRS 102, and how it is applied by the SORP, also relates to areas where more complex accounting may be required.

Potential accounting complexities

The SORP itself is over 200 pages long and provides a comprehensive, although technical, guide to accounting for the situations a charity may encounter, describing acceptable accounting policies and what information should be disclosed in the accounts. Some more common areas that you may encounter include income recognition, cost estimation, and **fair value** and impairment.

Income recognition

To record income correctly in SORP-compliant accounts, you need to understand the nature of a particular income transaction. Two considerations, among others, are whether there is any restriction on the income (see chapter 3), and whether it arises from an exchange transaction (such as a **contract**) or is a gift (see chapters 7 and 8). These factors will allow you to ensure the income is reflected in the correct area of your accounts, but you also need to be aware of the principles of income recognition.

The SORP requires income to be recognised when your charity is entitled to it, when it is probable that the income will be received and when the value can be measured reliably. This has implications for **performance-related grants** and for grants that are conditional on matched funding, where the terms imply that entitlement to the funding is dependent on meeting certain milestones. For example, imagine a grant of £100,000 over two years has been awarded on the basis that the charity will deliver a series of workshops to help beneficiaries learn practical work skills. The grant agreement stipulates that £75,000 is payable at the start of the project and the final £25,000 will be payable only when a certain number of beneficiaries have completed the course. If, at the end of the year when the accounts are drawn up, there is uncertainty about whether the required number of beneficiaries will be reached and it is not considered probable that the charity will receive the final £25,000, this should not be recognised in the annual accounts and only £75,000 should be recorded as income.

In contrast, imagine that there is no stipulation on the number of beneficiaries. The terms indicate that all funding is receivable as long as the workshops are carried out; however, it will be paid in quarterly instalments, with the final £25,000 falling in the following financial year. In this case, the charity is entitled to the full £100,000 and it is probable that it will be achieved if the project is being carried out. Therefore, the charity should recognise the full £100,000 income in its annual accounts, even though it has only received £75,000 in the year.

In the same way, a legacy may be recognised as income once you have been notified of the death of the legacy **donor** and the amount due to your charity, even though the funds may not be received until a future financial year. This can result in having much higher income declared in your accounts than your cash flow reflects. It may therefore be helpful for readers of your accounts to explain the legacy, and when it is likely to be received, in a note to the accounts.

Multi-year funding

The principles of income measurement may appear problematic with multi-year funding, especially for a large funding agreement for a relatively small charity. For example, imagine a grant of £300,000 has been awarded to a charity to carry out a three-year project. There are no milestones, but the grant will be paid in three equal instalments at the start of each financial year. In this case the charity is entitled to the full £300,000, it is probable that it will be received as it is set out in the grant award letter, and it is measurable as the award states the amount. The SORP therefore requires the charity to recognise the full £300,000 income in year one, even though £200,000 of it has not yet been received. The £200,000 is recorded as a debtor (grant receivable) on the balance sheet.

For a small charity, recognising such a large amount of income in year one may mean its accounts look confusing to some readers. Someone only reading the **SOFA** may think the charity has a high level of income and not appreciate that it is to cover a three-year period. However, it will often be the case that multi-year funding relates to a restricted grant, and therefore the unspent balance (which relates to future years) would be identifiable as a restricted balance carried forward in the **funds note** (as shown in figure 14.3, on page 279). And of course, it is possible for the trustees to highlight and explain any multi-year funding that has been received in their annual report. Also be aware that recognising a large multi-year grant could push your charity over the audit threshold. In some exceptional cases, there may be the opportunity to apply for an audit dispensation (see page 295) if going over the audit threshold is a worry.

However, the need to recognise a multi-year grant in full when the grant is awarded only applies when there are no significant conditions on the subsequent instalments. For example, where it is uncertain that conditions attached to the grant can be met in future years due to factors beyond your charity's control, it may be possible to recognise the income only when it is received. It is advisable to discuss situations like this with your external examiner when they arise.

Where you need to recognise a multi-year grant in full but you will receive instalments in the future, it may be necessary to consider the present value of money in recognising those instalments if current and future predicted **inflation** rates are material. In times of high inflation, the portion of the grant you receive in later years will probably be worth much less than currently; therefore, the difference from the present value is likely to be material. This can be a complicated calculation, but it rests on the principles of **fair value** (see page 267) and the idea that money received in the future will not be worth as much as it would be today.

For example, take the above grant of £300,000 that is receivable in three equal annual instalments. The calculation requires the trustees to consider a discount rate (usually based on the cost of borrowing or inflation) and use that to discount the income receivable each year in the future back to what it would be worth now. For example, with a discount rate of 4%:

- £100,000 in year one has a present value of £100,000;
- £100,000 in year two has a present value of £96,000;
- £100,000 in year three has a present value of £92,160.

Therefore, although the grant is £300,000 over three years, the total amount to recognise as income in year one is £288,160. On the other side of the **double entry**, £100,000 is recorded as in the bank and £188,160 as a debtor. In the following year, when the second £100,000 is received, there is no additional income recorded, but the debtor is reduced by £96,000 and the £4,000 treated as finance income (similar to bank interest). The same principle occurs in the following year.

Income received in advance

Sometimes income is received *before* it can legally be used – for example, a grant with a condition that it cannot be spent until the following year, or payments from attendees at a conference that your charity is organising for next year. In that case, the income should be **deferred** in the current year, so it can be included as income in the following year when your charity is entitled to use it. Deferring an amount means recognising it on your balance sheet as a liability (a creditor) rather than as income. Where this relates to funding over more than two years, the figures in the balance sheet will need to be split into amounts receivable and payable within one year and over one year.

Donated goods and services

The income recognition principles should also be applied to donated goods and services that your charity receives. For example, if you receive free office space or premises to carry out your activities, you are receiving an economic resource to help you deliver your **charitable purposes**. Under the SORP, it is necessary to value this donated space. In this instance, you would be able to use the cost of the commercial rent on the space used, or a similar alternative to reflect the costs your charity would have to pay elsewhere, to determine an 'income' amount to include in your accounts. You would enter this same amount as a cost to your charity too, to reflect that it is needed to deliver your charity's purpose. Overall, therefore, there is no effect on your charity's **surplus** or **deficit**. However, in increasing your charity's income, you should consider whether this affects any threshold, such as for external scrutiny.

An exception to this is the contribution of general volunteers, which does not need to be valued and included in the accounts. This is because the monetary value of the impact of volunteers cannot be measured reliably for accounting purposes, in most part due to there not being an open market rate for volunteers. Instead, you should make a disclosure regarding the extent and nature of volunteering within your charity in the trustees' annual report or the notes to the accounts.

Estimating costs

The SORP also requires calculations to estimate costs to your charity that may never result in any payment. One example would be accrued staff holiday time. For example, if a staff member had not taken all their holiday entitlement that they were due at the year end, your charity would effectively owe them those 'holiday days' at the time of the accounts. A calculation can be made using salary costs apportioned over the number of holiday days not taken to determine the extra salary cost needed for the accounts. This will reduce the salary costs in the following year once the holidays are taken. (However, adjustments of this kind are only needed where they would be material to a reader of the accounts.)

Under the SORP, you are also required to assess whether any conditions exist on the balance sheet date that may result in a financial obligation in the future – for example, a contract your charity has entered into with obligations that need to be met, or perhaps a situation where you may be obliged to make a future payment because of a dispute. A common example is where a charity has received a grant towards a major building project but under the condition the funder could reclaim the building if the charity folded.

Where any obligations are known with certainty (both the amount due and that it will have to be paid), they will be accounted for as creditors or accrued as discussed in chapter 4. However, if there is uncertainty that the obligations will in fact arise, a judgement will need to be made. A cost must be recognised in the accounts if, at the balance sheet date, as a result of a past event, it is probable that a payment will be needed and the amount can be measured or estimated reliably. As part of your audit or independent examination (where relevant), you will be asked about any future obligations, such as contracts, legal claims or potential disputes.

Fair value and impairment

Fair value is an accounting term that means the amount at which an asset or liability of your charity could be exchanged in an arm's length transaction (i.e. an estimate of what that asset or liability would be worth in a free market transaction). Under FRS 102, and therefore the SORP, this has implications for any asset or liability your charity holds, especially where benefits and obligations exceed 12 months (for example, the £300,000 multi-year grant described on page 264).

For assets and liabilities that can be readily exchanged for cash, the fair value is generally the same as the cost. In other cases, determining the fair value is pretty straightforward, as there will be a ready market – for example, if you hold **investments**, they should be valued at the market price on the balance sheet date. But for other assets, you may need to use the trustees' best estimate of fair value, where necessary using the services of an expert valuer.

Fixed assets, such as buildings, equipment and vehicles, used in your charity's operational work should usually be recorded in your accounts at cost. For most equipment and vehicles, it is likely their value will decrease over time. The **depreciation** policy adopted will spread the cost of the asset over its estimated **useful life**, thus reducing the balance sheet value of the asset in your annual accounts over time. It is probable that this net book value of the asset will be similar enough to the actual value of the asset to be considered the fair value.

However, where the trustees consider there has been a significant change in the value of an asset – either an increase or decrease – there are options to revalue it. If the trustees choose to adopt an accounting policy of revaluing **tangible assets**, this must be carried out across all assets of the same kind. For example, if your charity owned two operational buildings, you could not choose only to revalue one to fair value; you would need to revalue both (the entire class of asset). But it is possible to have a policy to revalue buildings, but not vehicles or office equipment, for example.

This revaluation principle applies to operational assets used in your charity's work, such as a building which serves as your charity's base of work. But some charities also have investment assets – for example, a building they rent out purely to generate income. Others have investment portfolios, often managed by external advisers. The SORP states that investment assets *must* always be revalued to a reasonable estimate of market value.

Where the trustees decide that they should adopt a policy of revaluation, they will need to have a reliable means of market valuation, such as evidence of an active resale market (for example, the commercial real estate market), a report from a professionally qualified valuer or similar. Your policy should also indicate how frequently the valuations will be carried out. The trustees will need to consider the cost of these appraisals, especially as valuers' fees may be significant. If assets are revalued, specific accounting treatment needs to be followed, including establishing a revaluation reserve/fund in your funds analysis to record the difference between the original value of the asset and the new fair value on the balance sheet and recognising the same gain or loss in the SOFA.

In some cases, the fair value of the asset may have substantially decreased, and the value shown on the balance sheet may then exceed any recoverable amount that would be received if the asset were sold. This is known as impairment. An impairment loss reflects a decline in the potential for future use of an asset compared to what was previously anticipated. The trustees should assess whether there is any indication that an asset may be impaired at each year end. If there is no indication of impairment, there is nothing further to do.

Factors to consider which may suggest a reduction in the value of an asset include both internal and external elements, such as a significant decline in the market value of the asset, changes in technology which make something obsolete or evidence of physical damage. There may also be occasions where changes in your charity's activities mean that an asset does not have the same value to your charity any more. However, changes in the use of an asset due to fluctuations in the demand for your charity's services would not necessarily mean the asset's value itself is impaired, especially if there is an open resale market where it could be sold to another organisation that was able to use it. However, ceasing to use, or a permanent significant reduction in the use of, an asset (for example, where technological advances mean the asset is no longer of use) may indicate that an impairment should be accounted for.

Accounting for an impairment involves reducing the amount of the asset in the balance sheet and recognising that reduction as a loss in the SOFA. Further disclosures may also be needed in the notes to the accounts. If you are seeking to make a revaluation or impairment of your charity's assets, you should consult the SORP and you may also require the advice of a professional accountant.

Preparing the accounts

The sections above cover examples of only some matters that need to be considered for SORP-compliant accounts, but they highlight the complexity involved and technical accounting that could be required. It is not possible to include all principles and rules here; this chapter can only attempt to draw your attention to some of the areas that, as a treasurer or finance officer, you should be aware of in preparing accruals accounts. You should, in all respects, refer to the SORP as your main point of guidance and seek the support of your external examiner or auditor or even a specialist charity accountant where needed.

Whenever you are considering the accounting required in these situations, or other areas in the SORP, remember that the concept of materiality applies. As explained above, something is considered material when, if it were omitted or misstated, this would lead to the accounts not giving a true and fair view. Therefore, it may be appropriate to say, for example, that recognising the present value of multi-year grants would not be material to the accounts, and therefore the adjustment has not been made. However, to use this as a reason, you need to have an idea of the cost and compare that to the total expenditure in the accounts to make the judgement.

You will also need to decide how the accounts are going to be drawn up once the figures are finalised. For very simple accruals accounts, CCEW has an accruals accounts pack (CC17 – see the further reading on page 313). Some professional accountants, and even charities themselves, have specialist software to help them prepare a well-presented full set of accounts in the SORP format, including all the notes.

But even charity-specific accounts software tends to be generic and may not appropriately reflect your charity. There may be some notes that are automatically generated but are not relevant, and others that do not quite say what you want. Therefore, the task of preparing the notes is sometimes best carried out with a word-processing application. If you are using a professional accountant, they may do that for you, but it is good practice to make sure that all the notes and explanations – for example, explanations about the purposes of each fund – are worded in a way that suits the readers of your charity's accounts. In some instances, it will not be possible to avoid technical terms, but these can be explained. You can always give more information than the bare minimum to help readers understand the details presented.

The next section considers the content of accounts in more depth.

Contents of accruals accounts

The Charities SORP is very clear on how a charity's annual accounts should look, particularly in the format of the main statements, and the notes and disclosures that need to be made. There are some minor concessions to charities with an annual income of £500,000 or less. But in general, if a charity is preparing accruals accounts, the full SORP presentation and notes must be used.

A set of accruals accounts, often called **financial statements** when it contains all of the documents listed below, will normally include the following when it complies with the SORP:

- *A title page*: Although not strictly required, a cover page to the accounts is useful to state the name of the charity, its registered number (where applicable) and the year of the accounts. It can have your charity's logo and will often have a title, such as 'Annual report and accounts'.
- *A contents page*: This sets out what is in the remainder of the document (not compulsory, but helpful for readers).
- *Trustees' annual report (annual report or TAR)*: This is crucial to explain the work of your charity alongside the financial details in your accounts. Chapter 12 explains the requirements for the annual report (the requirements are essentially the same whether the accounts are on the accruals (SORP) basis or the R&P basis).
- *Independent examiner's or auditor's report*: This is covered in chapter 15. It tends to be placed before the accounts so that readers can appreciate whether there are any issues with the accounts, or be assured that everything is as it should be.
- *Statement of financial activities (SOFA)*: This provides a true and fair view of your charity's income and expenditure over the year (see the next section).
- *Balance sheet*: This gives a true and fair view of your charity's financial position at the end of the year. It considers the assets and

liabilities of the charity and how they reconcile to the funds it holds (see page 273).

- *Statement of cash flows*: This provides information as to how your charity has generated cash resources and used those resources in delivering its activities. It is only compulsory to include this statement for larger charities (see page 276).
- *Notes to the accounts*: Under the SORP, notes are required for most items appearing in the SOFA and balance sheet. The notes are used to analyse and explain the numbers in the accounts and are considered essential for both a full understanding of the finances of your charity and comparability with similar organisations (see page 277).

In the past, there have been different versions of the SORP aimed at charities of different sizes, but there is now just one version in operation: that based on FRS 102. If you look at a charity's accounts from previous years, you may see references to SORP 2005 or the FRSSE SORP (based on the Financial Reporting Standard for Smaller Entities, which has now been withdrawn). Unfortunately, you may also come across these references in more recent accounts. These are probably retained in error by treasurers, finance officers, examiners and accountants who are not up to date with charity accounting.

Note that at the time of writing, the 2008 Regulations for charities in England and Wales still refer to the SORP 2005, but this is out of date, and CCEW encourages trustees to use a 'true and fair override' in order to apply the Charities SORP FRS 102 (Part 8.1.4 of CC15d; see the further reading, on page 313). A true and fair override is permissible when the regulations are out of date. In the accounts, it is achieved by including a note (as part of the accounting policies) that the trustees have applied a true and fair override to depart from the 2008 Regulations in order to apply the SORP FRS 102. This note is only needed in England and Wales. Most charity accounts should now reference the SORP FRS 102 – though, as explained above, it is likely this SORP will be replaced in the next few years.

Statement of financial activities

The **SOFA** is an **income and expenditure account** divided into columns to reflect the main categories of funds: **unrestricted funds** (including **designated funds**), **restricted income funds**, and capital or **endowment funds** (see chapter 3 for definitions). There is also a column showing the total income and expenditure of all funds in the current year (and normally a comparative total for the year before). Although it may seem complex at first, the SOFA can be a very helpful way of understanding the income and expenditure of a charity – as a whole but split between

unrestricted and **restricted funds** – on one page. See the example in figure 14.1, later in this section.

The SORP requires that every figure in the SOFA has a comparative. In practice this is achieved in one of two ways. You can create the SOFA with eight columns – all of the current year's figures in one set of four, followed by the prior year's figures for comparison. To fit this on one page with the descriptions for each row, it is likely that the page will need to be landscape. An alternative way, and probably more widely adopted, is for the SOFA to have the current year's figures across all funds and the total, but comparatives only for total figures. A full prior year's SOFA can then be included in the notes to the accounts. This may be clearer for readers of the accounts. You can omit columns where the funds are not applicable.

Within each of the columns, there could actually be several funds added together. For example, a charity might have a number of projects supported by different restricted funds; however, in the SOFA, they would be combined into one 'restricted funds' column. But in the notes to the accounts, there must be a description of any individual balances for each of the funds. An example of a 'funds note' is given in figure 14.3 (on page 279).

The rows of the SOFA are split into income and expenditure categories, and there is a separate line for transfers between funds (see page 46 for more on this). This makes it clear where, for example, unrestricted funds have been used to support a restricted fund, or overheads have been covered by a restricted fund where the terms of the restricted funding allow for an element of overhead or core costs. The total of this row should always be zero, as it does not show new income or expenses but a movement between funds. In some instances, there may be further rows in the SOFA to record gains and losses on investments, and any unrecognised gains on revaluation of assets (where an asset has been revalued to a higher amount but that has not crystalised as the asset has not been sold – see page 267 for more information).

The SORP rules specify the various **functional headings** to be used for the income and expenditure lines. This is to ensure comparability between different charities; however, there is an alternative for smaller charities, as will be explained below.

The standard functional headings have varied with different versions of the SORP, and the current ones are shown in figure 14.1. The SORP encourages this analysis of income and expenditure by what it terms 'activity', or the purpose of the spending. This means that on the SOFA you will need to distinguish between your expenditure on 'raising funds' and that on 'charitable activities'. Charitable activities can be further split if your charity carries out work in several distinct fields. This generally means you will need to identify which costs are attributable to which 'activity'. In some cases, this could mean splitting a salary. For example, if your **charity co-ordinator** spends 25% of their time on **fundraising**, 25% of their costs should be allocated to the 'raising funds' line with the balance to 'charitable activities'.

Although the SORP encourages the use of this format for all charities, and requires it for those with an annual income of over £500,000, there is an exception for smaller charities, which can report their income and expenditure on an alternative basis where this would be easier. For example, expenses could be broken down under headings such as 'salaries', 'premises', 'depreciation costs' and similar – these are described as 'natural headings'. Even for larger charities, some analysis of costs under these types of natural heading is needed in the notes to the accounts. However, a smaller charity producing SORP-compliant accounts must still follow all other aspects of the SOFA format.

Figure 14.1 provides a typical example of a SOFA format for a charity that has one or more restricted funds and an endowment fund but does not have any gains or losses from investments or fixed assets. This example assumes that the comparative figures for the prior year's analysis of funds are given by way of a note to the accounts, with only a prior year's total shown on the SOFA itself.

Balance sheet

The balance sheet is designed to show all of a charity's assets and liabilities. These are balanced against the funds that the charity holds (see the example in figure 14.2, on page 275) An important point is that all debtors, creditors and fixed assets must be included in the fund to which they relate. This is not expressly shown on the balance sheet but is analysed in a note to the accounts.

