

# Charity Accounting Webinar

Ken Brew

AAT is a registered charity. No. 1050724

aat

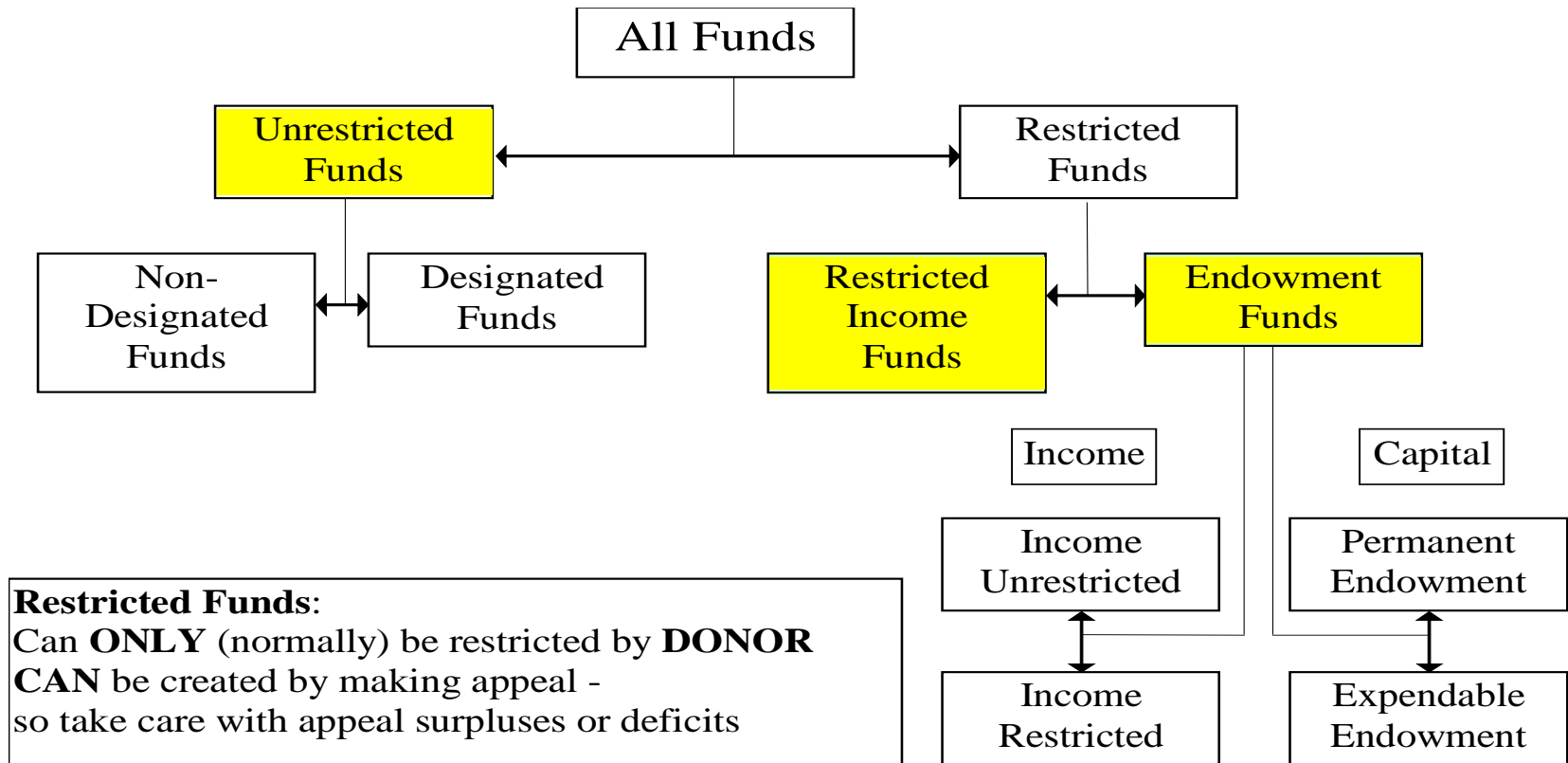
# What's new in the SORPs?