The top half of the balance sheet is very similar to any used by a commercial business. But the bottom half is very different. For a charity, all assets belong to the charity either to meet its general purposes (unrestricted funds) or to meet certain restricted or endowment purposes. As the Charities SORP is based on FRS 102, all assets and liabilities must be measured at fair value (see page 267). For many of the items, particularly debtors and creditors, the fair value will be at the cost that is due to be paid by the charity or funder. The SORP sets out the rules surrounding obtaining valuations on assets.

MIDDLEHAM COMMUNITY HALL CIO

STATEMENT OF FINANCIAL ACTIVITIES FOR THE YEAR ENDED 31 MARCH 2024

	Note	Unrestricted funds 2024 £	Restricted funds 2024 £	Endowment funds 2024 £	Total 2024 £	*Total 2023 £*
Income and endowments from						
Donations and legacies	x	11,500	230,000		**241,500**	*195,700*
Charitable activities	x	22,750			**22,750**	*20,795*
Other trading activities	x	5,050			**5,050**	*6,700*
Investments	x	222			**222**	*199*
Total receipts		**39,522**	**230,000**	**0**	**269,522**	*223,394*
Expenditure on						
Raising funds	x	9,800			**9,800**	*8,990*
Charitable activities	x	22,675	216,800		**239,475**	*208,875*
		32,475	**216,800**	**0**	**249,275**	*217,865*
Net income		**7,047**	**13,200**	**0**	**20,247**	*5,529*
Transfers between funds						
Contribution to projects		(4,500)	4,500	0	**0**	*0*
Net movement in funds		**2,547**	**17,700**	**0**	**20,247**	*5,529*
Reconciliation of funds						
Total funds brought forward		87,565	8,650	225,000	**321,215**	*315,686*
Total funds carried forward	x	**90,112**	**26,350**	**225,000**	**341,462**	*321,215*

In this example, 'x' indicates where a note may be needed to analyse the numbers in the accounts in more detail. These would be set out in the 'Notes' section of the accounts.

It is usual in this type of accounts to distinguish negative numbers, which represent an outflow of funds compared to an inflow, by using parentheses – as shown in the 'Transfers between funds' section.

Fig. 14.1 An example of a SOFA for a charity with one or more restricted funds and an endowment fund

MIDDLEHAM COMMUNITY HALL CIO

BALANCE SHEET AS AT 31 MARCH 2024

	Note	**Total 2024 £**	*Total 2023 £*
Assets and liabilities			
Fixed assets – tangible			
Community Centre	*x*	**225,000**	*225,000*
Furniture and equipment	*x*	**18,650**	*17,300*
Total fixed assets	*x*	**243,650**	*242,300*
Current assets			
Debtors and prepaid expenses	*x*	**13,680**	*5,290*
Cash at bank and in hand		**92,582**	*93,760*
Total current assets		**106,262**	*99,050*
Creditors: amounts falling due within one year			
Deferred income	*x*	**0**	*(12,500)*
Accruals and other liabilities	*x*	**(8,450)**	*(7,635)*
Total current liabilities		**(8,450)**	*(20,135)*
Net current assets		**97,812**	*78,915*
TOTAL NET ASSETS		**341,462**	*321,215*
Represented by funds			
Unrestricted funds		**90,112**	*87,565*
Restricted funds		**26,350**	*8,650*
Endowment funds		**225,000**	*225,000*
TOTAL FUNDS	*x*	**341,462**	*321,215*

Approved by the Trustees on [add date] and signed on their behalf by:

Name　　　　　　Name

Treasurer　　　　Chair

In this example, 'x' indicates where a note may be needed to analyse the numbers in the accounts in more detail. These would be set out in the 'Notes' section of the accounts.

It is usual in this type of accounts to distinguish negative numbers, which represent liabilities, by using parentheses – as shown in the 'Creditors' section.

Fig. 14.2 An example of a balance sheet for a charity with one or more restricted funds and an endowment fund

The balance sheet must show comparative figures for the previous year, for all figures, and must be signed by the trustees to show that they have approved the accounts. Figure 14.2 provides a typical example of a balance sheet for a charity.

Statement of cash flows

For any charity with an annual income of more than £500,000, the SORP requires another statement, known as the statement of cash flows. This is different from any cash flow that you may produce as part of your charity's ongoing financial management (as described on page 117). It is normally placed after the SOFA and balance sheet, but before the notes. Smaller charities (with an annual income of under £500,000) have the option of preparing this statement but can take advantage of an exemption to not include one (in practice, very few such charities include this).

The statement of cash flows is used to demonstrate where a charity has generated money coming into the charity and how that money has been used – literally the movements of money (cash, bank balances and short-term deposits) in and out of the charity. In some ways, it is taking what is on the SOFA and balance sheet and reverting that to R&P accounts, although the format that must be used is very different. The reason for this statement is that it highlights the solvency of the charity. A charity may look like it has a lot of income, but do the cash balances reflect that, or is the cash flow very tight? However, as with the SOFA, this is a historical statement of the movements that have already happened – it does not forecast how the charity can meet its future obligations.

The SORP sets out the requirements of the statement of cash flows. You are required to show the cash flows in three broad areas – both for the current and the prior year:

- those from *operating activities*, or the normal running of your charity's activities;
- those from *investing activities*, which may be income from dividends, interest or rents from investment properties, as well as proceeds from any sales of investments, or costs to purchase them;
- any cash flows relating to *financing activities*, such as repayments of borrowings, cash inflows from a new borrowing or a receipt of an endowment.

The net amount of all those cash flows should be equal to the change in the cash and bank balances of your charity from the start of the year to the end of the year. If you do need to include a statement of cash flows in your annual accounts, the SORP has an example of the layout needed and your auditor or independent examiner will be able to assist in the preparation of this statement.

Notes to the accounts

With accruals accounts, notes are legally required. In fact, there is usually a great deal of information that has to be disclosed in the notes. Even for some relatively small charities, the notes may run to four or five pages, sometimes more. Generally, where a figure is provided in the SOFA or balance sheet, there will be a note behind it.

In most cases, where a note is not applicable, it can be omitted. But in some cases, a negative statement is needed. For example, if no remuneration or expenses have been paid to trustees, the accounts must have a note that states something along the lines of 'No remuneration or expenses were paid to any trustees during the year.' As with all figures in the accounts, comparatives must be provided for the prior year.

The list below explains some notes that could be required; full details can be found in the Charities SORP:

- Your *accounting policies* can require a long note in itself. This note sets out the accounting policies your charity has adopted – for example, in recognising income, valuing donated services, allocating costs and recording fixed assets. The note will usually set out the basis of preparation of the accounts and refer to the relevant charity legislation and the SORP. It will also confirm whether the trustees have prepared their accounts on a going concern basis (see page 259).
- Where you note the *accounting standards* you have used, you will need to mention FRS 102 and the Charities SORP, as well as the details of, and reasons behind, any departures from the regulations and SORP needed for the accounts to show a true and fair view.
- *Critical judgements and estimation techniques* used by the trustees to measure any of the material figures in the accounts.
- Details of any *material changes in accounting policies and techniques* from the prior year, and any change in your accounting year-end date.
- Any *adjustments to last year's figures* due to errors or changes in accounting policy or estimation technique.
- The *nature and purpose of each fund ('funds note')*, together with balances at the start and end of the year, and the movements through the year. This can be an extremely meaningful note for users of the

accounts – an example is provided in figure 14.3. The funds note should highlight any **inter-fund transfers**, and, for any fund with a negative balance at the end of the year, why this is so and how the trustees will address it.

- *Transactions with related parties* – for example, any fees paid to trustees or their relatives or businesses where they have significant interests. Where none, the note must expressly state 'none'.
- *Trustees' expen*ses. Where none, the note must expressly state 'none'.
- *Details of staff costs* split between gross salaries, employer's National Insurance and pension costs. Where individual staff salaries are over £60,000 a year, additional disclosures are required.
- *Auditor's or independent examiner's remuneration*, and any other fees for services provided by them.
- Analysis of your charity's *main income lines* – for example, listing major grants and **donations**.
- Details of any *grants made* to organisations and individuals.
- Analysis of your charity's *expenditure*, including fundraising costs and how support costs (core costs or overheads that support the activities of your charity, such as **governance** costs, payroll administration and computer costs) have been allocated.
- Analysis of *fixed assets and investments* to explain movements in the year.
- Analysis of *debtors and creditors* in the balance sheet.
- Analysis of how *net assets* are split between unrestricted, restricted and endowment funds.
- Details of any *incoming resources to capital or endowment funds*.
- Details of any *subsidiaries* of your charity (including turnover, net profit and details of any audit report).
- Details of any *guarantees* (legal obligations to underwrite a debt or liability) given to third parties.
- *Loans* to your charity (if secured on the charity's property) or loans it has made.
- *Comparative statement* for the SOFA, where all comparatives are not given on the SOFA itself.
- *Any other information* needed to give a true and fair view or to assist readers to understand the accounts.

This list is not exhaustive, and you should refer to the SORP and relevant regulations where necessary.

MIDDLEHAM COMMUNITY HALL CIO

MOVEMENT IN FUNDS NOTE FOR THE YEAR ENDED 31 MARCH 2024

	Note	Opening funds as at 1 Apr 2023 £	Income £	Expenditure £	Transfers £	Closing funds as at 31 Mar 2024 £
Unrestricted funds						
General Fund	[a]	87,565	39,522	(32,475)	(14,500)	80,112
Designated – building repairs	[b]	0	0	0	10,000	10,000
Total unrestricted funds		**87,565**	**39,522**	**(32,475)**	**(4,500)**	**90,112**
Restricted funds						
Staying Active Project	[c]	0	150,000	(128,500)	0	21,500
Mental Health Project	[d]	6,650	65,000	(76,150)	4,500	0
Dementia Friendly Project	[e]	2,000	15,000	(12,150)	0	4,850
Total unrestricted funds		**8,650**	**230,000**	**(216,800)**	**4,500**	**26,350**
Endowment funds						
Community centre building	[f]	**225,000**	**0**	**0**	**0**	**225,000**
TOTAL FUNDS		**321,215**	**269,522**	**(249,275)**	**0**	**341,462**

Nature and purpose of funds:
[a] The General Fund represents the free reserves of the charity, which are available for any expenditure within the charity objects.
[b] Provision agreed for expected repairs in 2024/25.
[c] The Staying Active Project is an initiative funded by the Better Communities Trust to introduce projects that meet the needs of people living in the local community and encourage them to take part in a wider range of activities. We have used this funding to deliver projects for all age groups in the year and they will continue into the next year.
[d] The Mental Health Project was funded by the Wellness Foundation as a two-year project to address mental health needs among young families. This project is now complete.
[e] The Dementia Friendly Project is an initiative set up by the community centre to raise funds specifically to make the centre a dementia-friendly space.
[f] The endowment fund represents the value of the community centre building.

Transfers between funds:
A transfer was made of £4,500 from the General Fund to meet the final costs of the Mental Health Project.
A transfer was made of £10,000 from the General Fund to a designated fund by a decision of the trustees to earmark some funds for necessary building repairs.

It is usual in this type of accounts to distinguish negative numbers, which represent outflows of funds, by using parentheses – as shown in the 'Expenditure' and 'Transfers' columns.

Fig. 14.3 An example of a funds note for a charity with one or more restricted funds and an endowment fund

Charitable companies

When preparing accounts, charitable companies must also ensure they are complying with the Companies Act 2006. For the accounts, there are similar requirements. In general, SORP-compliant accounts will be sufficient to meet the Companies Act requirements, but you may also need to add other disclosures. For example, the title of the SOFA should make it clear that it also includes the 'income and expenditure account'.

A charitable company will occasionally need a separate income and expenditure account for the purposes of the Companies Act, where company accounting requires a different treatment from the SORP. However, this only applies in rare cases – for example, where a charity has received new endowment funds.

Additional disclosure for a charitable company

A key requirement for charitable companies is to reflect on the balance sheet that the trustees acknowledge their responsibilities for complying with the Companies Act as directors in respect to accounting records and preparing accounts, and that, where applicable, accounts have been prepared with the special provisions given to smaller entities.

A smaller entity, for the purposes of the Companies Act, is described under Part 15 of the Act. In general, to be classified as small, a company must meet at least two of the following:

- income not more than £10.2 million;
- balance sheet total not more than £5.1 million;
- no more than 50 employees.

These limits (which have to be considered for both the year for which accounts have been prepared and the previous year) are much more generous than those in charity legislation. So, for any company with charitable status, these limits can largely be ignored for accounting and reporting reasons, and they will only have an impact on the disclosures for the balance sheet.

Small companies receive the concession that they are exempt from audit (Part 16 of the Act). However, as noted in chapter 12, an audit is required for any entity with charitable status, including a company, where its annual income exceeds £1 million in England and Wales, or £500,000 in Scotland or Northern Ireland. Therefore, this exemption is only available to charitable companies where their income is below the charity audit threshold. However, strictly speaking, it is a decision for the *members* of the company as to whether a company below the audit threshold should still have an audit (rather than the trustees/directors), so the note on the balance sheet must refer to a decision of the members.

It is common to see a statement along the lines of the following example wording at the end of the balance sheet for a charitable company, to comply with the Companies Act 2006 requirements.

Example of a balance sheet statement for a charitable company subject to audit:

> These accounts have been prepared in accordance with the special provisions relating to small companies within Part 15 of the Companies Act 2006.
>
> Approved by the board and authorised for issue.

Example of a balance sheet statement for a charitable company where an audit is not required:

> For the year ended [add date] the charitable company was entitled to exemption from audit under section 477 of the Companies Act 2006 relating to small companies.
>
> - The members have not required the charitable company to obtain an audit of its accounts for the year to [add date] in accordance with section 476.
> - The directors (who are also the trustees) acknowledge their responsibilities for complying with the requirements of the Act with respect to accounting records and the preparation of accounts.
>
> These accounts have been prepared in accordance with the special provisions of Part 15 of the Companies Act 2006 relating to small entities.

Bear in mind that a charitable company below the audit threshold will still need an independent examination of its accounts (except for those in England and Wales with an income of no more than £25,000) – see chapter 15. But company law does not require any mention of independent examination on the balance sheet.

Charities with subsidiaries: group accounts

In cases where a charity owns a **trading subsidiary** company (see chapters 8 and 10) or if one charity is a subsidiary of another, there may be a legal requirement to prepare **group accounts**. This means the accounts of the charity and its subsidiary are taken together and presented in one set of accounts. Currently, group accounts are compulsory when a charity and its subsidiary have **aggregate gross income** of over £1 million in England and Wales or over £500,000 in Scotland or Northern Ireland. Aggregate income is the income of the charity plus the income of the subsidiary less the income received by the charity from the subsidiary, which avoids any double counting of income.

Note that group accounting is not applicable with R&P accounts. However, if you are a small charity with an annual income that meets the R&P threshold and you also have a subsidiary, you should check whether the aggregate income level is met; if so, accruals accounts will be needed to account for the group.

For a charity with a subsidiary, in the accounts of the charity only, the SOFA will include a single line under 'income and endowments' for the profits donated to the charity by the subsidiary. Where group accounts are needed – technically termed 'consolidated accounts' – the group SOFA and balance sheet needs to show the combined income, expenditure, assets and liability of the charity and the subsidiary. However, '**consolidation** adjustments' may be required when you are bringing the figures together to ensure nothing is counted twice.

The thresholds for group accounts are the same as the charity audit thresholds (see page 283) – but they are based on the income of the charity and subsidiary taken together. Any charity preparing group accounts will be subject to an audit, even if the income of the parent charity is well below the audit threshold as a stand-alone entity.

The details of group accounts and consolidation are beyond the scope of this book. The SORP has information in section 24, and your auditors will probably be your first source of advice.

This chapter has set out the main requirements that, as the treasurer or finance officer, you need to take into account when preparing charity accounts on an accruals basis. As has been highlighted, there can be many technical accounting issues to navigate to ensure that your accounts are compliant with the Charities SORP. If you do prepare your accounts on this basis, you may find the services of an auditor or independent examiner with good charity accounting experience invaluable. Chapter 15 looks at the concept of external scrutiny in more detail.

15 Audit and independent examination

Trustees are responsible for preparing the **annual report and accounts** for their **charity** to provide supporters, **funders** and others with assurance that the charity's resources have been managed appropriately. Except in the smallest charities in England and Wales, once the accounts are complete, there is a further legal requirement that they are scrutinised from an independent perspective. Many people use the term **audit** to describe this process. In fact, that can be a misleading term to use as the vast majority of charities in the UK will not be subject to a full audit. As the **treasurer** or **finance officer**, it is likely you will take the lead in driving the audit or **independent examination** process.

This chapter considers the legal requirements and important thresholds that trustees need to be aware of in determining the level of scrutiny needed for their charity's accounts. It looks at the factors that trustees should consider in appointing an **auditor** or **independent examiner**, what you can expect their work to involve and the report they produce. It next outlines what you need to be aware of concerning sharing your accounts with others. Finally, it explores auditors' and independent examiners' statutory duty to report serious concerns to the **charity regulators**.

Scrutiny requirements

An independent report on the accounts of a charity is vital protection for all concerned. For funders and **donors**, it provides assurance that the resources they have given to the charity have been managed appropriately. For the trustees, it is an added financial control to demonstrate that the **transactions** of the charity are accounted for, providing confidence in the overall position of the charity. That being said, it must be noted that neither an audit nor an independent examination is designed specifically to find or prevent fraud – that responsibility remains with the trustees.

There are two possible forms of independent scrutiny of the accounts of a charity that apply throughout the UK: audit and independent examination.

An audit is generally more demanding and more costly and is only required for large charities. For the vast majority of small to medium-sized charities, an independent examination will be the appropriate form of scrutiny.

There are some differences to be aware of in the thresholds and requirements between the three UK **jurisdictions**. If your charity is registered in more than one jurisdiction, you will need to adhere to the strictest rules. These scrutiny rules are almost identical for all legal forms of charity, whether an **unincorporated** association, a **CIO** or **SCIO**, a trust or a **charitable company**. However, different rules apply to **exempt charities** in England and Wales (for example, academy schools); these organisations are generally subject to separate requirements and are not considered in this book. Charitable community benefit societies are subject to an independent examination or audit but the thresholds (which are not covered in this book) differ and are set by the Financial Conduct Authority (the regulator of **CBSs**) (see the useful addresses on page 319).

Although people often refer to 'having the accounts audited' for either form of scrutiny, as the treasurer or finance officer, it is important for you to be aware of the distinction and use the correct term. The two forms of scrutiny are very different in terms of who can carry them out, what the work involves and the assurance that the report gives. The Charities Acts across the UK make clear distinction between the two terms, acknowledging that independent examination is designed as an alternative to a full audit for smaller charities.

The rules are mainly based on the organisation's total income for the current year (which means the income reported in the accounts that are subject to scrutiny – although guidance from the charity regulators allows new receipts into **endowment funds** to be excluded from the total). Table 12.3 (see page 228) sets out the income thresholds for the three jurisdictions. As a summary, charities that must have an audit are as follows:

- England and Wales – charities with an annual income of over £1 million;
- Northern Ireland – charities with an annual income of over £500,000;
- Scotland – charities with an annual income of £500,000 or more;
- any charity where a full audit is required in its **governing document**;
- any charity where a funder, umbrella body or similar third party requires a full audit.

For charities with **assets** over £3.26 million (perhaps in buildings or **investments**), the income level for an audit is reduced to £250,000 both in England and Wales and in Scotland, but no similar requirement exists in Northern Ireland.

All other charities can opt to have an independent examination rather than an audit. And in England and Wales, very small charities with an annual income under £25,000 are not required to have any form of independent scrutiny so long as their accounts have been properly approved by the trustees (there is no lower limit in Scotland or Northern Ireland).

It must be stressed that the thresholds are minimum requirements in law, and some charities may want or need more than the minimum, such as on the request of a funder. In saying that, if a funder does ask for audited accounts (for example, as part of a funding application or your report on how funding has been spent), you should check whether they really mean 'audited' or whether an independent examination would be sufficient. As previously noted, often the terms are unintentionally interchanged. Certainly, when you are applying for funding, independently examined accounts should be sufficient for most funders – even those in the public sector.

Approval of accounts by trustees only

As mentioned, the very smallest charities in England and Wales, where annual income is under £25,000, generally do not require any form of independent scrutiny. This is intended to keep things simple for small local voluntary groups and any charity with a modest income. This includes CIOs and charitable companies. **Trustees' annual reports** and accounts are still required, and the trustees must approve them.

There must be a formal trustee meeting at which the accounts are approved. If you are the treasurer, you may have prepared the accounts yourself (a very small charity is unlikely to have a finance officer, but if one exists they may also have had a major role in preparing the accounts). However, it is unwise for the remainder of the trustees to simply approve them on your say-so. When no one is checking your work, it is very easy to make a mistake that would then not get picked up – for example, addition errors, mistyping a figure or omitting transactions. There should be at least one other trustee, not involved in the day-to-day **bookkeeping**, who does a detailed check from the accounts back to the **accounting records**. If they consider the accounts are correct, they can recommend their approval to the rest of the trustees (see page 238).

With an annual income level below £25,000, most charities will choose to do **R&P accounting**, although bear in mind that a charitable company will still need to prepare **accruals accounts** in line with the Charities SORP and Companies Act 2006 requirements. The accounts will need a declaration that the company has dispensed with the audit requirement (see page 280).

Although they do not need external scrutiny, the accounts must be sent to CCEW on request, and to anyone else who requests a copy: the accounts of any charity are a public document. Indeed, CIOs are always required to submit their accounts to CCEW even if their annual income is under £25,000, and charitable companies are always required to file their accounts with Companies House.

For charities registered in Scotland or Northern Ireland, the accounts must at least have an independent examination no matter how small the income.

Independent examination

The independent examination regime is intended to provide a certain level of consistency to the scrutiny of small charities' accounts. As the treasurer or a finance officer acting on behalf of the trustees, it is important to be clear about what you should expect from an independent examination. It should not be thought of as just another layer of red tape that has to be completed quickly before the accounts are due to be filed, and it is not enough to simply have someone look over the accounts and sign their name at the bottom.

As mentioned, charities with an annual income of up to £1 million in England and Wales, or of up to £500,000 in Scotland or Northern Ireland, can have an independent examination. This is a significant proportion of all UK charities. Therefore, the idea of the regime is to provide proportionate scrutiny which will give assurance to the users of accounts, but without requiring small charities to spend significant amounts of their funds and time on a costly audit. There are two main differences between the audit and independent examination regimes: who can act as an independent examiner and the nature of the report attached to the accounts.

A wide range of people can be independent examiners. In some cases, they must be professionally qualified (as set out on page 290), but in other cases a lay examiner may be sufficient.

There are some differences between the independent examination requirements in each jurisdiction, although the overarching aims of the regimes are the same. In England and Wales, the duties are laid down by section 145 of the Charities Act 2011, by the Charities (Accounts and Reports) Regulations 2008, and by CCEW's publication *Independent Examination of Charity Accounts: Directions and guidance for examiners (CC32)*. In Northern Ireland, similar duties are laid down in section 65 of the Charities Act (Northern Ireland) 2008, and *Independent Examination of Charity Accounts: Examiner's guide* (ARR07) sets out directions by CCNI. There are slightly different rules in Scotland under the Charities Accounts (Scotland) Regulations 2006, but the principles are similar. OSCR also has published guidance – *Independent Examination: A guide for independent examiners* – which, although not legally binding, provides a helpful framework.

Although the directions and guidance from the regulators are primarily aimed at independent examiners, as the treasurer or finance officer, you may find it useful to familiarise yourself with what a good independent examination should look like.

An independent examiner's goal is to provide a report that gives negative assurance. This is completely different from an audit report, which, at least with accruals accounts, aims to report on whether the accounts give a **true and fair view** of the state of affairs of the charity (see chapter 14, especially page 259, for more on the phrase 'true and fair'). To be able to provide negative assurance the independent examiner needs to be confident that no **material** matters have come to their attention giving them cause to believe that any one or more of the following applies:

- proper accounting records were not kept;
- the accounts do not accord with those records;
- the accounts do not comply with requirements of the relevant Charities Act;
- there is further information needed for a proper understanding of the accounts.

If the examiner is happy, the report says that no concerns were identified (using standard wording which cover the four points – see figure 15.1). This is called an **unqualified report**, as the examiner is not making any reservations or qualifications regarding the accounts.

However, there are times when this is not the case. There could be missing accounting records, **restricted funds** may not have been managed appropriately, or the charity may be very late in filing its accounts or unwilling to present its accounts in the required manner. The independent examiner must express these concerns in their independent examination report. This is called a **qualified report**.

Independent examiner's report to the trustees of Midshire Youth Project CIO

I report to the trustees on my examination of the accounts of Midshire Youth Project CIO (the Charity) for the year ended 31 March 2024.

Responsibilities and basis of report

As the trustees of the Charity you are responsible for the preparation of the accounts in accordance with the requirements of the Charities Act 2011 ('the Act').

I report in respect of my examination of the Charity's accounts carried out under section 145 of the 2011 Act and in carrying out my examination I have followed all the applicable Directions given by the Charity Commission under section 145(5)(b) of the Act.

Independent examiner's statement

I have completed my examination. I confirm that no material matters have come to my attention in connection with the examination giving me cause to believe that in any material respect:

1. accounting records were not kept in respect of the Charity as required by section 130 of the Act; or
2. the accounts do not accord with those records.

I have no concerns and have come across no other matters in connection with the examination to which attention should be drawn in this report in order to enable a proper understanding of the accounts to be reached.

Signed:

Name:

Relevant professional qualification or membership
of professional bodies (if any):

Address:

Date:

Note: This is an example of an unqualified independent examination report for a non-company charity registered in England and Wales with an income for the year under £250,000 and preparing R&P accounts. The wording will be different in other scenarios – for example, if the accounts were on an accruals basis or the charity was registered in Scotland – to comply with the prevailing legislation.

Fig. 15.1 An example of an independent examination report that could accompany the R&P accounts featured in figures 13.2, 13.4 and 13.6

In some cases the qualification can be relatively minor, such as if the accounts are being submitted late to the regulator because of an administrative oversight. This may not cause a charity too many concerns as long as the trustees address the issues raised and are seen to be acting on any recommendations to improve processes and controls. But a more serious qualified wording can mean the charity is in real trouble – for example, it may not be managing its restricted funds correctly and therefore be in breach of trust, or it may be making unauthorised payments to the trustees. Many funders are cautious about awarding funding to a charity where the auditor or examiner issues a qualified report, whatever the issue. A qualified report will also mean an independent examiner is required to raise any matters of material concern with the relevant charity regulator (see page 297).

There can be misunderstandings over this terminology, with some trustees thinking a clean report with no issues is 'qualified', perhaps confusing the term with the notion of a professionally qualified independent examiner. But a qualified report is very different – as explained, it means the examiner has concerns. Even a lay examiner will need to issue a qualified report where issues have arisen in the examination which need to be highlighted to those reading the accounts. Take care during the annual return process with the appropriate regulator (see chapter 12) that you only mark your accounts as qualified if the auditor or examiner included a qualified wording in their report. Many small charities have affected their reputation with funders by filing accounts flagged as qualified when in fact the examiner gave an unqualified report.

To reach an opinion on the accounts, the independent examiner must carry out a significant amount of work; it is not simply a case of checking that the numbers add up or the balances agree with the bank statements. The directions from CCEW set out 13 stages to follow (and the other regulators have similar provisions). These include checks to ensure that the charity is eligible to have an independent examination, that the examiner is appropriately qualified where this is required, and that there is no conflict of interest between the examiner and the charity or its trustees. The examiner must also gain a good understanding of the charity and of the controls and processes in place, and check that the accounting records are held properly. They also carry out work to ensure the figures in the accounts themselves are consistent with the accounting records, and that any **accounting policies**, estimates and judgements are appropriate (in the case of accounts on the accruals basis). The examiner will need to enquire about any restricted funds, transactions with related parties and trustees, and your charity's financial outlook.

You can expect your examiner to need access to all your accounting records for the year, including any minutes of trustee meetings, and to ask questions to check their understanding. Once their review is complete, they will be able to prepare a report for the accounts. There are standard templates available from all regulators (see figure 15.1 for an example). They set out the responsibilities of both the examiner and the trustees, refer to the relevant legislation and provide the examiner's conclusion on the negative assurance statements noted previously.

For most small charities, the independent examination can provide effective scrutiny, and often the examiner will make recommendations on how processes can be improved going forward. Sometimes this is given informally, but at other times an examiner will issue a formal report to the trustees with their findings, often called a 'management letter' or 'post-independent examination report'. This can be a very important and valuable document for the trustees, explaining how they can improve their financial **governance** of the charity.

Selecting an independent examiner

It is the responsibility of the trustees to appoint an independent examiner who is appropriate for the charity. Independent examiners come from a wide range of backgrounds; they do not necessarily have to be a qualified accountant or have a financial background. Some will work professionally as independent examiners to numerous charities and will probably charge a fee (however, this is usually considerably less than the fee for an audit). Other independent examiners may work on a voluntary basis or charge a nominal fee, perhaps only working with a few charities.

An independent examiner is defined in the Charities Act 2011 (section 145) as 'an independent person who is reasonably believed by the charity trustees to have the requisite ability and practical experience to carry out a competent examination of the accounts' (this definition applies throughout the UK). There are two important parts to this definition: 'independent' and 'requisite ability and practical experience'.

The issue of independence is crucial to external scrutiny. Both the independent examiner and the trustees have to be confident that the examiner is independent. This means that the independent examiner should not be related to any of the trustees or have a business relationship with them. The examiner should not be involved in the running of the charity or be a material donor or beneficiary. The examiner could, however, be a member of the wider membership. For example, a member of a church congregation could act as the independent examiner for the church as long as they had no involvement in the management of the church's affairs. The independent examiner must always be an individual. Where a firm of accountants carries out the examination, the report must always come from one named person.

Requisite ability and practical experience may be more difficult for trustees to judge. The person must have a good understanding of charity accounts and be aware of the relevant regulations and, if the accounts are on the accruals basis, the SORP. The expertise required to examine R&P accounts may not be as technical as that for accruals accounts, but the examiner still needs to appreciate the specific requirements of charity accounts on the R&P basis, including concepts such as restricted funds and the various statements that are needed in a set of R&P accounts. Even among accountants, only a few firms specialise in charities, and others may not be fully aware of all the requirements.

In England and Wales and in Northern Ireland, where the annual income of the charity is under £250,000, the trustees are able to appoint an examiner of the charity's choice (see table 12.3, on page 228). This is someone that they know to be independent and have the requisite ability and practical experience to carry out the work. No professional qualification is needed, but the trustees should be confident the person chosen has the knowledge to carry out a competent examination. These people are sometimes referred to as 'ordinary' or 'lay' examiners.

In Scotland, trustees can appoint an examiner of the charity's choice only when the charity's annual income is under £250,000 and the accounts are prepared on the R&P basis. For any accounts prepared on the accruals basis, the examiner has to be professionally qualified.

In all jurisdictions, where the charity's annual income is over £250,000, the independent examiner must be professionally qualified. Ability and experience still apply; there is no point appointing a professional accountant, who will likely charge fees, if they have no knowledge of charity accounts or of the independent examination requirements. Even where a charity's annual income is over £100,000, the regulators advise appointing a professionally qualified rather than a lay examiner.

A professionally qualified examiner is one who holds one of a number of qualifications. These are listed in the relevant Charities Act. To be eligible, the person must be a qualified member of one of the following bodies:

- Institute of Chartered Accountants in England and Wales (ICAEW);
- Institute of Chartered Accountants of Scotland (ICAS);

- Chartered Accountants Ireland;
- Association of Chartered Certified Accountants (ACCA);
- Association of Authorised Public Accountants (AAPA);
- Association of Accounting Technicians (AAT);
- Association of International Accountants (AIA);
- Chartered Institute of Management Accountants (CIMA);
- ICSA: The Governance Institute (ICSA);
- Chartered Institute of Public Finance and Accountancy (CIPFA);
- Association of Charity Independent Examiners (ACIE);*
- Institute of Financial Accountants (IFA);**
- Certified Public Accountants Association (CPAA).**

ACIE was established specifically to provide advice, training and qualifications for independent examiners. For a charity looking to find an experienced independent examiner, ACIE can provide lists of full members (for contact details see the useful addresses, on page 319). Presently, no other professional accountancy body provides lists of accountants who carry out independent examinations, although the ICAEW lists members who hold the organisation's Diploma in Charity Accounting qualification, and some bodies do have a list of members on their websites. You might also find an examiner to approach through **third sector** advice organisations, word of mouth, visiting your local high street accountant, searching online and recommendations from other local charities.

If, as the treasurer or finance officer, you are looking to appoint an independent examiner, you may want to review their website (if applicable), interview potential candidates, and confirm their qualifications and experience. Good independent examiners will be happy to provide examples of their work and references. Even if your charity's accounts are simple enough that the trustees are happy to use a lay examiner, there still needs to be a proper discussion as to the examiner's experience and familiarity with the directions or guidance on independent examinations issued by the relevant charity regulator.

---

* The rules of ACIE specify that to carry out an independent examination of a charity with an annual income over £250,000, the member must be a fellow (FCIE); however, an associate member can carry out examinations of charities with an annual income below £250,000 where a professionally qualified accountant is required. Affiliate members of ACIE can only act as lay examiners.

** Members of these bodies are not yet authorised to act as professional independent examiners for Scottish charities, but they may act in England and Wales and in Northern Ireland.

Note that it is not the treasurer or finance officer who appoints the independent examiner; it is the trustees as a whole who must agree and make the appointment. And in some cases, the trustees can only propose an appointment which is put to members to approve as part of the AGM business. You should check your governing document to confirm what process your charity must follow.

Trustees should not expect the independent examination to be free, although (as mentioned) there are many voluntary independent examiners who mostly act for smaller charities and do not charge a fee. An independent examination of a larger charity is a demanding process which will take a good deal of time. Professional examiners will probably have to hold a practising certificate, undertake continuing training, have appropriate insurance in place and issue engagement letters. They also have to carry out anti-money-laundering checks at the start of the process. This means, as with any other professional accounting service, they will charge a fee to cover the work they are carrying out. As when you are taking on any professional service for your charity, the trustees can approach several examiners for a quote and compare the options open to them before making a decision.

Audit

For larger charities, with an annual income of more than £1 million in England and Wales, or more than £500,000 in Scotland or Northern Ireland (or over £250,000 if the assets are valued at over £3.26 million), the accounts must be subject to a full audit (see table 12.3, on page 228). An audit can only be carried out by a registered auditor, generally a firm of accountants. Registered auditors must meet specific criteria and are subject to extensive professional monitoring. There are some auditors that have whole departments specialising in charity accounts.

An audit is much more involved than an independent examination and will follow specific auditing standards which are developed by the Financial Reporting Council and are UK-wide. Essentially, an audit involves three main stages. Initially the auditor will conduct a substantial **risk** assessment to build up a picture of your charity. This will probably involve speaking to people within the charity – not necessarily just the treasurer or finance officer, but those responsible for other areas, such as IT or HR – and reviewing the finance systems and policies in place. This will allow them to obtain a detailed understanding of your charity and its processes and financial controls, and to assess where there could be a risk of inaccuracies in the **financial statements**. For example, if your charity does not have good controls over managing its restricted funds, the auditor will need to do more work in that area, to check that the funds have been accounted for correctly. In general, the greater the risk the auditor identifies, the more evidence they will need to see to satisfy their requirements.

The second stage of the audit is gathering evidence. This may involve looking at invoices to substantiate purchases that a charity has made or reviewing paperwork to check a **grant** is accounted for correctly. They may also need to follow some of the transactions in the year through the systems and controls your charity operates to ensure they are working as intended. For example, if an invoice over £500 should be approved by two trustees, they will need to see evidence that this is happening. In some cases, obtaining the evidence may require discussion with charity staff or trustees, perhaps even challenging them on some decisions that have been made and obtaining evidence to corroborate explanations, not simply taking things at face value.

Once the auditor has satisfied themselves that they have enough evidence to ensure the risk of inaccuracies in the accounts is low – for example, by determining that it is highly unlikely that a transaction has been missed or recorded incorrectly – they embark on the final stage of the audit, which is the audit report. As a result of the substantial work carried out during an audit, the report gives much more assurance than an independent examiner's report. It should be noted that it is likely that more than one person will be involved from the audit firm, and you will probably be assigned an audit partner (who will sign the audit report, but you may not see them), an audit manager (who you will probably have more involvement with) and junior staff (who will carry out most of the work). This is all dependent on the size of your charity and the audit firm. Nevertheless, an audit is usually much more costly than an independent examination.

Usually, an audit will be carried out on accruals accounts, and the auditor's opinion will be that the accounts give a 'true and fair' view of the charity's position. In contrast, if R&P accounts are audited, the auditor declares that they are 'properly presented'. As with an independent examiner, an auditor can issue a qualified report where necessary (see page 286) – for example, where there are doubts about certain figures or where the auditor considers that the accounts do not comply with methods and principles in the SORP.

Dispensation from audit

If your charity normally has an independent examination but, unusually, crosses the audit threshold in a particular year, you may be able to apply for an exemption from audit. For charities in England and Wales, if a one-off blip takes a charity over the £1 million audit threshold (for example, as a result of the sale of a building, a one-off unexpected legacy or a transfer of funds from a former charity), the trustees can apply to CCEW to have an independent examination rather than an audit. This is achieved by applying through CCEW's general enquiry form (https://forms.charitycommission.gov.uk/enquiry-form) and selecting the option to apply for an exemption from audit. You should ensure this is done as soon as you know the threshold has been (or will be) breached to ensure CCEW has time to consider your case and ensure the circumstances are exceptional. CCNI has similar powers, but there is no equivalent power for OSCR, meaning that whenever the £500,000 annual income threshold is exceeded, an audit will always be required for charities in Scotland.

Selecting an auditor

As noted above, if you require an auditor, you will have to look for a registered audit firm. It is a good idea to find a firm that is appropriate for your size of organisation but which also has reasonable experience with charities and voluntary organisations.

All UK-registered auditors will be regulated by one of the first four bodies in the list on page 291 (ICAEW, ICAS, Chartered Accountants Ireland or ACCA). You can search their websites for a list of registered audit firms (see the useful addresses, on page 319), but often it is better to ask for recommendations from other local charities. You could even identify accountancy firms on your local high street or business park to ask if they carry out charity audits.

It is a good idea to approach two or three firms and ask for quotes. But if you do this, you will need to be clear about what you need, what information you will supply and the timescales involved, as well as being realistic about when you can have the information ready. Audit firms tend to work to tight deadlines. Remember that the fees quoted may not be the only factor to consider in selecting an auditor. You may want to check whether the audit firm has similar clients to your charity and understands the complex charity accounting rules. As with appointing an independent examiner, it is perfectly acceptable to ask for references or for examples of charities they work with or accounts they have audited. Audit fees can be substantial due to the work involved, but some firms do have lower rates for charities. However, the audit of a charity is typically much more work than the audit of a commercial business of a similar size, due to the complexities of the SORP and **fund accounting**. In fact, most non-charitable companies are nowadays exempt from the audit requirement unless their turnover is over £10.2 million, so those firms of accountants that continue to provide audit services below this level will often be paying significant fees to maintain their audit registration specifically because of their charity audit work.

Issuing your accounts to others

Whenever you are asked to send a copy of your accounts (for example, with a funding application), you must always provide:

- the annual report (signed by the trustees);
- the scrutiny report on the accounts (signed by the auditor or independent examiner);
- the **annual accounts** (signed by the trustees).