Ken Brew

AAT is a registered charity. No. 1050724

aat

# The Fund Framework



# Proposed Accounts requirements England and Wales (excludes CIOs)

Income	≤ £10k	£10k- £25k	£25k-£250k	£250k- £500k	£500k
Accounts	Cash basis (non-company) Accruals basis (company)			Accruals basis	
				Simpler?	Full
Trustees' annual report	Simple				Full
Scrutiny	None		Independent Examination*		Independent Audit
			Independent Person	Qualified Accountant	
Report to regulator	Update form	Simple return, report and accounts			Return, report & accounts

If Income >£250k and assets >£3.26m audit required. Company charities may have IE.



# SoRP Consultation - Modules

- Modular approach
- “Pick and mix” online
- 29 Modules
  - 14 Core
  - 3 Special transactions (including grant making)
  - 2 Types of assets (Heritage and Acting as Custodian)
  - 3 Investments  
(Total Return, Pooling, Social investment)
  - 7 Group Accounts

# Charities SoRP 14 Core Modules

Statements	Underlying concepts	Accounting Treatments for Charities
1. Trustees' Annual Report	3. Accounting Standards, policies, concepts and principles...	8. Allocating costs by activity within SoFA
4. SoFA	5. Recognition of Income	6. Donated goods and services
10. Balance Sheet	7. Recognition of expenditure	9. Disclosure of trustee and staff remuneration
14. Statement of Cash Flows	11. Accounting for financial assets and liabilities	13. Events since the year end
2. Fund Accounting	12. Impairment of assets	

# Charities SoRP -15 “Special” Modules

Charity Operations	Types of Asset and investments	Branches, groups and Combinations
15. Charities and company law	18. Heritage Assets	23. Combinations overview
16. Presentation of Grant making	19. Custodian Trustee	24. Accounting for Groups
17. Retirement and post- employment benefits	20 Total Return on Investments	25. Branches and Joint arrangements
	21. Social Investments	26. Subsidiaries
	22. Pooling Investment Funds	27. Mergers 28. Associates 29. Joint ventures

# SoRP Consistent Terminology

**MUST**

- Compliance necessary in order to show “a true and fair view”
- Non-adherence is a departure from the SoRP

**SHOULD**

- Good practice
- Not a departure from the SoRP

**MAY**

- Optional
- Indicates that there are alternative approaches available

# Changes to the Trustees' Annual Report (all charities)

- Common format – whether FRSSE or FRS 102 or cash accounting
- Distinguishes requirements of all charities from those of 'larger' charities (those subject to statutory audit) as a separate section
- Main changes to content requirements for all charities are:
  - All trustees must be listed
  - Must disclose if no reserves policy with reasons

# Changes to the Trustees' Annual Report (larger charities)

- Main changes to content requirements for larger charities are **explanations** of:
  - Social investment policies
  - Financial effect of significant events
  - Principal risks and uncertainties and a summary of plans and strategies for managing them
  - Reserves definition – (use SORP or explain your own)
  - Arrangements for setting pay of key management personnel and any benchmarks, criteria or parameters used

# Module 1 TAR Reserves

Paragraphs 1:22 and 1:48

**MUST**

- Explain any policy for holding reserves
- State the amount of reserves and why they are held
- If decided not to hold reserves, disclose fact and explain