You should never send accounts to anyone without all three elements being present, because, under charity law, all three must be present in a compliant set of charity accounts (under both the R&P regime and the SORP). If a funding application asks for accounts and you only have one part ready, you should send the prior year's accounts and explain that the current year's are in the process of being prepared. Many funders will, quite rightly, reject unsigned accounts or accounts without the independent report, because legally they are no more than draft documents.

The requirements for signing the accounts and reports had to change during the COVID-19 pandemic as a result of the restrictions on movement. All regulators started to accept electronic signatures. At present, unless your charity's governing document specifies otherwise, handwritten – or 'wet' – signatures are not required. Electronic signatures can be used instead, and this includes a typed signature or an electronic version of a handwritten signature. This may be subject to change, and it is best practice to have a signed (not typed) copy for your own records. As noted in chapter 12, charity accounts to be filed with Companies House must also be sent as a paper signed version (but the signature can also be an electronic version).

In all cases, the final accounts must always show the date of approval by the trustees and the name(s) of the specific trustees who signed. It would be a very serious fraud for a treasurer or finance officer to type in trustees' signatures before the trustees had formally approved the report and accounts. Likewise, if the independent examiner is willing to allow their signature to be typed in, this must only happen once the examiner has given formal approval of their report (which must always come after the approval by the trustees).

In the past, trustees would arrange for several copies of hand-signed accounts to be prepared, so that copies were available to send to the regulators and any funders, and to be copied for anyone who requested them. Now, accounts are nearly always shared electronically, and it is very rare to have more than one hand-signed copy of accounts. In fact, as charities move towards paperless working, sometimes only electronic copies of accounts are retained. With concerns over identity theft, some trustees and examiners prefer to issue accounts for circulation with printed signatures rather than copies of the actual signatures.

Reporting matters of material significance

Auditors and independent examiners have a statutory duty to report any matters of material significance to the relevant regulator. The requirement is the same across all UK jurisdictions. A matter of material significance can be thought of as something that the trustees have done, something they have not done, or an instance where they have not taken sufficient action to prevent something happening, where this has or could adversely affect the charity in some way. It could even be something in the accounts that is not very well disclosed so that the reader may not understand its meaning or that it could be ambiguous in meaning. The regulators specify that something can have 'material significance' not only in a financial respect but also as something that the regulators may need to investigate, or which could impact the charitable status of the organisation (refer to *Matters of Material Significance Reportable to UK Charity Regulators*, listed in the further reading, on page 313).

Consequently, matters of material significance are wide-ranging. They include situations where financial crimes have been committed, such as money laundering, dishonesty and fraud (either externally or internally); breaches of law; and instances where harm has been caused to beneficiaries from a lack of appropriate safeguarding. But they arise too where trustees have failed to carry out their duties effectively – for example, if trustees have not implemented, or regularly override, internal controls, or do not follow procedures to properly manage restricted funds or declare conflicts of interest. Examiners may have concerns if trustees refuse to report transactions with **connected persons** of trustees (see page 25) or payments to trustees sufficiently in the accounts. And, in fact, for any reason that an examiner needs to qualify the accounts, there is an obligation on them to raise a matter of material significance with the regulator.

The auditor or examiner is not expected to carry out additional work to find matters to report, and often the matter will have been raised by the trustees (as is their duty) with the regulator already. However, even if a matter has been raised, this does not relieve the examiner of the duty to report it, as they may be able to provide the regulator with more complete and balanced information. If the trustees subsequently address the issue, the examiner can report on the actions taken. As the treasurer or finance officer acting on behalf of the trustees, in your dealings with your auditor or examiner, you will be expected to disclose any matter reported to the regulator (such as **serious incidents** – see page 23).

It is not necessarily a complete disaster for a charity to have dealings with a regulator. In most cases, the regulator will want to take action to support the trustees in improving the charity's practices.

This chapter has explained the duties that the trustees have in making sure that the annual accounts of their charity are appropriately scrutinised, and how, in your role as treasurer or finance officer, you may be required to guide the trustees throughout the scrutiny process. You should not see an independent examination or audit of your charity's annual accounts only as meeting a compliance requirement. It is a chance to ensure your charity is operating with good financial controls and procedures and that the trustees are governing the charity effectively. Most examiners and auditors will be happy for you to contact them throughout the year with questions, and they can be a very good source of knowledge about those tricky accounting issues you may experience.

◆ ◆ ◆

With this book, we have aimed to provide a comprehensive introduction to managing a charity's finances effectively and responsibly. Even in the smallest of charities, being a treasurer is not simply about keeping a record of the money received and spent. We have looked at various topics you may encounter in your role as a treasurer or finance officer, such as the technical aspects of fund accounting, charity taxation and annual reporting, and the broader concepts of risk, financial controls and fundraising. Charity finance continues to evolve, and in some cases you will need to refer to further sources or seek professional advice, but we hope this book gives you the foundation to guide and support your charity in its vital work.

Additional notes

This section provides an overview of the actions involved in running a charity that you will need to be aware of in your role as a treasurer or finance officer. Its aim is to act as a guide and point you to the relevant chapters in the book for further details. It considers what is involved in:

1. setting up a charity;
2. setting up a charity bank account;
3. registering with HMRC;
4. managing a charity.

Setting up a charity

This book does not provide a step-by-step guide to setting up a charity, as that will differ depending on individual circumstances. However, if you are looking to set up a new charity, the main considerations are:

- Is setting up a charity the best option – does another charity already exist which could carry out the work you want to achieve?
- What will your charitable purposes be?
- How will you demonstrate that you provide a public benefit?
- Where will the charity be registered and, therefore, which regulations and charity regulator will apply?
- What legal form will your charity take?
- Who will be the founding trustees?

Chapter 1 provides a summary of the information that will help you to answer these questions.

Applying for charitable status

If your answers to the above questions lead you to apply for charitable status, you will need to do the following:

- decide what your charitable purposes will be and what activities your charity will aim to carry out to achieve those purposes for public benefit;
- choose an appropriate governing document that fits the legal form of your charity and sets out how the organisation will be run;
- include trustee eligibility declarations for the founding trustees (the format of these forms differs for each jurisdiction);
- fully understand your duties as a trustee;

- with the above information, complete an online application for charitable status with the relevant regulator.

Do not underestimate the work and time involved in applying for charitable status. Each regulator has a website with detailed guidance on applying for charitable status and an online application process. The further reading (see page 313) and useful addresses (see page 319) sections of this book list other organisations that provide helpful information. It is also possible to take on the services of an adviser or consultant who is experienced in helping to set up charities, but this will usually be at a cost. Where a CIO or SCIO legal form is appropriate, Gareth G. Morgan's book *Charitable Incorporated Organisations*, also published in this series, is a thorough guide.

Once charitable status is granted, there are some actions to be taken:

- Set up a bank account in the name of the charity (see next section).
- Register with HMRC to recognise the organisation as a charity for tax purposes (see page 302).
- Take out any insurance needed for the charity.
- Register with any other organisations and regulatory bodies as required.
- Seek to appoint new trustees as needed.
- In the case of a charity with members, establish the register of members and make arrangements for new members to join.

Alternatively, if the organisation was already in existence before it received charitable status, the above may already be in place and only need to be updated.

Note that a CIO or SCIO does not exist until it has been registered with the relevant regulator, so a bank account cannot be opened until the charity is registered.

Chapters 1 and 2 provide further information that will be helpful in the early stages of setting up a charity.

Setting up a charity bank account

The procedure to open a bank account for a charity tends to be quite lengthy and requires a significant amount of information to be submitted to the bank. The exact requirements will likely differ between financial institutions, but the following is a general overview of the process:

1. Identify a bank that meets the needs of your charity – if you will be paying in cash regularly from fundraising events, you may want to have a local high street branch or alternative means of making cash deposits available, and this may influence your choice of bank. If having a local branch isn't important to you, you may want to bank with one of the

other major banks, which generally have charity-focused accounts available, or a more charity-specific banking institution, such as the CAF Bank, Reliance Bank or Unity Trust Bank. Online comparison sites and searches may be useful.

2 The account will need to meet your needs in terms of the charity's expected income level. Some banks provide free banking for charities with annual incomes under £50,000 or £100,000; however, for incomes over this level, a normal business account, with charges, may be required. Note that some banks charge for non-online banking transactions, so paying in cash and cheques will incur a fee.

3 In most cases, it will be simplest to opt for a current account that can be managed with online banking – but not all banks allow this to be combined with dual authorisation (see next point).

4 The account will need to allow authorisation of payments. This includes a cheque book requiring at least two signatories and, more usually now, an authorisation process for online payments. Some banks do not offer this facility, so it is worth having this confirmed before applying. The dual-authorisation procedure will work differently with each bank, but it usually follows the principle that one authorised signatory can set up the payment and a second will need to log into the account and authorise it.

5 Some applications for opening an account can be started online, and some will need a phone call first from one of the trustees (but see point 6 regarding additional documents).

6 All current trustees at the time of opening the account must normally be entered on the bank mandate and you may find all are required to sign it. In some cases, every trustee has to provide identification documents. This can be time-consuming if you have a significant number of trustees. However, some banks only need this information for the authorised signatories, which makes the process easier.

7 The trustees will need to decide who the authorised signatories are. This does not need to be all trustees and can also include staff members. Each signatory will also need to complete the relevant parts of the application form and sign it.

8 The application form normally needs to be accompanied by the governing document for the charity and any other information the bank requests.

9 Some banks also require a letter from a solicitor or qualified accountant, independent of the charity, who can confirm the full names of the trustees in the bank application. Your independent examiner or auditor can fulfil this role if you have one appointed and they are a member of one of the recognised professional accountancy bodies (such as ICAEW, ICAS, ACCA or Chartered Accountants Ireland). The letter needs to be on their letterhead.

Once all paperwork has been submitted, there may be a delay for processing, but, eventually, documentation will come back to your charity. Individual bank signatories with online banking access will be contacted separately regarding other verification procedures to enable them to receive access to the account.

Registering with HMRC

A charity should be registered with HMRC for tax purposes as the recognition means it can register for Gift Aid (see chapter 10). You can register your charity as soon as it receives charitable status or at a later date. But, if you haven't registered with HMRC, it may be that your charity's first encounter with HMRC will be through taking on an employee (chapter 11) or needing to pay VAT or complete a corporation tax return (chapter 9).

Whichever way you first make contact with HMRC, you will create a Government Gateway ID. This is a 12-digit number that you can use to access the HMRC online services portal for your charity (www.gov.uk/log-in-register-hmrc-online-services). You will also create an accompanying password and recovery word and link these to an email address and mobile phone number. The Government Gateway ID must be linked to the HMRC online services account of your charity; it should not be the same one that you may have to deal with your personal taxes or a different charity or company. The ID shouldn't be shared with other trustees or staff (in a similar way that you shouldn't share bank account log-ins). Once you have one ID set up to access the HMRC online services account, you can provide access to additional users – perhaps a second trustee or staff member – with their own Government Gateway ID and set different access levels.

The process that follows describes, currently, how to obtain charity recognition with HMRC when this is your first contact with them.

Begin by visiting www.gov.uk/charity-recognition-hmrc.

Once you press the 'Start now' button, you will be taken through a series of questions to assess that your charity is eligible. You will then be asked to enter specific details about your charity, such as the main address and contact details, bank account, charity registration number with the relevant regulator, charitable purposes and governing document details.

During this process you will create the Government Gateway ID mentioned above. You will also receive a case reference number and will be required to post copies of some documents to HMRC. These include proof of registration with the relevant regulator (CCEW, OSCR or CCNI), your governing document, proof of bank account (such as a bank statement), and some evidence to show activities have been or will soon occur (perhaps fundraising activities or the delivery of a service).

Once HMRC has assessed this information, it will post a letter to your charity confirming recognition and providing your HMRC charity reference number, which should be entered on all correspondence with HMRC. This number will start with two letters or an X and will include up to five numbers.

At this point, if you use your Government Gateway ID to log in to your HMRC online services account, you should see the details for your charity and a section called 'Charities'. This is where you can make a claim for Gift Aid (see chapter 10).

When you access the HMRC online services account for your charity, you will be able to see all taxes that your charity has registered to manage online. Note that you must register for a tax before you can see it on this account. Once you have registered for a tax (employment, VAT or corporation tax), you can add it to your HMRC online services account by selecting the link 'Get online access to a tax, duty or scheme'. You will need to answer a series of questions and provide the relevant reference number before the tax is added. See chapter 9 for information on registering for VAT and chapter 11 for information on registering as an employer.

Managing a charity

Once you have established a charity, or if you have taken on a role in an existing charity, you will have certain ongoing responsibilities. The following table sets these out, particularly as they relate to your role as a treasurer or finance officer.

You should	**Refer to chapter(s)**
Know the legal form of your charity, who the regulator is, have a copy of the constitution, and fully understand your charitable purposes and how your charity provides a public benefit.	1
Understand your role in the charity, what it involves and the interaction required with other trustees, staff and volunteers.	2

You should	Refer to chapter(s)
Know the important reference dates for the charity, for example: • the year-end date; • when accounts must be filed (with the regulator and, if applicable, Companies House); • when the annual return is due to the regulator; • when the annual confirmation statement is due to Companies House, if applicable.	2, 12
Understand your responsibilities for annual reporting to the regulator (and that they may not be the same each year), including: • which type of annual accounts are required based on your legal form and income level, and what accounting regulations apply; • what is required in the trustees' annual report; • what level of scrutiny those accounts need, how and when to appoint an auditor or independent examiner, and who that person should be; • what other annual return is needed.	12–15
Understand the tax status and requirements for your charity and know that this should be under constant review – especially where trading activities are involved. New activities, fundraising methods and changes in income level can affect the VAT and corporation tax status of a charity. If you are required to complete tax returns, know the filing dates, methods and payment dates.	8–9
Understand the key concept of fund accounting and how this applies in your charity.	3
Maintain good financial records that properly record your charity's transactions, are accessible, and can be used to provide management and annual accounts.	4
Adopt relevant and robust policies and financial controls that reduce the risks that your charity may face. Risks and controls should be subject to ongoing monitoring.	5
Provide good ongoing financial management which forms the basis of the trustees' decision-making.	6
Know how the treasurer or finance officer and fundraising roles are interlinked, and how and when you should be involved. For example: • methods and types of fundraising and the costs involved; • budgets and costing for funding applications; • the implications (including taxes) of charity trading; • applying the Gift Aid scheme correctly.	7–10
Know your responsibilities for employing and paying staff, where applicable, including regarding reporting to HMRC, minimum wage legislation and auto-enrolment pension obligations.	11
Understand the implications of payments made to volunteers, including trustees.	2, 11

Although the list in this table is not exhaustive, it provides a summary of the common areas that a treasurer or finance officer may be involved with in their role at a charity. It is very easy, when you take on the role of treasurer or finance officer, to just carry on with the tasks that have been handed over by your predecessor. But it is useful to stand back and consider whether anything has been missed or if anything could be done better. These areas are covered in detail throughout this book as indicated.

Thresholds: minimum accounting requirements

The following tables provide a summary of the minimum accounting requirements in law for charities in each jurisdiction as at 9 August 2023. The details, including explanations of the terms used, are covered within this book, mainly in chapters 4, 12 and 15. Remember, where a charity is registered in more than one jurisdiction, the stricter requirements will always apply.

The tables for England and Wales and for Scotland generally split the information out according to whether the charity has over £3.26 million in assets (in Northern Ireland, this is not relevant because the asset condition does not apply). Where there is no difference between the requirements depending on asset levels, the columns are combined.

Minimum accounting requirements for charities subject to the law of England and Wales

Annual income of the charity	Minimum requirements where the charity has no more than £3.26 million in assets	Minimum requirements where the charity has over £3.26 million in assets
Any level of income	• Must keep proper accounting records and retain them for six years • Must produce an annual report and accounts (non-company charities with an income under £250,000 can choose the R&P or accruals basis) – no external scrutiny is required where annual income is less than £25,000 • Must provide accounts to CCEW if required and to members of the public on request • CIOs (which are all registered charities) must file annual report and accounts with CCEW, and complete an annual return • Charitable companies must file accounts, which will always be on the accruals basis and Charities SORP compliant, with Companies House	
Greater than £5,000	• Must apply to become a registered charity (unless exempt or excepted) • Where registered, must complete CCEW's annual return and ensure the information held is current (for income under £10,000, report income and spending only; there are additional questions where income is greater than £10,000)	

<table>
<tr><th>Annual income of the charity</th><th>Minimum requirements where the charity has no more than £3.26 million in assets</th><th>Minimum requirements where the charity has over £3.26 million in assets</th></tr>
<tr><td>Greater than £25,000</td><td colspan="2">• Accounts must be independently examined (although the examiner does not need to be professionally qualified)
• Trustees' annual report and accounts must be filed with CCEW
• Must complete an annual return with CCEW</td></tr>
<tr><td>Greater than £250,000</td><td>• Full accruals accounting required following the Charities SORP
• Presentation of accounts and report must comply with the Charities (Accounts and Reports) Regulations 2008 – including SOFA, balance sheet and notes – but simplified SOFA headings are permitted
• Independent examiner must be professionally qualified</td><td>• Full accruals accounting required following the Charities SORP
• Presentation of accounts and report must comply with the regulations – including SOFA, balance sheet and notes – but simplified SOFA headings are permitted
• Full audit required</td></tr>
<tr><td>Greater than £500,000</td><td>• Full Charities SORP compliance required, including the use of functional headings on the SOFA, inclusion of a statement of cash flows, and increased disclosures in the trustees' annual report
• Independent examiner must be professionally qualified</td><td>• Full Charities SORP compliance required, including the use of functional headings on the SOFA, inclusion of a statement of cash flows, and increased disclosures in the trustees' annual report
• Full audit required</td></tr>
<tr><td>Greater than £1 million</td><td colspan="2">• Full Charities SORP compliance required, including the use of functional headings on the SOFA and inclusion of a statement of cash flows
• Increased disclosures in the trustees' annual report as set out in the regulations
• Full audit required</td></tr>
</table>

Where following the Charities SORP is required, this table assumes the trustees have accepted CCEW's recommendation to apply a 'true and fair override' in order to use the Charities SORP (FRS 102) (even though the Charities (Accounts and Reports) Regulations 2008 still refer to the SORP 2005 – see page 271).

Minimum accounting requirements for charities registered in Scotland

Annual income of the charity	Minimum requirements where the charity has no more than £3.26 million in assets	Minimum requirements where the charity has over £3.26 million in assets
Any level of income	• Must apply to OSCR to be registered if making any claim to charitable status in Scotland • Must keep proper accounting records and retain them for six years • Must produce an annual report and accounts (non-company charities with an annual income of under £250,000 can choose the R&P or accruals basis using the Charities SORP) following the Charities Accounts (Scotland) Regulations 2006 (as amended) • Accounts must be independently examined; where using the R&P basis, the examiner does not need to be professionally qualified, but all accruals accounts must be examined by a professionally qualified independent examiner • Must submit accounts to OSCR and to members of the public on request • Must complete an annual return with OSCR (expected to be a legal requirement from 2023) • Charitable companies must file accounts, which will always be on the accruals basis and Charities SORP compliant, with Companies House	• Must apply to OSCR to be registered if making any claim to charitable status in Scotland • Must keep proper accounting records and retain them for six years • Must produce an annual report and accounts (non-company charities with an annual income of under £250,000 can choose the R&P or accruals basis using the Charities SORP) following the Charities Accounts (Scotland) Regulations 2006 (as amended) • Accounts must be independently examined; where using the R&P basis, the examiner does not need to be professionally qualified, but all accruals accounts must be examined by a professionally qualified independent examiner • Must submit accounts to OSCR and to members of the public on request • Must complete an annual return with OSCR (expected to be a legal requirement from 2023) • Charitable companies must file accounts, which will always be on the accruals basis and Charities SORP compliant, with Companies House
£250,000 or above	• Accruals accounting required following the Charities SORP • Presentation of the accounts and report must comply with the regulations – including SOFA, balance sheet and notes – but simplified SOFA headings are permitted • Independent examiner must be professionally qualified	• Full accruals accounting required following the Charities SORP • Presentation of the accounts and report must comply with the regulations – including SOFA, balance sheet and notes – but simplified SOFA headings are permitted • Full audit required
£500,000 or above	• Full Charities SORP compliance required, including use of functional headings on the SOFA and inclusion of a statement of cash flows • Increased disclosures required in the trustees' report, as outlined in the Charities SORP • Full audit required	• Full Charities SORP compliance required, including use of functional headings on the SOFA and inclusion of a statement of cash flows • Increased disclosures required in the trustees' report, as outlined in the Charities SORP • Full audit required

Minimum accounting requirements for charities registered in Northern Ireland

Annual income of the charity	Minimum requirements regardless of assets
All charities	• Must apply to CCNI to be registered;* however, existing charities can wait until called forward to apply • Must keep proper accounting records and retain them for six years • Must produce an annual report and accounts – non-company charities with an annual income of under £250,000 can choose the R&P or accruals basis using the Charities SORP, following the regulations • Accounts must be independently examined • Must submit accounts to CCNI and to members of the public on request • Must complete an annual return with CCNI • Charitable companies must file accounts, which will always be on the accruals basis and SORP compliant, with Companies House
Greater than £250,000	• Accruals accounting is required following the Charities SORP • Presentation of the accounts and report must comply with the Charities (Accounts and Reports) Regulations (Northern Ireland) 2015 – with the SOFA, balance sheet and notes – but simplified SOFA headings are permitted • Independent examiner must be professionally qualified
Greater than £500,000	• Full Charities SORP compliance required, including use of functional headings on the SOFA and inclusion of a statement of cash flows • Increased disclosures required in the trustees' report, as outlined in the Charities SORP • Full audit required

* It is possible that an exemption from charity registration will be introduced for charities in Northern Ireland with an annual income of up to £20,000 under powers in the Charities Act (Northern Ireland) 2022; however, there will be no lower registration limit for Northern Irish CIOs (the option of becoming a CIO is also due to be introduced).

References

[1] Charities Act 2011, s. 3(1).

[2] Analysis of charity registration data shows that two-thirds of charities registering in England and Wales and in Scotland are CIOs or SCIOs – see Gareth G. Morgan, *Charitable Incorporated Organisations*, 2nd edition, London, Directory of Social Change, 2018.

[3] For more information see ‘Excepted charities’ [web page], CCEW, 2014, www.gov.uk/government/publications/excepted-charities/excepted-charities--2, accessed 14 April 2023 and ‘Exempt Charities (CC23)’ [web page], CCEW, 2023, www.gov.uk/government/publications/exempt-charities-cc23/exempt-charities, accessed 11 July 2023.

[4] *Independent Review of Charity Regulation: Departmental Response* [PDF], Department for Communities, 2022, www.communities-ni.gov.uk/sites/default/files/publications/communities/independent-review-of-charity-regulation-ni-dept-response.pdf, accessed 14 April 2023.

[5] Charities Act 2011, s. 178; Charities and Trustee Investment (Scotland) Act 2005, s. 69; and Charities Act (Northern Ireland) 2008, s. 86.

[6] See detailed guidance at ‘Charity fundraising appeals: Using donations when you have not raised enough money or you cannot achieve your appeal purpose’ [web page], CCEW, 2022, www.gov.uk/government/publications/charity-fundraising-appeals-for-specific-purposes/charity-fundraising-appeals-using-donations-when-you-have-not-raised-enough-money-or-you-cannot-achieve-your-appeal-purpose, accessed 14 April 2023.

[7] Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102) [PDF], CCEW, OSCR and CCNI, 2019, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/870619/charities-sorp-frs102-2019a.pdf, Module 2, accessed 14 April 2023.

[8] Charities Act 2011, ss. 130–1; Charities and Trustee Investment (Scotland) Act 2005, s. 44; and Charities Act (Northern Ireland) 2008, s. 63.

[9] *Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland* (FRS 102) [PDF], CCEW, OSCR and CCNI, 2019, www.charitysorp.org/documents/496625/496655/charities-sorp-frs102-2019a.pdf, Module 2, accessed 14 April 2023.

[10] 'Code of Fundraising Practice' [web page], FR, www.fundraisingregulator.org.uk/code/all-fundraising/responsibilities-charitable-institutions, s. 2.3.1, accessed 14 April 2023.

[11] See Sam Jackson, 'Cryptocurrencies: what are they, and should charities use them?' [web article], CCEW, https://charitycommission.blog.gov.uk/2022/07/12/cryptocurrencies-what-are-they-and-should-charities-use-them, 12 July 2022.

[12] See 'Gift Aid claim template letter: Standard method' [web page], HMRC, www.gov.uk/government/publications/gift-aid-claim-template-letter-standard-method, accessed 14 April 2023; 'Charities: Detailed guidance notes on how the tax system operates' [web page], HMRC, www.gov.uk/government/publications/charities-detailed-guidance-notes, accessed 14 April 2023.

[13] 'UK Civil Society Almanac 2022' [web page], NCVO, 2022, www.ncvo.org.uk/news-and-insights/news-index/uk-civil-society-almanac-2022, accessed 14 April 2023.

Further reading

Publications from the Charity Commission for England and Wales

CCEW produces a wide range of guidance publications for charities. They are available from CCEW's website (some are available as PDFs which can be downloaded and printed, but some guidance is only available in the form of a web page). In almost all cases, the details apply to excepted charities in England and Wales as well as registered charities.

The following guidance is particularly relevant to treasurers and finance workers and is most quickly accessed using the link www.gov.uk/government/collections/list-of-charity-commission-cc-guidance-publications.

CC3 – *The Essential Trustee: What you need to know, what you need to do*
CC3a – *Charity Trustee: What's involved*
CC8 – *Internal Financial Controls For Charities*
CC11 – *Trustee Expenses and Payments*
CC12 – *Managing a Charity's Finances: Planning, managing difficulties and insolvency*
CC14 – *Charities and Investment Matters: A guide for trustees*
CC15d – *Charity Reporting and Accounting: The essentials*
CC16 – *Receipts and Payments Accounts Pack*
CC17 – *Accruals Accounts Pack (available for different legal structures)*
CC19 – *Charity Reserves: Building resilience*
CC20 – *Charity Fundraising: A guide to trustee duties*
CC26 – *Charities and Risk Management*
CC29 – *Conflicts of Interests: A guide for charity trustees*
CC31 – *Independent Examination of Charity Accounts: Guidance for trustees*
CC32 – *Independent Examination of Charity Accounts: Examiners*
CC35 – *Trustees, Trading and Tax: How charities may lawfully trade*

The specific guidance on public benefit (which trustees *must* consider by law) is available at www.gov.uk/government/collections/charitable-purposes-and-public-benefit. The revised guidance from 2013 comprises three publications:

PB1 – *Public Benefit: The public benefit requirement*
PB2 – *Public Benefit: Running a charity*
PB3 – *Public Benefit: Reporting*

The following document, available from www.gov.uk/government/publications/guidance-for-auditors-and-independent-examiners-of-charities, is produced jointly by all three UK regulators:

Matters of Material Significance Reportable to UK Charity Regulators

CCEW also produces a range of 'five-minute guides' (www.gov.uk/guidance/charity-commission-guidance), which include video clips on the basics all trustees need to know. Currently, they are available on the following topics:

- Charity purposes and rules
- Making decisions at a charity
- Managing charity finances
- Managing conflicts of interest in a charity
- What to send to CCEW and how to get help
- Safeguarding for charities and trustees
- Political activity and campaigning by charities

Publications from the Office of the Scottish Charity Regulator

OSCR has a wide range of guidance for Scottish charities (generally published as PDFs). The specific accounting guidance is available at www.oscr.org.uk/guidance-and-forms, which has easy-to-use links to access detailed information and includes the following publications:

A Guide to Charity Accounts
Receipt and Payments Accounts (work pack with templates)
Independent Examination: A guide for charity trustees
Independent Examination: A guide for independent examiners
Trustees' Annual Reports: Guidance and good practice
Charity Reserves Factsheet
Fraud: How to reduce the risks in your charity
SORP
Whistleblowing Guidance

The OSCR website also includes a range of examples of charity accounts and trustees' annual reports.

OSCR's key guidance on charitable status in Scotland, including the Scottish approach to public benefit, is available at www.oscr.org.uk/becoming-a-charity/meeting-the-charity-test and includes:

Meeting the Charity Test: Full guidance
Being a Charity in Scotland

Note that many of the principles in CCEW's publications (if not the legal details) are also relevant in Scotland.

Publications from the Charity Commission for Northern Ireland

CCNI has issued a wide range of accounting guidance, all available as PDFs, that can be downloaded at www.charitycommissionni.org.uk/manage-your-charity/annual-reporting. The key publications are as follows:

ARR01 – *Charity Reporting and Accounting: Overall summary*
ARR02 – *Charity Reporting and Accounting: The essentials*
ARR03 – *Receipts and Payments Accounts for Smaller Charities*
ARR04 – *Accruals Accounts: Preparing accruals accounts*
ARR05–ARR05c – *Guidance on completing the annual monitoring return*
ARR07 – *Independent Examination of Charity Accounts: Examiner's guide*
ARR08 – *The Trustees' Annual Report and Public Benefit Reporting*

Note that ARR07 includes a section 'The Commission's Directions'. These mandatory directions must be followed by anyone undertaking an independent examination of the accounts of a registered charity in Northern Ireland (they have similar status to the directions made by CCEW in CC32 for independent examiners in England and Wales, but they are not identical).

CCNI's key guidance on charitable status in Northern Ireland – including the statutory guidance on public benefit, which *must* be considered by trustees of Northern Irish charities – is available at www.charitycommissionni.org.uk/manage-your-charity/register-your-charity/the-public-benefit-requirement. Key publications include:

PBR1 – *The Public Benefit Requirement*
PBG – *Public Benefit Glossary*
EG016 – *Registering as a Charity in Northern Ireland*

In addition, CCNI has detailed guidance in relation to each of the main categories of charitable purposes (PBSD01 to PBSD12).

Note that many of the principles in CCEW's publications (if not the legal details) are also relevant in Northern Ireland. In general, charity law in Northern Ireland is closer to that in England and Wales than to that in Scotland. Therefore, in the absence of specific CCNI guidance, the relevant guidance from CCEW will normally be more relevant than the guidance from OSCR.

Legislation on charity accounts

Acts and secondary legislation can be accessed free online at www.legislation.gov.uk. Statutes (i.e. Acts) are generally updated on www.legislation.gov.uk when they are amended, but this often takes some time after the amendment is made – look for the notes on each Act regarding amendments outstanding. This updating does not, however, apply to secondary legislation, which is currently only available in original versions. So, for example, while charity accounting in Scotland remains subject to the 2006 Regulations (as amended), the full legal details can only be obtained by taking the original 2006 Regulations together with the Charities Accounts (Scotland) Amendment Regulations of 2007, 2010, 2014, 2016, 2017, 2018 and 2019.

Acts

The major relevant Acts are:

Charities Act 2011 (as amended – primarily by the Charities (Protection and Social Investment) Act 2016 and the Charities Act 2022)

Charities and Trustee Investment (Scotland) Act 2005 (as amended – primarily by the Public Services Reform (Scotland) Act 2010 and by the Charities (Regulation and Administration) (Scotland) Act 2023)

Charities Act (Northern Ireland) 2008 (as amended – primarily by the Charities Act (Northern Ireland) 2013 and the Charities Act (Northern Ireland) 2022)

Secondary legislation

The major relevant secondary legislation is:

Charities (Accounts and Reports) Regulations 2008

Charities Accounts (Scotland) Regulations 2006 (as amended)

Charities (Accounts and Reports) Regulations (Northern Ireland) 2015

Tertiary legislation (by charity regulators)

Regulations made by the charity regulators (rather than by the parliaments or the Northern Ireland Assembly) are not available from www.legislation.gov.uk but can be obtained from the websites of the charity regulators themselves. This includes CCEW's *Independent Examination of Charity Accounts: Directions and guidance for examiners* (CC32) and CCNI's *Independent Examination of Charity Accounts: Examiner's guide* (ARR07).

Likewise, the regulations made by charity regulators regarding charities' annual returns are tertiary legislation.

Accounting standards

The latest SORP – *SORP (FRS 102)* (second edition, effective 1 January 2019) – plus various explanatory help sheets, is jointly published by CCEW, CCNI and OSCR. The SORP and help sheets are available from the SORP website: www.charitysorp.org. On this site, you can also download a tailored SORP containing only the modules required, or purchase a copy of the printed SORP.

FRS 102: The Financial Reporting Standard applicable in the UK and Republic of Ireland (and amendments) was published by the Financial Reporting Council in 2018 and is available online from www.frc.org.uk.

See also the guidance earlier in the further reading section on charity accounting from CCEW, OSCR and CCNI.

There are also a number of documents that apply the SORP in relation to particular types of charity – see page 322.

Charities and tax issues

Two publications are of particular relevance:

Alastair Hardman and Kate Sayer, *The Complete Charity VAT Handbook*, 4th edition, London, Directory of Social Change, 2016
How VAT Affects Charities (VAT Notice 701/1), last updated September 2022, www.gov.uk/guidance/how-vat-affects-charities-notice-7011 (this explains the main VAT rules specific to charities, though various supplementary notices may also be applicable)

Charity law and legal structures

The following two publications provide comprehensive overviews of charity law and legal structures:

Gareth G. Morgan, *Charitable Incorporated Organisations*, 2nd edition, London, Directory of Social Change, 2018
Mike Eastwood and Jacqueline Williams, *The Charity Trustee's Handbook*, updated 3rd edition, London, Directory of Social Change, 2023

The General Data Protection Regulation

Paul Ticher, *Data Protection for Voluntary Organisations*, 4th edition, London, Directory of Social Change, 2021

Useful addresses

Statutory and regulatory bodies

Charity Commission for England and Wales

Charity Commission, PO Box 211, Bootle L20 7YX
Tel: 0300 066 9197
Website: www.gov.uk/guidance/online-services-for-charities
Contact form: https://forms.charitycommission.gov.uk/enquiry-form

Office of the Scottish Charity Regulator

2nd Floor, Quadrant House, 9 Riverside Drive, Dundee DD1 4NY
Tel: 01382 220446
Website: www.oscr.org.uk
Contact form: www.oscr.org.uk/contact-oscr/contact-form

Charity Commission for Northern Ireland

Marlborough House, Central Way, Craigavon BT64 1AD
Tel: 028 3832 0220
Website: www.charitycommissionni.org.uk
Contact form: www.charitycommissionni.org.uk/about-us/contact-us

Companies House

Tel: 0303 1234 500
Website: www.gov.uk/government/organisations/companies-house
Email: enquiries@companieshouse.gov.uk

Registrar of Companies (England and Wales)

Companies House, Crown Way, Cardiff CF14 3UZ

Registrar of Companies (Scotland)

Companies House, 4th Floor, Edinburgh Quay 2, 139 Fountainbridge, Edinburgh EH3 9FF

Registrar of Companies (Northern Ireland)

Companies House, 2nd Floor, The Linenhall, 32–38 Linenhall Street, Belfast BT2 8BG

Financial Conduct Authority

FCA Head Office, 12 Endeavour Square, London E20 1JN
Tel: 0300 500 8082
Website: www.fca.org.uk
Contact form: www.fca.org.uk/contact

Fundraising Regulator

Eagle House, 167 City Road, London EC1V 1AW
Tel: 0300 999 3407
Website: www.fundraisingregulator.org.uk
Email: admin@fundraisingregulator.org.uk

Scottish Fundraising Adjudication Panel

c/o OSCR, 2nd Floor, Quadrant House, 9 Riverside Drive, Dundee DD1 4NY
Tel: 0808 164 2520
Website: www.goodfundraising.scot
Email: info@goodfundraising.scot

HM Revenue and Customs (Charities)

HMRC, Charities, Savings and International 2 BX9 1BU
Tel: 0300 123 1073
Website: www.gov.uk/charities-and-tax

This HMRC office covers charities throughout the UK and deals with charity-specific issues relating to both direct tax questions (such as Gift Aid) and indirect taxes (such as VAT). All the requirements for applying for charity tax recognition and operation of Gift Aid schemes are available from the website above.

National Cyber Security Centre

The NCSC supports organisations in cyber security.
Website: www.ncsc.gov.uk

Professional bodies concerned with charity finance

The following professional associations are established specifically for those working with charities.

Association of Charity Independent Examiners

ACIE provides support, training and a qualification for independent examiners, and a referral service for charities seeking an independent examiner.

9th Floor, Block C, The Wharf, Manchester Road, Burnley BB11 1JG
Tel: 07899 891616
Website: www.acie.org.uk
Email: admin@acie.org.uk

Charity Finance Group

The Charity Finance Group offers a range of services relevant to finance managers in charities of all sizes. It includes a section listing some community accountancy services (i.e. bodies that help charities to manage their finances) in England and Wales.

15–18 White Lion Street, London N1 9PG
Tel: 0845 345 3192
Website: www.cfg.org.uk
Email: info@cfg.org.uk

Charity Tax Group

The Charity Tax Group represents all types of charitable activity, making representations to the government on tax issues affecting charities. It is the leading voice for charity taxation.

Church House, Great Smith Street, London SW1P 3AZ
Tel: 020 7222 1265
Website: www.charitytaxgroup.org.uk
Email: info@charitytaxgroup.org.uk

Chartered Institute of Fundraising

Although members of the Chartered Institute of Fundraising are normally fundraisers rather than treasurers and finance staff, some of its work is also of relevance to treasurers (see chapters 7 and 10).

Canopi, 7–14 Great Dover Street, London SE1 4YR
Tel: 020 7840 1000
Website: www.ciof.org.uk
Email: info@ciof.org.uk

Honorary Treasurers Forum

The Honorary Treasurers Forum provides online support and regular meetings to support treasurers in the important work that they do, so as to share expertise and promote best practice.

c/o Centre for Charity Effectiveness, Bayes Business School, 106 Bunhill Row, London EC1Y 8TZ
Tel: 0207 0408781
Website: www.honorarytreasurers.org.uk
Email: info@honorarytreasurers.org.uk

Networks for treasurers in specific types of charity

There are also a number of networks and associations of treasurers and finance staff within particular types of charity. Some of these produce quite detailed guidance on accounting, but do check that it is accurate and up to date in terms of complying with charity law. If your local charity is part of a national network, contact the central office to find out if there is any specific support for local treasurers and finance staff.

Other professional bodies

Many more general professional bodies have a charity-specialist group or special newsletters for those working with charities, including ACCA, CIPFA, ICAEW, ICAS and ICSA. You can also use these bodies to help you find accountants, and some provide extensive guidance documents on charity accounting issues on their websites. Firms of registered auditors will always be regulated by ACCA, ICAEW, ICAS or Chartered Accountants Ireland.