**SHOULD**

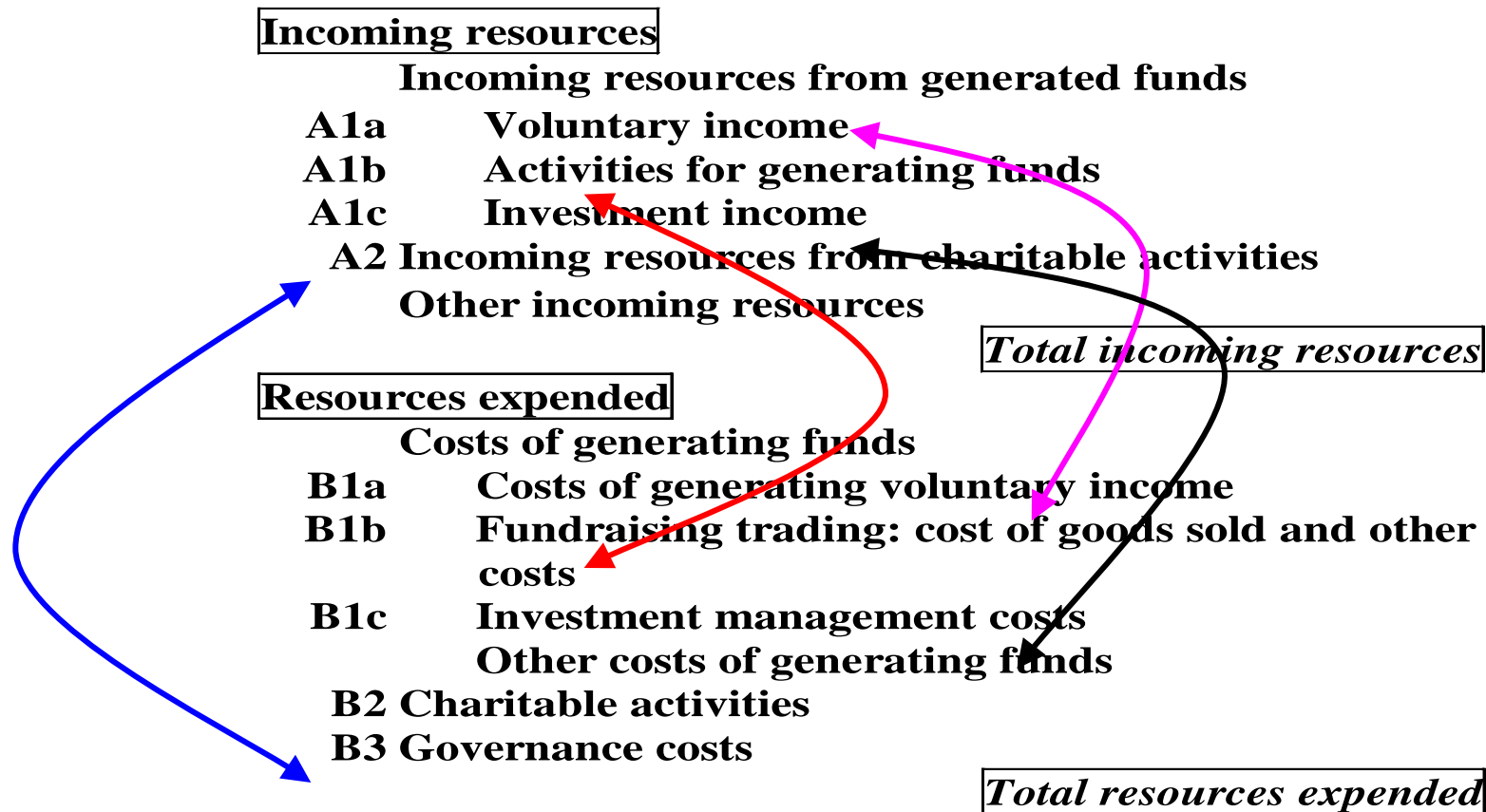
- State total funds at the end of the period
- Identify restricted or fixed assets or programme related investments
- Identify and explain designated funds and timing of spend
- Calculate the amount of reserves at the end of the period
- Compare this with the reserves policy and provide explanations of how it will be brought into line in future

# Trustees' Annual Report

Reserves are charity's **freely available income funds**

Definition normally <b>excludes</b>	<b>Permanent endowment funds</b>
	<b>Expendable endowment funds</b>
	<b>Restricted funds</b>
<b>And</b> unrestricted funds not readily available for spending	Funds only available by disposing of: <ul style="list-style-type: none"><li>■ <b>Fixed assets for charity use</b></li><li>■ <b>Programme related investments</b></li></ul>
<b>But</b> charities may have more or less reserves available e.g..	<b>Expendable endowments</b>
	<b>Unrestricted funds earmarked or designated for essential spending</b>

# Statement of Financial Activities per SoRP 2005





# New Charities SoRPs – SoFA changes

## **Statement of financial activities (SOFA)**

- The income and expenditure headings in the SOFA have been changed and simplified.
- New heading “cost of raising funds” and
- governance costs are not shown separately on the face of the SOFA but are treated as a component of support costs.
- Investment gains and losses now counted as a component of net incoming resources / resources expended.