Association of Accounting Technicians (AAT)

30 Churchill Place, London E14 5RE
Tel: 020 3735 2468
Website: www.aat.org.uk
Email: customersupport@aat.org.uk

Association of Chartered Certified Accountants (ACCA)

110 Queen Street, Glasgow G1 3BX
Tel: 0141 582 2000
Website: www.accaglobal.com
Contact form: www.accaglobal.com/gb/en/footer-toolbar/contact-us.html

Chartered Accountants Ireland

Belfast office: The Linenhall, 32–38 Linenhall Street, Belfast BT2 8BG
Tel: 028 9043 5840
Website: www.charteredaccountants.ie
Contact page: www.charteredaccountants.ie/about-us/Contact-Us

Chartered Governance Institute UK and Ireland (ICSA)

Saffron House, 6–10 Kirby Street, London EC1N 8TS
Tel: 020 7580 4741
Website: www.cgi.org.uk
Contact form: www.cgi.org.uk/about-us/contact-us

Chartered Institute of Management Accountants (CIMA)

The Helicon, One South Place, London EC2M 2RB
Tel: 020 8849 2251
Website: www.aicpa-cima.com

Chartered Institute of Public Finance and Accountancy (CIPFA)

77 Mansell Street, London E1 8AN
Tel: 020 7543 5600
Website: www.cipfa.org
Email: customerservices@cipfa.org

Institute of Chartered Accountants in England and Wales (ICAEW)

Chartered Accountants Hall, Moorgate Place London EC2R 6EA
Tel: 01908 248250
Website: www.icaew.com
Charity-specific resources: www.icaew.com/technical/charity-community
Email: communities@icaew.com

Institute of Chartered Accountants of Scotland (ICAS)

Chartered Accountants House, 21 Haymarket Yards, Edinburgh EH12 5BH
Tel: 0131 347 0100
Website: www.icas.com
Charity-specific resources: www.icas.com/professional-resources/charities
Email: connect@icas.com

Glossary

The following terms are shown in **bold** at their first main use in each chapter. Bold within the glossary means that a term has its own entry elsewhere in the glossary. Please note that this glossary seeks to explain the use of terms in a charity accounting context – some terms may have other meanings when applied to commercial accounts. In most cases it also seeks to give a plain English explanation of the typical usage in a charity context rather than a legal definition of the term. (Some of these terms are defined more formally in the chapters where relevant or in the relevant module of the Charities **SORP** – see the further reading, on page 313.)

Accountable body: Where funding is agreed for work involving a partnership of two or more organisations, or where one **charity** is passing on funding to other charities, the accountable body is the lead charity which is accountable to the **funder** for ensuring the use of the funding as agreed, or accountable for the overall service provision. (The term is mainly used in relation to public sector funding, but it could apply to funding from any source.)

Accounting period: The period of time used for a particular set of accounts. For **annual accounts**, the period is normally 12 months, but **management accounts** may be prepared for a shorter period such as a month or quarter.

Accounting policies: A set of guidelines that explains how a group of **transactions** are treated for accounting purposes, or how a method of valuation is applied – for example, a policy to set out how and when income is recognised in the accounts, or how **depreciation** is calculated on **fixed assets**. See also **true and fair view**.

Accounting records: The formal term for the basic books of the **charity**, where every **transaction** – every receipt, payment or other entry – is recorded individually. The term also includes supporting documents such as invoices, payslips and **donation** forms, whether paper based or electronic. In general, charities must keep accounting records for the current year and six prior years.

Accounting standards: A document used with **accruals accounting** which sets out principles to be used in the preparation of **financial accounts** to assist in ensuring that they give a **true and fair view** and to introduce consistency between the accounts of different organisations. Accounting standards are usually divided into general-purpose standards that apply to any industry or type of organisation – for which the key standard at the time of writing is **FRS 102**, and sector-specific standards – which for **charities** is the Charities **SORP**. General-purpose standards are issued in the UK by the Financial Reporting Council. The Financial Reporting Council then authorises appropriate sector bodies to prepare SORPs, subject to Financial Reporting Council approval that a SORP does not depart from the principles in the relevant general-purpose standards.

Accrual: An entry in the books of an organisation to allow for costs applicable to a particular accounting year that are not yet paid by year end. (It is the opposite of a **prepayment** – see chapter 4 for further details.) Accruals may include expenses that are known to apply even if no bill has been received by year end – for example, for fuel which has been consumed up to year end (if **material**) even though the next bill may not be expected until several months into the following year. Accruals normally appear on the **balance sheet** under the heading '**Creditors** due within one year'.

Accruals accounting: **Charity** accounts prepared on the accruals basis show all income earned during the **accounting period** (the accrued income) and all expenses incurred in running the charity for that time (the accrued expenditure). This is contrasted with **R&P accounting**, which only accounts for money received and paid out. Final charity accounts on the accruals basis must be presented in Charities **SORP** format. Accruals accounting is considered essential for accounts to give a **true and fair view.** (See chapters 4 and 14 for more details.)

Accumulated depreciation: The total of all **depreciation** that has been charged against an **asset** over its **useful life**.

Aggregate gross income: The total income (after **consolidation**) of a **charity** group comprising a charity with one or more subsidiaries. It is calculated as the income of the charity plus the income of the subsidiaries, but deducting income received by the charity from the subsidiaries to prevent double counting.

Ancillary trading: A trading activity carried out that is in addition, but linked, to the primary purpose or to complement the **charity's purposes**. See also **primary-purpose trading** and chapter 8.

Annual accounts: The final year-end published accounts of a **charity**, as approved by the **trustees**, sometimes called the **financial accounts**. All charities must publish annual accounts, and in most cases they must be sent to the relevant **charity regulator** (CCEW, OSCR or

CCNI). A report from an **auditor** or **independent examiner** should usually be attached, and the accounts should normally be accompanied by the **trustees' annual report** (see chapters 2 and 7 for specific rules).

Annual report: See **trustees' annual report**.

Annual report and accounts: The financial and related documents which a **charity** is required to publish at year end. For most charities, the annual report and accounts (sometimes called the **financial statements**) comprise the **trustees' annual report**, the **annual accounts**, and the report of the **auditor** or **independent examiner**.

Annual return: An annual form with questions set by the **charity regulator** which registered **charities** must complete – normally at the same time as filing their annual report and accounts. The **trustees** are responsible for completing the return, but the task is usually delegated to the **treasurer** or **finance officer**. The questions differ depending on the regulator and individual charity but will cover areas such as income, expenditure, employees and transactions with trustees.

Articles of association: The **governing document** of a **charitable company** (in the past, charitable companies had two governing documents, known as the 'memorandum and articles of association', but, since 2009, provisions that were in the memorandum are now treated as part of the articles).

Asset: Any money, object or resource which is owned by the **charity** or its **trustees** for the work of the charity (or to which the charity or the trustees have a legal entitlement). Assets must be shown on the charity's **balance sheet**, **SOAL** or **statement of balances**. The assets are usually divided into **fixed assets** and **current assets**.

Asset lock: Certain organisations, such as **charities** and **CICs**, are subject to a framework which makes it illegal for money or other resources to be removed from the organisation except for expenditure directly related to its stated purposes. (In the case of CICs, up to 35% of profits can be paid to investors, but otherwise the **assets** remain locked.) By contrast, a normal company limited by shares generally has no asset lock, and assets can be used to pay dividends to private shareholders.

Audit: The scrutiny of accounts by a registered **auditor**, who, as an audit professional, will apply auditing standards issued by the Auditing Practices Board. A registered auditor is one registered with a recognised supervisory body in accordance with the Companies Act 2006.

Audit trail: A trail of information which enables an **auditor** or **independent examiner** to verify how any figure in the accounts was reached. A key element of any audit trail is a list of all the **transactions**

entered into the **charity's** books, usually broken down under the account headings used. With manual accounting, a cashbook is central to the audit trail. Most computer-based accounting systems automatically create an audit trail of transactions entered (but this is not the case with spreadsheets).

Auditors: A firm of accountants that holds the status of a registered auditor, appointed to report on the **annual accounts** of a **charity** in accordance with applicable legislation – in particular, with **accruals accounts**, to state whether the auditors consider that the accounts give a **true and fair view**. (However, for many small and medium-sized charities, it is possible to appoint an **independent examiner** rather than an auditor.)

Auto-enrolment: The requirement that all employees in the UK (with limited exceptions, such as those earning under £10,000 a year) must be automatically enrolled in a pension scheme (such as the government's NEST scheme) unless they specifically request otherwise. This includes **charity** employees. Once enrolled, both employer and employee make pension contributions based on a percentage of earnings. See chapter 11.

BACS (Bankers' Automated Clearing System): A system that allows electronic money transfers between banks, either as a one-off or on a recurring basis. It is often used by large **funders** to send **grant** payments or third-party payroll services to send salary payments to employees. Direct debits are a form of **BACS** payment.

Balance sheet: One of the two **primary statements** (the other is the **SOFA**) in any set of **charity** accounts prepared on the **accruals accounting** basis. The balance sheet shows the various **assets** and **liabilities** of the charity at year end totalled to a figure for net assets which must equal the total of the charity's **fund** balances at year end. The required format for the balance sheet is set out in the Charities **SORP** (see chapter 14).

Balancing off: See **closing off**.

Bookkeeping: The term used to describe drawing up and maintaining the **accounting records** of an organisation. It involves recording and organising the financial **transactions** and records on a daily basis and, from them, preparing the **annual accounts**. See also **double-entry bookkeeping**.

Budget: An estimate of the income and expenditure of a **charity** over a specific period, often a year. See chapter 6.

Budget variance: The difference between the actual figure on a particular account and the **budget** that was set. It can be expressed as an absolute difference in pounds or as a percentage. The process of determining it is known as **variance analysis**. See chapter 6.

Capitalisation: The act of recognising an item on the **balance sheet** as an **asset** rather than as an expense in the **SOFA**. It is generally used in reference to the purchase of **fixed assets**, such as equipment that will be used in the **charity** for more than one year.

Capitalisation limit: In general, with **accruals accounts**, **fixed assets** will be **depreciated** over a number of years. However, to avoid keeping track of depreciation on small items, it is normal to set a **capitalisation limit** below which the entire cost of an item is charged at the time of purchase (even for items expected to last several years) where it would not make a **material** difference to someone reading the accounts. The same principle can be used with **R&P accounts** to decide whether or not an **asset** is included in the **SOAL** (or **statement of balances** in Scotland).

Cash flow forecast: A financial report, normally prepared for internal use by **trustees** and staff (or as part of a funding bid), that shows the likely movements of money for some time ahead, either for the **charity** as a whole or for a certain project. Particularly for activities where costs may be incurred before the corresponding receipts (such as a project paid in arrears), a cash flow forecast is vital to consider whether the charity has sufficient cash **reserves** or borrowing is required. Depending on the activity, a cash flow forecast may relate to a short period such as a few weeks, or may cover a period as long as several years for a project which has extensive start-up costs that will take time to recover. (This should be distinguished from a **statement of cash flows**, which provides historical cash flow information.)

Charitable association: An **unincorporated** structure used by many **charities** where members come together under the terms of a **constitution**. Usually the members elect a committee and those who serve on the committee are the charity **trustees**.

Charitable company: A **charity** which is formed as a company with charitable aims (almost always a company limited by guarantee) and is also recognised as a charity. Charitable companies are subject to both company law and charity law.

Charitable incorporated organisation (CIO): A type of **charity** with corporate status and limited **liability** but governed solely by charity law (thus giving many of the advantages of a **charitable company** but without the organisation being subject to company law). A CIO is formed by registration with the relevant **charity regulator** (CCEW or

OSCR, or CCNI in the future). See also **Scottish charitable incorporated organisation (SCIO)**.

Charitable object: A statement of the overall aims or purposes of a specific charity. The resources of a charity must always be used in the way that the trustees consider will best advance its objects. See also **charitable purpose**.

Charitable purpose: Every **charity** is established for one or more charitable purposes as stated in its objects. The headings listing purposes that are charitable in law are set out in the relevant legislation in each **jurisdiction**: for England and Wales, in the Charities Act 2011; for Scotland, in the Charities and Trustee Investment (Scotland) Act 2005; and for Northern Ireland, in the Charities Act (Northern Ireland) 2008.

Charitable trust: The simplest structure for a **charity**. It is formed when an initial **donor** (the **settlor**) makes a gift of money or other property and appoints the initial charity **trustees**. Most charitable trusts are governed by a **trust deed**, but a charitable trust can also be established through the terms of a legacy (sometimes called a 'will trust') or by a scheme of CCEW (a legal document created under the powers of CCEW).

Charities SORP: See **Statement of Recommended Practice on Accounting and Reporting by Charities (SORP)**.

Charity: An organisation with exclusively charitable aims established for **public benefit**, as defined in the relevant **jurisdiction** (slight differences in the definition apply between England and Wales, Scotland and Northern Ireland, and in tax law). Registration requirements vary, but in England and Wales many **charities** are **exempt** or **excepted** from registration with CCEW.

Charity co-ordinator: The term used through this book to mean the most senior paid member of staff at the **charity** (although it could also be a volunteer role which is not carried out by any of the **trustees**). In a small or medium-sized charity, this is likely to be the person who co-ordinates the activities, staff, **fundraising** and administration of the charity and reports back to the trustees, while delegating some tasks to other staff and volunteers.

Charity regulator: A body with statutory responsibility for the oversight and regulation of **charities**. In the UK, the term encompasses CCEW (for charities in England and Wales), OSCR (for charities in Scotland) and CCNI (for charities in Northern Ireland).

Charity shop: A retail premises operated to raise money for a **charity**. Charity shops can sell a variety of donated goods, items made by the charity's beneficiaries, items that promote the charity and its work, and other stock.

Closing off (or balancing off): In any **bookkeeping** system, whether manual or computerised, at the end of an **accounting period** the two sides of any account must be deducted from one another to give a net figure, leading to the final balance on the account. This is often called 'closing off' or 'balancing off'. The difference between the two sides, plus the opening balance (if applicable) at the start of the period, is then carried forward to the following period. For example, on a particular **fund**, payments may be deducted from receipts to give a balance of net receipts to the fund over that period. Or, on a **debtors** account, credits may be deducted from debits to give the net movement in debtors over that period: this is then added to the opening balance of the debtors account at the start of the period to give the final debtors balance. See chapter 4.

Collective responsibility: No one individual charity **trustee** has more responsibility, power or control over the **charity** than the others, including the chair or **treasurer**. All decisions and actions are taken collectively by the trustees as a whole.

Commercial participator: A person who carries on a business and, in the course of that business, promotes goods or services on the basis that it will make **donations** to a charitable organisation (this does not include a company associated with the charity such as a trading subsidiary). See chapter 7.

Community benefit society (CBS): A corporate body, sometimes called an **incorporated** society or a bencom, which is established for purposes which benefit the community. Available throughout the UK, a CBS can be recognised as a **charity**, but the primary regulator is the Financial Conduct Authority. CBSs are established under the Co-operative and Community Benefit Societies Act 2014 (and previously under the Industrial and Provident Societies Acts). In England and Wales, a charitable CBS is currently an **exempt charity**. (Note that this book does not cover the specific accounting rules for CBSs or other exempt charities.)

Community interest company (CIC): A company that has social aims. A CIC does not have charitable status and therefore is not covered by this book.

Confirmation statement: An **annual return** (online form) sent to Companies House by **charitable companies** on the anniversary of their **incorporation**. It confirms that the details Companies House holds are correct.

Conflict of interest: Any situation where a **trustee**'s personal interest could, or could be seen to, prevent them from making a decision only in the best interests of the **charity**. This is usually where the trustee, or a **connected person**, may benefit financially or some other way.

Conflict of loyalty: A particular type of **conflict of interest** where a **trustee**'s loyalty, or that of a **connected person**, to another person or organisation could, or could be seen to, prevent the trustee from making a decision only in the best interests of the **charity**.

Connected person: As set out in law, this is a close relative (e.g. spouse, civil partner, parent, grandparent, child or sibling) or business partner of a **trustee**. It also refers to businesses that a trustee (or their relative) has ownership or control over. It is an important factor to consider when making decisions, as a potential **conflict of interest** or **conflict of loyalty**, and also when making payments to someone connected to a trustee.

Consolidation: When an organisation has one or more subsidiary bodies which maintain their own accounts, the term 'consolidation' refers to the process of bringing the separate sets of accounts together into an overall account. Sometimes the subsidiary bodies are simply groups or branches within the structure of one **charity**, so the charity is only required to produce one set of **annual accounts** (see page 106). However, in the case of a charity which has a **trading subsidiary** company or where a charity controls subsidiary charities, each entity must produce **individual accounts**, which are then consolidated to produce **group accounts** (see page 281).

Constitution: One of the most common forms of **governing document** for a **charity**, setting out its **charitable purposes** and rules for members and **trustees**. The term 'constitution' can be applied to any kind of governing document but is most commonly applied to the rules of a **charitable association** or a **CIO** or **SCIO**.

Contract: An agreement between two or more parties where one party agrees to provide goods or services to the other in return for 'consideration' (normally the consideration is a payment of money – generally described as a **fee**). Where a **charity** receives income from contracts or fees, that money should be classed as **trading income** in the accounts.

Co-operative society: A jointly owned, people-centred organisation regulated by the Financial Conduct Authority. A co-operative society does not have charitable status and therefore is not covered by this book.

Creditors: People or organisations to which a **charity** owes money or other resources.

Current asset: An **asset** which is either in the form of money or which can be readily converted to money within 12 months. Current assets typically include cash at the bank, cash in hand (i.e. petty cash and cash receipts not yet banked), **debtors** (where the receipt of the amount due is expected within 12 months), **prepayments**, stocks (if **material** for the **charity** concerned) and short-term **investments** such as **deposit accounts** requiring less than 12 months' notice to make a withdrawal.

Current liability: A **liability** for which a **charity** expects to make payment within the next 12 months (otherwise it would be a **long-term liability**). Current liabilities generally include trade **creditors** (where due within 12 months), **accruals** and **deferred income**.

Custodian trustee: See **holding trustee**.

Debits and credits: See **double-entry bookkeeping**.

Debtors: People or organisations which owe money or other resources to a **charity**.

Declaration of trust: See **trust deed**.

Deemed list: A list of bodies in Northern Ireland that are not yet registered with CCNI but which had been recognised as **charities** for tax purposes (by **HMRC**) as at February 2011. They are deemed to be charities for the purposes of CCNI oversight until CCNI makes a formal decision on whether they should be registered.

Deferred income: The technical term for income received in advance of the year in which it should be recognised (although when it arises, it is best in your **annual accounts** to use a more meaningful explanation such as 'Subscriptions received in advance' or '**Grant** only to be used next year'). Such amounts normally appear on the **balance sheet** under '**Creditors** due within one year' because, at the end of the year concerned, the **charity** is not yet entitled to use the amount held in its bank balance.

Deficit: A deficit arises when the expenditure was more than the income in a given year – either for a particular **fund** or for the **charity** as a whole.

Defined benefit scheme: A type of pension scheme whereby the pension fund commits to paying a certain proportion of an employee's salary as a pension for the rest of their life (often with commitments to **inflationary** increases).

Deposit account: A type of bank account usually used for savings, as opposed to a current account, which is usually used for everyday needs. The money you deposit in the account earns interest. There may be time restrictions on when you can withdraw the money – for example, you may have to give the bank 90 days' notice that you want to withdraw some or all of your money.

Depreciation: In **accruals accounting**, the process of spreading the cost of a **fixed asset** over a number of financial years. In each year's **SOFA**, only that year's depreciation appears as expenditure. Different methods can be used to calculate depreciation, such as **straight line depreciation** or the **reducing balance method**.

Designated fund: A **fund** holding resources set aside by the **trustees**, usually to provide for significant expenditure that may arise in future years. However, a designated fund is not a **restricted fund**, as there is no external restriction on its use, so designated funds are included within **unrestricted funds** in a **charity's annual accounts**.

Direct payments: Payments made to a **charity** to provide support to a particular individual, usually in terms of health or social care. They can be paid by the local authority or government department responsible to the charity, but are normally paid directly by the individual concerned (out of the benefits they receive) or by those responsible for their care.

Disclosure: The act of making available relevant information. In the context of **charity** accounting and reporting, this may be financial information and additional explanations to describe something more fully. This is to enable the reader to have the information they need to understand the true position of the charity, and for the charity to be accountable for its actions.

Donated income: Income which is given to a **charity** with no expectation of anything in return other than a receipt or acknowledgement and possibly feedback on how it was used. It is given to advance the charity's aims, not for any benefit to the **donor**. The term 'donated income' generally includes **donations** from individuals (including tax recovered under Gift Aid), legacy gifts and **grants** from other organisations.

Donation: A gift to a **charity**, usually made by an individual. The donation may be given for the charity's general work (an **unrestricted** donation) or for a specific project or appeal (a **restricted** donation). (If the donor is an organisation, it is more usual to describe the gift as a **grant**, but sometimes companies and smaller grant-making charities prefer the term 'donation'.)

Donor: A person (or organisation) who makes a **donation** to a **charity**.

Double-entry bookkeeping: The process of **bookkeeping** where every **transaction** is recorded against two accounts, one side known as a 'debit' and the other side as a 'credit'. This makes it much easier to verify the resulting figures than with single-entry bookkeeping (see chapter 4). Double-entry bookkeeping is more or less essential to **accruals accounting**; however, even with **R&P accounting**, it is very much recommended if the charity has several **funds** and/or several bank accounts. Most computer-based accounting systems inherently use double-entry bookkeeping principles.

Dual authorisation: A security process (a financial control) that requires two or more authorised **charity** officers (**trustees**, staff or volunteers) to approve certain **transactions** – for example, to make a purchase or to authorise a payment from the bank. See chapter 5 for more information.

Dual regulation: The situation where a **charity** is subject to regulation by more than one **charity regulator**. For example, if a charity established in England has regular activities in Scotland, it will typically be subject to regulation by both CCEW and OSCR.

Endowment fund: A **fund** which is given to a **charity** on terms where, normally, the fund itself cannot be spent. Typically, the endowment is invested and the resulting **investment income** is allocated to another fund to support the work of the charity, but the capital cannot be spent. In some cases, an **endowment fund** may comprise property rather than **investments** – such as a historic building, village hall or place of worship. In such cases, the property is to be retained permanently for the operational work of the charity. If the endowment can never be spent, it is called a **permanent endowment**, but where the **trustees** have the authority, in certain circumstances, to use the capital (or to sell the property) for other charitable expenditure, it is called an **expendable endowment**.

Excepted charity: A **charity** in England and Wales which is excepted from registration with CCEW – but it remains subject to the authority of CCEW and to the accounting requirements in the Charities Act 2011. The definition currently includes most English and Welsh charities (other than **CIOs**) with annual incomes of up to £5,000, and many Christian churches (in specified denominations), Scout and Guide groups, and certain armed forces charities with annual incomes of up to £100,000.

Exempt charity: A **charity** in England and Wales which is exempt from the direct oversight of CCEW. These include academy schools, most English universities and charitable **CBSs**. Many, but not all, exempt charities are subject to a principal regulator – such as a government department – which has oversight of their charitable status. (Note that this book does not cover the specific accounting rules for exempt charities.)

Expendable endowment: See **endowment fund**.

Extended trial balance: See **trial balance**.

Fair value: In **accruals accounting** under **FRS 102** (and therefore the Charities **SORP**), **assets** and **liabilities** are normally shown in the accounts at **fair value** – that is, the value that would be placed on them in an arms-length **transaction** between unconnected parties. Sometimes the computation of fair value can be quite complex – see the example on page 264 regarding the valuation of a multi-year **grant** commitment.

Fee: An amount charged to a person or organisation for access to a service or activity provided by a **charity**, either to meet the **charitable purposes** or for **fundraising**. See also **contract**.

Finance officer: A person who has been appointed to a role, by the **trustees**, to manage the accounting processes and finances of a **charity** on their behalf. This could be a paid or voluntary position. The role may not specifically be called 'finance officer'; typically terms such as 'bookkeeper' or 'finance manager' are used (see the discussion on page 29).

Financial accounts: This term usually refers to accounts which are prepared for external use (as with a **charity's annual accounts**) in contrast to **management accounts**, which are only for internal use within a charity.

Financial records: The collection of documents that record, summarise and support all of the **transactions** of a **charity**, also known as **accounting records**.

Financial statements: See **annual report and accounts**.

Fixed asset: An **asset** which a **charity** intends to hold for at least 12 months. **Fixed assets** are generally divided into **tangible assets** (for example, buildings, equipment or vehicles used in the operational work of the charity) and **investments**, which are held purely to generate an income to support the charity's work (provided the intention is to hold them for at least 12 months). However, other types of **asset** are possible, including **heritage assets** (such as paintings owned by an art gallery or artefacts in a museum) and **intangible assets** (if, for instance, the charity had acquired some form of valuable intellectual property which needed to have a value on its **balance sheet**). Some charities also have programme-related investments, more commonly known as **social investments**.

Fixed asset register: A record of all a **charity's fixed assets**, generally including details such as a description and location of the item, the serial or registration number (if applicable), the supplier and price paid, and possibly warranty or insurance details. In the case of fixed assets subject to **depreciation** with **accruals accounting**, the fixed asset register should be updated to show the depreciation charged each year. To avoid recording numerous small **assets**, newly acquired fixed assets are generally not added to the fixed asset register if their cost or value is below the **capitalisation limit** that the charity has set. The fixed asset register is an important part of a charity's **accounting records**, although for straightforward cases, a copy of the supplier's invoice for the fixed asset may provide most of the information needed. (Even for a charity using **R&P accounting**, a fixed asset register of some kind is needed in order to produce a **SOAL** for the **annual accounts**.)

FRS 102: See **accounting standards** (and see also further discussion in chapter 14).

Full cost recovery: When an external body is funding a particular service provided by a **charity** (whether under a **grant** or a **contract**), the charity will usually wish to agree a level of funding which at least should cover the full costs of the service, including an appropriate share of the charity's overheads. (In some cases, with **contract** funding, the **trustees** may require sufficient funding to provide a **surplus** in addition to the full cost.) Where the **funder** will not agree to pay the full cost, trustees have to consider whether to undertake the work at a lower price (by subsidising the project from other income) or decline the work.

Functional headings: The income and expenditure lines in the **SOFA**. Income and expenditure are categorised by activity under these headings, such as 'costs of raising funds' or 'costs to deliver charitable activities'. This is opposed to what the income or cost is actually for, such as salaries or rent.

Fund: A pool of money or resources held by a **charity** for particular purposes. For more details see **unrestricted funds**, **designated funds**, **restricted funds** and **endowment funds**.

Fund accounting: The process of maintaining **accounting records** so that all **transactions** involving income or expenditure are allocated to specific **funds** within the **charity's** books. Fund accounting is one of the most significant issues that distinguishes charity accounting from most commercial accounting. Where a charity has any **restricted funds**, the **trustees** are likely to be committing a breach of trust if they do not use fund accounting to keep track of the separate funds. Transfers between funds require use of an **inter-fund transfer** type of **transaction**.

Funder: A person, or more usually an organisation, that provides funds to a **charity**. The term is typically used to describe those that make income available to charities in the form of **grants**, **SLAs** or **contracts**.

Fundraising: The process of raising or securing the necessary income to support the work of a **charity**. Sometimes the term is used to refer to **funds** provided by individual **donors** only; however, in this book, the term fundraising refers to the process of generating income from any sources that may support the work of a charity.

Fundraising consultant: A specialist in **fundraising** that a **charity** can appoint to give advice and provide services, such as to develop a fundraising strategy and draft applications and campaigns, but without the authority to approach and contact **funders** and **donors** on the charity's behalf, unlike a **professional fundraiser**. Refer to chapter 7.

Funds note: A note to be added into the **annual accounts** of a **charity** which explains the movements in funds over the year of the accounts. It shows the opening balance, income and expenditure for the year, and closing balance for each of the **unrestricted**, **designated** and **restricted fund**s. It also shows transfers between the **funds** and includes a narrative to describe what each fund is used for (see chapters 13 and 14).

Funds transfer: This term normally refers to an **inter-fund transfer** in a **charity's accounting records**. (Sometimes the term is used to describe the transfer of funds between bank accounts or **investments**; however, to avoid confusion, this type of **transaction** is better described as an '**asset** transfer', as it is a transfer between asset accounts – it does not involve a transfer between the **funds** of a charity.)

General fund: The main **unrestricted fund** of a **charity** which is also undesignated – so it is available for the general work of the charity. Every charity should have a general fund (to be used at least for miscellaneous income and expenses, even if most of the income is allocated to **restricted funds**).

Going concern: An accounting term which means it is probable that an organisation will be able to keep going for the foreseeable future – that is, it has resources available to meet its **liabilities** and obligations as they fall due. **Trustees** are responsible for making this assessment. In making the assessment, the trustees should take into account all available information about the future for at least, but not limited to, 12 months from the date the accounts are approved.

Governance: The act of managing a **charity** with accountability. It tends to mean the processes, roles and responsibilities by which an organisation is directed and managed by the **trustees**.

Governing document: Every **charity** requires a formal document which sets out the basis on which it is established. The governing document will include the **charitable purposes**, how **trustees** are appointed, how decisions are made, and normally a clause to say what happens if the charity is dissolved. The governing document can take various forms – most commonly a **constitution**, **trust deed** or **articles of association**.

Grant: A gift or **donation** made to a **charity**, or made by a charity to an external recipient. A grant (as opposed to a **contract**) has no requirement for anything to be provided back to the **donor** or **funder** other than an acknowledgement and potentially feedback and/or monitoring information. (There is no legal distinction between a grant and a donation, but the term 'grant' is more frequently used when the gift is made by an organisation rather than an individual.) Many grants are made to charities for specific purposes, and in such cases the grant must be allocated to an appropriate **restricted fund**. If a grant has conditions such that the charity is only entitled to receive the grant subject to achieving specific outputs or service levels, it should be treated as a **performance-related grant**.

Gross up: In a **charity** context, the phrase 'to gross up' is mainly used in relation to Gift Aid **donations**. It involves converting the net value of a gift to the gross value including tax reclaimed. With income tax at 20%, the gross value of a gift is the net value plus 25% (see chapter 10).

Group accounts: In cases where a **charity** owns a **trading subsidiary** company (see page 281) or in a few rare cases where one charity is a subsidiary of another, there may be a legal requirement to prepare group accounts – accounts based on **consolidating** the figures from the **charity** and its subsidiary (or subsidiaries) together. The group accounts must generally be prepared in addition to the **individual accounts** for the separate entities – though often the group accounts and the individual accounts for the parent body are shown together in the same document, with columns headed 'Group' and 'Charity' respectively.

Heritage assets: See **fixed assets**.

His Majesty's Revenue and Customs (HMRC): The body responsible for assessment and collection of the vast majority of taxes in the UK (although Scottish devolved taxes are administered by Revenue Scotland).

Holding trustee: An **unincorporated charity** cannot hold property in the name of the **charity**, so holding trustees (also called custodian trustees) may be appointed to hold the legal title to property held for **charitable purposes**. In some cases, the holding trustees are the same individuals as the charity **trustees**, but it is common to appoint a smaller number of people who will hold the property on a long-term basis. The holding trustees must act on any properly taken decisions of the charity trustees with regard to the property. If a corporate body is appointed to hold property (for example, a larger charity structured as a **charitable company** or **CIO**), the term 'custodian trustee' is normally used.

Impairment: In **accruals accounting**, impairment is the process of reducing or 'writing down' the value of an **asset**, usually for exceptional reasons. It generally refers to a reduction in value in excess of the normal **depreciation** that would be charged – for example, if the asset has become out of date or damaged and has less potential for future use than previously anticipated.

Income and expenditure account: An income and expenditure account shows the different categories of income received by and expenditure paid by an organisation; these in turn determine the **surplus** or **deficit** for a particular period of time. It is a generic term often used by not-for-profit organisations instead of 'profit and loss account', more commonly used by commercial organisations. For **charities** that use **R&P accounting**, this is usually termed a **R&P account**. For charities that use **accruals accounting**, this will form the basis of the **SOFA.**

Incorporated charities: This term refers to **charities** which have 'legal personality' – in other words, charities which are recognised in law as persons in their own right. An incorporated charity can hold property in its own name and can sue or be sued in the courts. The main forms of incorporated charity include **CIOs**, **SCIOs**, **charitable companies** and charitable **CBSs**.

Independent examination: A less onerous form of scrutiny than an **audit**. Examiners report whether specific matters have come to their attention. It is carried out by an **independent examiner**. Independent examination is an option for most small and medium-sized charities if there is no requirement for a report by an **auditor**. There is a detailed legal framework for independent examination of accounts, with separate rules in each of the three UK **jurisdictions**. For some charities, the independent examiner must be professionally qualified, but in other cases, the **trustees**

can appoint anyone suitably independent of the charity to be an independent examiner, provided they are satisfied that the examiner has the necessary skills and experience for a competent examination. (See chapter 15 for details.)

Independent examiner: A person appointed to provide an independent report on the **annual accounts** of a **charity**.

Individual accounts: The accounts for a single **charity** or other entity (in contrast to **group accounts**).

Inflation: A general increase in prices leading to a fall in the purchasing value of money.

Intangible assets: See **fixed assets**.

Inter-fund transfer: An entry in the books of a **charity** recording a transfer of resources from one **fund** to another (expenditure of one fund which becomes income to another fund). With **accruals accounting**, inter-fund transfers appear on a special line on the **SOFA**. In most cases, where the resources of several funds are held in the same bank account, an inter-fund transfer is purely a book entry – it does not relate to any movement in the bank account. Where **restricted funds** are involved, inter-fund transfers must only be entered with appropriate authorisation within the relevant restrictions and they must therefore be explained by **notes to the account**s (this is mandatory with **accruals accounts** and good practice with **R&P accounts**).

Internal financial controls: Policies and procedures that minimise **risk** of financial loss from theft, fraud, human error, unforeseeable circumstances and even bad management decisions. They do not eliminate financial risk entirely, but they reduce it and act as an early warning sign to **trustees** to identify an issue and take action (see chapter 5).

Investment: An **asset** held by a **charity** with the expectation of a financial return. See **fixed assets**, **current assets** and **social investments**.

Investment income: Income to a **charity** from **investments** of any kind – for example, bank interest, share dividends or rental income from investment properties. (Note that capital growth on investments is *not* **investment income** but is shown on a separate part of the **SOFA** as an 'investment gain'; however, the presentation of gains and losses in investments is not directly covered in this book.)

Journal: A specialised entry in the accounts – an unusual **transaction** – which is more complex than those entered on a regular basis. In **double-entry bookkeeping**, a **journal** may involve a number of **debits and**

credits. In a computer-based accounting system, it is normally possible to enter a journal using any combination of debits and credits across different accounts. Journals are commonly used for entries such as salary payments (if split across multiple accounts, possibly with **creditors** for tax, National Insurance and pension amounts), **depreciation**, **capitalisation** of a **fixed asset** purchase which was initially entered as normal expenditure, recharging income or expenditure between projects or **funds**, and possibly for **inter-fund transfers**. Also, an accountant preparing a **charity's annual accounts** may identify journals needed in order to adjust figures from the charity's internal books to reach the figures needed for the final accounts – for example, if the **treasurer** or bookkeeper has not entered depreciation or has allocated some income to the wrong fund. However, it is essential that any journals proposed by an external accountant are referred back to the charity's treasurer or bookkeeper for approval (or for rejection if there was a misunderstanding) and so they can be recorded in the charity's own **accounting records** – otherwise the charity's books will not agree with the final accounts.

Jurisdiction: A country or territory where a particular legal system applies. In the UK, there are three jurisdictions each with a separate framework of **charity** law: England and Wales, Scotland and Northern Ireland.

Liability: An obligation which a **charity** has towards a third party, such as an amount due to a supplier which has not yet been paid (a **creditor**) or the outstanding balance on a loan made to the charity. A **liability** is the opposite of an **asset**. Liabilities are treated as having a negative value on the **balance sheet**, **SOAL** or **statement of balances**. Liabilities are deducted from the assets to give the net assets of the charity. They are usually divided into **current liabilities** and **long-term liabilities.**

Long-term liability: A **liability** for which a **charity** does not expect to have to make any payment until more than 12 months in the future – for example, the value outstanding on a mortgage where capital does not have to be repaid for several years. (However, if any part of the capital is due to be repaid in the next 12 months, that part of the mortgage should be treated as a **current liability**.)

Management accounts: Accounts which present financial information in a form for internal decision-making by **trustees** or managers (as opposed to **financial accounts**).

Material: With **accruals accounting**, estimates and judgements have to be made in determining the specific amounts to include in the accounts and deciding which amounts should be **recognised** (see **true and fair**

view). However, sometimes the relevant amounts are so small that it would make no material difference to the reader of the accounts which of the alternative approaches were used. For example, in a **charity** with an annual income of £400,000, it is immaterial whether an outstanding staff expense claim for £3.50 at year end is treated as a **creditor** or simply left to be treated as expenditure in the following year. **Auditors** and **independent examiners** are not required to report on minor concerns that something might have been wrongly classified in the accounts which would be immaterial to most readers of the accounts (although fundamental discrepancies such as missing **transactions** or suspected theft of charity funds would almost always be material no matter how small the amount). There is no fixed percentage for measuring what is material – a judgement must be made on what would be relevant to someone carefully reading the charity's accounts.

Merger accounting: An accounting treatment that is sometimes used when one **charity** merges into another. It involves combining all income, expenditure, **assets**, **liabilities** and **funds** of the old and new charities as if they had always been part of the same charity. The Charities **SORP** sets out the criteria for when merger accounting can be used. Strictly speaking, it is only permitted with **accruals accounting**, though the **charity regulators** have generally indicated that they are also willing to accept **R&P accounts** using the same principles (provided the merged charity still falls within the limits for use of the R&P basis).

Non-business use: This term is most commonly used in relation to VAT accounting (see chapter 9), especially with regard to buildings. Even if a building is used exclusively for **charitable purposes**, it will be classed for VAT purposes as 'business use' if most of the work undertaken is supported by **fees**, **contracts** or other **trading income**. For a building to be classed as 'non-business use', at least 95% of the work undertaken in the building must generally be funded by **donated income** or **investment income**. However, the interpretation of these terms and the apportionment of use can be complex, and it is usually worth seeking specialist advice.

Non-charitable trading income: See **trading for fundraising purposes**.

Non-profit (or not-for-profit): An organisation or activity which is not intended to make a profit. All **charities** are not-for-profit organisations, but the term also includes many other organisations in the public sector and **third sector**. A charity may well make a profit on a particular activity or **fundraising** event, or it may have a **trading subsidiary** that makes a profit. But it is never appropriate to speak about the profit of a charity as a whole. Where the income of a charity is more than the expenditure, the accounts will show a **surplus** to support the ongoing work of the charity.

Notes to the accounts: Information that is included as part of the **annual accounts** in addition to the **primary statements**. With Charities **SORP** accounts, the notes include all information additional to the **SOFA**, **balance sheet** and (where applicable) the **statement of cash flows**. In the case of **accruals accounts**, the regulations in each **jurisdiction** and/or the SORP require many specific **disclosures** to be made by way of notes (see chapter 14). In the case of **R&P accounts**, the requirement for notes is more limited (though still good practice). However, for Scottish **charity** accounts and with **CIOs** in England and Wales, a number of notes are required even with R&P accounts. (See chapter 13 for more details.)

Performance-related grant: A **grant** where the **charity** only becomes entitled to the income once particular services have been carried out. Often such grants are expressed in terms of an amount of grant that will be paid for each unit of work undertaken (for example, a grant of £X per client per night). Performance-related grants are frequently linked to **SLAs** specifying the precise services to be provided by the grant funding; however, care is needed to distinguish performance-related grants from **contract** funding.

Permanent endowment: See **endowment fund**.

Prepayment: A prepayment arises when a **charity** pays in advance for a cost which should only be recognised as expenditure in the year ahead. (It is the opposite of an **accrual** – see chapter 10 for further details.) Prepayments normally appear under the '**Debtors**' heading on the **balance sheet**.

Primary-purpose trading: **Trading income** is classed as being for the primary purpose of the **charity** where a charge or a **fee** is applied for services or goods which are directly provided as part of the charity's **charitable purposes**. Common examples include course fees charged by educational charities and sales of theatre tickets by performing arts charities. Trading which is not undertaken for the primary purpose must be treated as **trading for fundraising purposes**.