# Structure of the SoFA

	Unrestricted funds	Restricted funds	Endowment funds	Total funds	Prior period total funds
	£	£	£	£	£
<b>Income and endowments from:</b>					
Donations and legacies					
I from Charitable activities					
Other trading activities					
I from Investments					
Other					
<b>Total Income and Endowments</b>					
<b>Expenditure on:</b>					
Raising funds					
Charitable activities					
Other					
<b>Total Expenditure</b>					
<b>Net gains/(losses) on investments</b>					
<b>Net income (expenditure)</b>					

# Main changes – SoFAs compared

2005 SORP (SoFA extract)		FRSSE SORP (SoFA extract)		FRS 102 SORP (SoFA extract)
Voluntary income	→	Donations and legacies		Donations and legacies
Activities for generating funds	→	Other trading activities		Other trading activities
Investment income	→	<i>Income from</i> Investments		<i>Income from</i> Investments
Incoming resources from charitable activities	→	<i>Income from</i> Charitable activities		<i>Income from</i> Charitable activities
Other incoming resources	→	<i>Other income</i>		<i>Other income</i>
Total incoming resources	→	Total income and endowments		Total income and endowments
Costs of generating voluntary income	→	<i>Expenditure on</i> Raising funds		<i>Expenditure on</i> Raising funds
Fundraising trading: cost of goods sold and other costs	↗			
Investment management costs	↗			
<i>Resources expended on</i> Charitable activities	→	<i>Expenditure on</i> Charitable activities		<i>Expenditure on</i> Charitable activities
Governance costs	→			
Other resources expended	→	<i>Other expenditure</i>		<i>Other expenditure</i>
				Net gains/(losses) on investments
Net incoming/outgoing resources before transfers	→	Net income/(expenditure)		Net income/(expenditure)
Gross transfers between funds	→	Transfers between funds		Transfers between funds
Gains on revaluation of fixed assets for charity's own use	→	Gains/(losses) on revaluation of fixed assets		Gains/(losses) on revaluation of fixed assets
Gains/losses on investment assets	→	Gains/(losses) on investment assets		
Actuarial gains/losses on defined benefit pension schemes	→	Actuarial gains/(losses) on defined benefit pension schemes		Actuarial gains/(losses) on defined benefit pension schemes
				Other gains/(losses)
Net movement in funds	→	Net movement in funds		Net movement in funds



# Income Recognition

- Income is recognised in the Statement of Financial Activities (SoFA) when a transaction or other event results in an increase in the charity's assets or a reduction in its liabilities.



# Income Recognition

- Income must only be recognised in the accounts of a charity when all of the following criteria are met:
  - **Entitlement** – control over the rights or other access to the economic benefit has passed to the charity.
  - **Probable** – it is more likely than not that the economic benefits will flow to the charity.
  - **Measurement** – the monetary value or amount of the income or costs can be measured reliably.

# Income Recognition Legacies

## ENTITLEMENT

- Know of the existence of a valid Will AND
- Know about the death of the benefactor

## TO RECOGNISE INCOME

- MUST show ENTITLEMENT PLUS
- “PROBABILITY of receipt” PLUS
- Ability to ESTIMATE with sufficient ACCURACY the amount receivable

## RECEIPT PROBABLE when

- There has been Grant of Probate AND
- Executors have established that there are sufficient assets in the Estate AND
- Any conditions attached are within the control of the charity or have been met

# Income Recognition : Legacies (cont).

- Payment is received or notified after the reporting date and before accounts are authorised BUT payment was agreed by the executors prior to the end of the reporting period., THEN treat as **adjusting event** and accrue it as income. Always use **fair value**.
- If charity has entitlement but the **amount** is uncertain then disclose as a **contingent asset**
- **Large** charities may use a **portfolio** approach
- If to be received > 12 months from the reporting date then **discounting** can be used but unwind against legacy income.
- If there is **impairment** then make the adjustment between income (not expenditure) and debtors.