Primary statements: The key financial reports within a statement of accounts (as opposed to supporting information, which is provided in **notes to the accounts**). In the case of **accruals accounts** under the Charities **SORP**, the primary statements are the **SOFA** and the **balance**

sheet. With **R&P accounts**, the primary statements are the **R&P account** and the **SOAL** (or **statement of balances** in Scotland).

Professional fundraiser: Any person who carries on a **fundraising** business and charges fees to a **charity** for services involved in fundraising – for example, writing funding applications and/or carrying out fundraising on behalf of a charity. They are authorised by the charity to approach and contact **funders** and **donors** on the charity's behalf. See also the slightly different role of a **fundraising consultant**. Refer to page 144 for more information.

Public benefit requirement: To be a **charity**, an organisation must be established for public benefit (as well as having **charitable purposes** which fall within the specific legislation), but the precise definition and interpretation of the public benefit requirement vary slightly between England and Wales, Scotland and Northern Ireland. Key issues include whether or not the purposes (purposes) of the charity are inherently beneficial, and whether there are undue restrictions on who can benefit (the class of beneficiaries) – for example, if there are substantial charges to access the charity's services, a **charity regulator** may decide the public benefit requirement is not met. If a charity ceases to meet the public benefit requirement, it could lose its charitable status. **Trustee**s are required to consider the public benefit requirement in the decisions they make. In England and Wales and in Northern Ireland, this includes considering the specific public benefit guidance from CCEW or CCNI (see the further reading, on page 313), and the **trustees' annual report** must explain how the activities of the charity during the year were carried out for public benefit.

Purchase ledger: A record of a **charity's** purchases and all invoices received from suppliers, showing the date each invoice was received, the supplier to be paid, the amount due and when the invoice was paid. The list is often organised by supplier so you can tell at a glance how many purchases have been made from a particular supplier and when you need to pay them.

Qualified accounts/report: The accounts of a **charity** are said to be 'qualified' when the report of the **auditor** or **independent examiner** contains some reservations or qualifications – in other words, the auditor or examiner was unable to give a clean report on the accounts. (See chapter 15 for further details. Note that this term has nothing to do with the professional qualifications of the auditor or examiner.)

Receipts and payments (R&P) account: One of the two **primary statements** (the other is the **SOAL** or **statement of**

balances) in any set of **charity** accounts prepared on the **R&P accounting** basis. The R&P account shows the various categories of receipts and payments, normally over a 12-month period. Where the charity has multiple **funds**, the accounts must either provide a separate R&P account for each fund or use multiple columns to distinguish the funds (as with a **SOFA** in **accruals accounting**). In Scotland, the categories to be used in the R&P account are specified in the Charities Accounts (Scotland) Regulations 2006. In England and Wales and in Northern Ireland, there is no prescribed format for an R&P account, but CCEW and CCNI both publish guidance (see the further reading, on page 313). Refer to chapter 13 for more details.

Receipts and payments (R&P) accounting: **Charity** accounts prepared on the R&P basis (sometimes called the 'cash basis') just show money received and paid out in the main **R&P account**. However, accounts on this basis must also contain a **SOAL** (in England and Wales and in Northern Ireland) or **statement of balances** (in Scotland). This is contrasted with **accruals accounting**, which shows income earned and expenses incurred. Charity accounts on the R&P basis are *not* subject to the accounting requirements of the Charities **SORP** and do not generally give a **true and fair view** even though they should be factually correct. (However, even when using the R&P basis, the **financial statements** must normally include a **trustees' annual report**, and the SORP guidance may be useful for that.)

Receipts and payments (R&P) accounts: The term used to refer to the **annual accounts** as a whole when made under **R&P accounting**.

Recognition (of income or expenses): With **accruals accounting**, recognition involves deciding the point in time when a **charity** is entitled to certain income or liable for certain expenditure, which therefore determines the financial year in which the income or expense should be included. With a simple **donation**, recognition occurs at the time the gift is made. However, with more complex items, there can be considerable debate – for example, with legacy income where a person has died leaving part of their estate to charity but it is unclear when the charity will receive the legacy or the amount is uncertain. Similarly, the recognition of expenditure involves policy decisions, such as the period of **depreciation** for the various types of **fixed asset**.

Reducing balance method: A method of calculating **depreciation** to reflect that **assets** may be used more in early than later years. A fixed percentage is applied to the assets' declining value each year rather than to the original cost (as in **straight line depreciation**). This means a higher depreciation charge is calculated in year one than year three, for example.

Register of members: Where a **CIO** or **SCIO** has members and charity **trustees**, it must keep a register of members to record names, addresses, category of membership, the date a person (or organisation) became a member and the date of ceasing to be a member (where applicable). DSC's publication *Charitable Incorporated Organisations* has more information (see the further reading, on page 313).

Registered charity: A **charity** which is registered with the relevant **charity regulator** (CCEW, OSCR or CCNI) and allocated a registered charity number. (Note that not all charities are registered, and for some charities dual registration applies – see chapter 1.)

Reserves: The reserves of a **charity** are the resources available at a given point in time that could be spent at the **trustees**' discretion on the short-term work of the charity (without, for example, selling **assets** which are essential to the charity's activities and without approaching **funders** for permission to use **restricted funds** outside the terms on which they were given). The reserves figure is normally therefore calculated as the balance of **unrestricted funds** less any tangible **fixed assets** that form part of the unrestricted funds. Where part of the unrestricted funds comprises **designated funds**, these are usually also excluded if they incorporate amounts set aside for specific future expenditure which the trustees consider fundamental to the long-term sustainability of the charity's work.

Reserves policy: A policy set by the charity **trustees** for the level of **reserves** they consider to be needed. The reserves policy must be stated (even by small **charities**) in the **trustees' annual report**. It is often expressed in terms of a number of months: the period of time for which the trustees consider the charity should be able to survive even if all income suddenly ceased.

Restricted fund: A **fund** where there is some external condition (beyond any imposed by the **trustees**) on how the fund can be used. The condition could arise either because the **charity** invited **grants** or **donations** for a specific purpose or because a **funder** or **donor** imposed an explicit condition. Strictly speaking the term 'restricted fund' can refer to either a **restricted income fund** or an **endowment fund** (but, in most cases, it refers to the former).

Restricted income fund: The official name for a normal **restricted fund**, where the income can be spent (within the terms of the restriction), as opposed to an **endowment fund**, where the **fund** itself cannot normally be spent.

Risk: A risk, technically speaking, is the uncertainty arising from a particular situation. This can result in either a favourable or an unfavourable result. In terms of the risks that **trustees** should manage, this book usually means those that would cause an adverse impact on the **charity** and its resources.

Risk register: A tool used to record, assess and note steps to mitigate **risks** that a **charity** may face (see chapter 5).

Sales ledger: For a trading charity, a record of a **charity's** sales and all invoices raised, showing the date the invoice was generated, the customer, the amount due and the date the payment was received. The list is often organised by customer so you can tell at a glance how many sales have been made to a particular customer and if they owe any money to your charity.

Scottish charitable incorporated organisation (SCIO): A **CIO** that is **incorporated** under Scottish **charity** law and registered with OSCR. (However, the legal framework for SCIOs has a number of important differences from that for **CIOs** in England and Wales, which will be registered with CCEW.)

Section 167 Register: A register to be maintained by CCNI of external **charities** operating in Northern Ireland. The legal basis of the register is section 167 of the Charities Act (Northern Ireland) 2008. However, at the time of writing, the Section 167 Register is not yet in operation.

Serious incident: All three **charity regulators** describe this as something that has a significant impact on a **charity** when it happens. It is not limited to financial impact, and the significance will depend on the size of the charity. It is up to the **trustees** to decide whether or not the event is serious enough to report to the appropriate charity regulator(s). Your **auditor** or **independent examiner** also has a duty to report matters of material significance to the appropriate regulator(s). (A serious incident is referred to as 'notifiable event' in Scotland.)

Service level agreement (SLA): An agreement with a funding body on the level of service to be provided by a **charity** as a condition of the relevant funding. Note that an SLA is not itself a funding agreement (so you cannot say 'we are funded by an SLA'), but either a **grant** agreement or a **contract** for services could incorporate an SLA as one of the conditions. (Sometimes the funding agreement begins with the SLA, and the grant or contract funding is only mentioned at the end.)

Settlor: The initial **donor** who makes a gift of money or property, creating a new **charitable trust**.

Social investment: An **investment** made by a **charity** which is not expected to give a commercial return but where the making of the investment will support the **charity's purposes**, and hence the **trustees** agree it is appropriate to accept a lower return than with a conventional investment. A charity can also be the recipient of a social investment.

Statement of assets and liabilities (SOAL): In a set of **charity** accounts prepared on the **R&P** basis in England and Wales and in Northern Ireland, the SOAL provides a list of the **assets** and **liabilities** of the charity at year end. In the SOAL, bank balances should be reconciled to the **fund** balances (from the **R&P account**) and other assets and liabilities should then also be listed: for example, **fixed assets**, **debtors** and **creditors**. In Scotland, the equivalent is a **statement of balances**. (See chapter 13.)

Statement of balances: The equivalent of a **SOAL** in **R&P accounting** by Scottish **charities**. The categories to be used in the statement of balances are specified in the Charities Accounts (Scotland) Regulations 2006.

Statement of cash flows: In a set of **charity** accounts prepared on the **accruals accounting** basis, a statement of cash flows shows the movements of money (cash) through the charity over the financial year. It forms an additional statement, usually presented immediately after the **SOFA** and **balance sheet**. For charities following the Charities **SORP** (**FRS 102**), a statement of cash flows is required if they have an annual income of more than £500,000 (below this level it is optional).

Statement of financial activities (SOFA): One of the two **primary statements** (the other is the **balance sheet**) in any set of **charity** accounts prepared on the **accruals accounting** basis. The SOFA shows the income and expenditure, normally over a 12-month period, broken down into columns for **unrestricted**, **restricted** and **endowment fund**s, totalled to a final balance at year end on each type of **fund**. The SOFA may also show **inter-fund transfers** and other gains and losses. The required format for the SOFA is set out in the Charities **SORP**. (See chapter 13.)

Statement of Recommended Practice on Accounting and Reporting by Charities (SORP): The SORP is the **accounting standard** which explains how **charities** preparing **accruals accounts** should set out their **financial statements**, including the **SOFA**, **balance sheet**, **statement of cash flows** (if applicable), **notes to the**

accounts and **trustees' annual report**. The current version is the **Charities SORP**: *Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102)*. See also **accounting standards.**

Straight line depreciation: A method used to spread the cost of an **asset** equally over its **useful life** and show that the value of the asset its reduced over the time it is held. In this method, equal amounts are charged in each year as expenditure over the life of the asset, based on the asset's cost, and likewise equal amounts are deducted from the value of the asset.

Surplus: A surplus arises when a **charity's** income was more than the expenditure in a given year – either for a particular **fund** or for the charity as a whole.

Tangible assets: See **fixed assets**.

Third sector: An umbrella term often used to cover those organisations that do not fit into the commercial (private) sector or public sector. The **third sector** includes **charities** and other voluntary or **non-profit** organisations.

Total return: A specific method of **charity** investing (usually in relation to a **permanent endowment fund**) where both the capital growth and the **investment income** are considered together to determine the amount available for charitable expenditure. In England and Wales, the **trustees** can adopt such an approach under the Charities Act 2011 (as amended by the Charities Act 2022), subject to compliance with CCEW regulations and guidance (see, in particular, the 'Total return investment for permanently endowed charities' guidance). (The details of total return investing are outside the scope of this book, but chapter 6 provides further explanation of the principles.)

Trading by beneficiaries: A charitable trade carried out mainly by the **charity's** service users in accordance with its objects.

Trading for fundraising purposes: When a **charity** sells goods or services in order to raise funds, the activity is classed as trading for fundraising purposes (as opposed to **primary-purpose trading**). Trading for fundraising purposes (also known as non-charitable trading income) includes sales of tickets for **fundraising** events, sales of gifts and souvenirs, sales of refreshments or donated goods purely to raise funds, and sales of the charity's core services where they are not being purchased on behalf of beneficiaries, such as a charity renting out its training room to a commercial business. Charities are allowed limited concessions regarding trading for fundraising purposes (see chapter 9), but, beyond those limits, the profits of the activity may be taxable.

Trading income: **Charity** income which arises from making some kind of charge for a product or service (as opposed to **donated income** and **investment income**). Trading income is divided into that which derives from **primary-purpose trading** and that which derives from **trading for fundraising purposes.**

Trading subsidiary: A non-**charitable company** established as subsidiary of a **charity**, normally to undertake **trading for fundraising purposes** (i.e. non-charitable trading) which would be taxable if it were undertaken by the charity itself (see chapters 8 and 9). The profits of the trading subsidiary are donated back to the charity.

Transaction: A financial event requiring an entry in the books of a **charity**, such as a receipt, a payment, receiving or issuing an invoice (this is still a **transaction** even if it will not be paid immediately), **depreciating** a **fixed asset**, posting an **inter-fund transfer**, or recording a **prepayment** or an **accrual.**

Treasurer: The person, normally a **trustee**, who takes the lead on financial matters within a **charity**. This will typically include taking the lead on any recommendations to trustees with regard to accounting procedures, **budgets**, and **annual accounts**; communicating on behalf of the trustees with the **auditors** or **independent examiner**; and generally supporting the trustees with all decisions of a financial nature. However, the treasurer has no power to make financial decisions alone: all decisions are for the trustees as a whole (or for staff where the trustees have authorised them to make decisions within pre-agreed budgets). In a very small charity, the treasurer's role may also include the day-to-day **bookkeeping**, payment of bills and so on (see the discussion on page 29).

Trial balance: In **double-entry bookkeeping**, at the end of each **accounting period**, after each account is **closed off** a list is prepared of every account showing its final debit or credit balance. This is called a 'trial balance'. Because the **debits and credits** on every **transaction** should balance, the total of the debits and credits across the whole **charity** should balance – if not, there has been an error in the double-entry recording of transactions. (In a computer-based accounting system, the trial balance is generated automatically and, unless there has been a malfunction in the system, the debits and credits will always balance.) The trial balance is often used as the starting point for preparing the **SOFA** and **balance sheet** in the **annual accounts**. A simple trial balance just has three columns, with the name of each account, a column for debit balances and a column for credit balances. However, it can be helpful to prepare an 'extended trial balance' where, rather than just having debit and credit columns, the account balances are allocated to various columns according to where they will appear in the final accounts.

True and fair view: Where **accruals accounting** is used, the aim is always for the final accounts to give a true and fair view of the financial strength of the **charity** in terms of its income, expenditure, **assets** and **liabilities**. For this to be possible, suitable **accounting policies** must be chosen to deal with issues such as **recognition** of income and expenditure, **depreciation of fixed assets**, and valuation of assets and liabilities, so that all **material** figures in the **financial statements** are meaningful and appropriate. It is also essential that all figures from the books are properly categorised on the **SOFA** and **balance sheet** (including analysis between different **funds**). However, simply presenting a SOFA and balance sheet on their own would not be sufficient to give a true and fair view: **notes to the accounts** are also needed to allow the reader to understand the breakdown of major figures and the accounting policies used, and to disclose details such as **transactions** with charity **trustees**. Compliance with relevant **accounting standards** (in particular, the Charities **SORP**) is generally considered to be a fundamental requirement for accounts to give a true and fair view. **Auditors** will state whether in their opinion the accounts give a true and fair view (but this is not part of the duties of an **independent examiner**, although an independent examiner must still review the accounting policies and the presentation of the accounts and state if any concerns have arisen). However, the responsibility for ensuring the accounts give a true and fair view rests with the charity trustees – *not* with the charity's **auditor** or **independent examiner**. (See page 259 for more on the principles.)

Trust deed: The usual **governing document** of a **charitable trust** (or the document may be called a 'declaration of trust').

Trustees: The people charged with the **governance** of a **charity**. Some charities use other terms, such as 'committee members', 'directors' or 'members of the council'. However, in law, those who have the authority to make formal decisions on behalf of the charity are charity trustees (whether or not that term is used) and thus have duties in relation to charity accounting as explained in this book. The **treasurer** is normally one of the trustees, but decisions must be taken by the trustees collectively. (Note that some charities have **holding trustees** (also called custodian trustees) as well as charity trustees.)

Trustees' annual report: The annual report of the charity **trustees**, which for most **charities** must accompany the **annual**

accounts in order to provide a full set of **financial statements**. The report will include legal and administrative information such as the charity's name and **charitable purposes**, details of the **governing document** and the names of the trustees who served during the year. It must also include a report on the work of the charity during the year (taking account of the **public benefit requirement**) and details of key policies set by the trustees – in particular, a **reserves policy**. The precise requirements vary between England and Wales, Scotland, and Northern Ireland, and between smaller and larger charities. (See chapter 12.)

Unincorporated charity: A **charity** which does not have its own 'legal personality' – in other words, the charity only exists by virtue of individual **trustees** coming together. Any property must be held in the names of the individual trustees (or possibly in the names of **holding trustees**) and any agreements are made by the trustees as individuals (so they do not have the benefit of limited **liability** in the event of a dispute). The main forms of unincorporated charity are **charitable trust** and **charitable association**.

Unqualified accounts/report: **Charity** accounts where the report of the **auditor** or **independent examiner** contained no qualifications or reservations in the wording – in other words, accounts with a clean **audit** or **independent examination** report which raised no concerns. All charities subject to audit or independent examination should aim for an unqualified report on their accounts. (See chapter 15.)

Unrestricted fund: A **fund** which has no external restrictions. The **trustees** can use the resources of the fund as they consider most appropriate to support their **charitable purposes**. Unrestricted funds can include a **general fund** and possibly also **designated funds**.

Useful life: A term used in relation to **fixed assets** and **depreciation**. The useful life of an **asset** (such as equipment, furniture or a building) is the estimated period for which it is expected to be functional and used by the **charity** in carrying out its operations.

Variance analysis: The process of determining the differences between two sets of figures, such as the actual and **budget** figures (a **budget variance**), and analysing and establishing an explanation for why there is a difference. (See chapter 6.)

Write off: An often-used accounting term which effectively means to eliminate an **asset** from accounts and to reflect the cost of doing so. Instead of being shown as an asset, the item is recorded as an expense. Two common examples are writing off a debt, when it is agreed that it is no longer possible to claim the money back from a customer, and writing off the value of a **fixed asset**. In this case, this could be because the cost of the asset was very small, under the **capitalisation limit**, or because the asset is being disposed of.

Zero-based budgeting: The process of preparing a **charity's budget** where nothing is based on the previous year – all budgets are set from first principles (in effect, starting from zero).

Index

Page numbers in *italics* refer to figures and illustrations and in **bold** refer to tables.

KEY GUIDES

The Charity Treasurer's Handbook

Steering a charity's finances can be one of the most challenging roles you'll face in the sector – not least because your aim is to help a charity fulfil its purpose, and charity finance rules are very different from those of business.

This established guide offers you the perfect foundation for being a treasurer or finance officer even if you are new to charity finance. Covering charity accounting across all four nations of the UK, this sixth edition will help you swiftly gain confidence and knowledge. Comprehensively revised and expanded by new lead author Elaine Alsop, it includes:

- Current legal and accountancy practice for charities across the UK
- Annual reporting and charity accounts including compliance with Charities SORP
- Corporation tax and VAT for charities: what you should be aware of
- Gift Aid: the benefits and how to get started
- Fund accounting and reserves
- Guidance for effective financial planning and management
- Introduction to risk and controls

With plenty of helpful examples, this guide is suitable for treasurers, finance officers and voluntary sector workers with little or no accounting experience.

It is also a vital guide for trustees and charity managers, which will help them understand their own role, that of the staff they oversee, and the charity's relationship with the external auditor or independent examiner.

'This plain-English guide will help trustees and managers navigate their way through the myriad of issues that any charity is likely to face. It will help them to make informed decisions, stay compliant and be more effective.'

Simon Bostrom FCIE, Chief Accountant,
West Yorkshire Community Accountancy Service CIO

ISBN 978-1-78482-089-3

9 781784 820893

www.dsc.org.uk