# New definition – “De facto” trustee

- **De facto trustee** is a person who has not been validly appointed as a trustee but
  - is acting as the trustee of the charity and is exercising the functions that could only be properly discharged by a trustee. This may have come about due to an error, omission or oversight in the appointment process of that trustee.
- May also be known as a de facto director.
- Key point is that they are included in disclosure requirements for Trustee and Staff remuneration



# UK Retail Gift Aid System

- Charity selling goods for third parties are
- Legally acting as agent...entitled to commission only
- Until donor waives repayment...then a donation (GA!)
- All handled under “Income from other trading”
- Large charities may use estimation techniques
- Income from FAIR VALUE of donated goods recognised when sold....
- Or in two stages received (if FAIR VALUE ESTIMATION is possible) and then when sold

# New definition of Related Parties

- A. any trustee and custodian trustee
- B. the donor of any land to the charity (on or after establishment; and
- C. any person who is:
  - 1. a child, parent, grandchild, grandparent, brother or sister of trustee (A) or land donor (B)
  - 2. an officer, agent or a member of the key management personnel of the charity;
  - 3. the spouse or civil partner of any of the above persons (A, B, C1 and C2);
  - 4. carrying on business in partnership with any of the above persons (A, B, C1, C2 and C3);
  - 5. a person, or a close member of that person's family, with control or joint control over the charity
  - 6. a person, or a close member of that person's family, with significant influence over the charity
- 'Close member of a person's family' refers to:
  - a. that person's children or spouse;
  - b. the children, stepchildren or illegitimate children of that person's spouse or domestic partner;
  - c. dependents of that person; and
  - d. that person's domestic partner who lives with them as husband or wife or in an equivalent same-sex relationship.

# Related Parties disclosures.....

- the description of a **relationship** between the parties
- (including the interest of the related party or parties in the transaction);
- a description of the transaction(s);
- the **amounts** involved;
- outstanding BALANCES with related parties and provisions for doubtful debts;
- any amounts written off from such balances during the reporting period;
- the terms and conditions, including any security and the nature of the consideration to be provided in settlement;
- details of any guarantees given or received; and
- **Any other** elements of the transactions which are necessary for the understanding of the accounts; and
- **this SORP requires** the disclosure of the **name(s)** of the transacting related party or parties.



## Related Parties (cont.)

- The reporting charity must not state that related party transactions were made at open market value or on terms equivalent to those that prevail in arm's length transactions unless such terms can be substantiated.
- If there have been no related party transactions in the reporting period that require disclosure, **this SORP requires** that this fact must be stated.



# Employee and Trustee Remuneration

- Important to show that the charity is operating for the public benefit and trustees are acting in the interests of their charity and not for private benefit.
- For this reason, this SORP requires that disclosure must be made of transactions involving trustees, related parties, staff remuneration and ex-gratia payments.
- The payments made to the auditor or independent examiner must also be disclosed.



# Paying Trustees?

- A transaction involving a trustee or other related party must always be regarded as material regardless of its size.
- Must make the same disclosures for de- facto trustees.

Most trustees are volunteers however,

- provided the arrangement is legally authorised, a trustee may be remunerated for their role as a trustee.
- On occasions, a trustee may also be employed in some other role, by the charity or a related entity.

# Trustee payments disclosure

**MUST**

- SORP requires Accounting Note that EITHER

**None**

**One or  
more**

- of the trustees have been paid any remuneration or received any other benefits from an employment with their charity or a related entity; or

# Payments to trustees

MUST show

- for each individual trustee who received remuneration or other benefits show

LEGAL AUTHORITY

TRUSTEE NAME

REASON FOR  
PAYMENT

AMOUNT

- remuneration, pension contribution or any other benefit

MAY show

- distinguish between as trustee and other services



# All charities MUST disclose

- the fact that there are no employees who received employee benefits (excluding employer pension costs) of more than £60,000 (€70,000); OR
- the number of employees whose total employee benefits (excluding employer pension costs) for the reporting period fell within each band of £10,000 (€10,000) from £60,000 (€70,000) upwards.

# FRS102 “Key Management Personnel” trustees and senior employees

**MUST**

- disclose the total amount of any employee benefits received by trustees and its other key management personnel

**SHOULD**

- give consideration to the information needs of their funders and other stakeholders in making their accounting disclosures.
- E.g. Chief Executive Officer or highest paid staff member,

**MAY**

- Disclose the amount of employee benefits paid to its key management personnel on an individual basis.



# Social investment

- ‘Social investments’ are either programme related and mixed motive investments (new category)
- Programme related investments are held to further the charitable purposes of the investing charity. There may be a financial return but it is incidental
- Mixed motive investments are a form of social investment made in part to further the charitable purposes of the investing charity and in part to generate a financial return.



# Accounting for social investments

- To account for the investment or contractual arrangement correctly, a charity needs to be able to identify:
- the nature of the asset or entitlement to income acquired;
- the basis upon which any financial return is calculated;
- the method(s) to be used to measure financial return;
- the nature of any liabilities or obligations acquired;
- the method(s) to be used to measure any liability or obligation; and
- their motive(s) for acquiring the investment.

# Total Return Approach to investment

Original  
endowment plus  
subsequent  
capital gifts

- Needs GD authority
- Needs CC permission
- HC amounts ring-fenced?

Unapplied total  
return

- Cumulative returns on investments
- Less previous transfers to income
- Record keeping is a challenge
- Evolved by CC since 2002



# Heritage Assets



## Module 18

- A heritage asset is a tangible or intangible asset with historical, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture.



# Attributes of a Heritage asset

- An asset may have the attributes of a heritage asset, e.g. be of historic or artistic importance, but unless
- It is **ALSO** held and maintained for its contribution to knowledge and culture then it will not fall within the definition of a heritage asset.



# Examples of (Non) Heritage Assets

- Assets with heritage attributes
- may be used operationally for other purposes unconnected with the promotion of knowledge and culture. In such instances, the asset is accounted for within tangible fixed assets or investments as appropriate.

## Examples:

- A historic building used by an educational establishment
  - Attributes not heritage
- Museum or gallery
  - collections held – Heritage
  - buildings or display cases – not usually heritage
- Works of art or historic buildings
  - Investments not usually heritage



# Heritage Assets

- Charities that do not have preservation or conservation purposes should account for an asset as a heritage asset only if that asset:
  - has historic, artistic, scientific, technological, geophysical or environmental qualities;
  - contributes to knowledge and culture through its retention and use; and
  - is accessible to the public for viewing and/or research.



# Heritage Asset - Disclosure

- Heritage assets are shown in a separate category
- Shown at cost or FAIR VALUE
- Charities are not required to recognise heritage assets on the balance sheet if
  - information on their cost or valuation is not available and such information cannot be obtained at a cost commensurate with the benefit to the users of the accounts and to the charity.

# The SoRPs in their context

Ken Brew

AAT is a registered charity. No. 1050724

aat



# Why is charity accounting changing?

- UK Generally accepted accounting Practice (GAAP) is changing from 1/1/2015
- New GAAP requires a new SORP
- SORP consultation in 2013 with 26 events, 1600 participants and 179 responses
- New SORPs take effect for financial years beginning on or after 1 January 2015
- New regulations required

# Why 2 SORPs?

- A separate FRS 102 SORP and a separate FRSSE SORP
- Trustees need to make the choice
- Why 2 SORPs? Because:
  - EU accounting Directive (mandatory from 2016) changes small company reporting and FRSSE
  - A new “FRSSE” framework needed in 2015-16
  - FRED59 published February 2015 small companies and other amendments
  - 2 SORPs avoids disruption to FRS 102 users
  - 2 SORPs simplifies the text of each

# What does SORP mean by a larger charity?

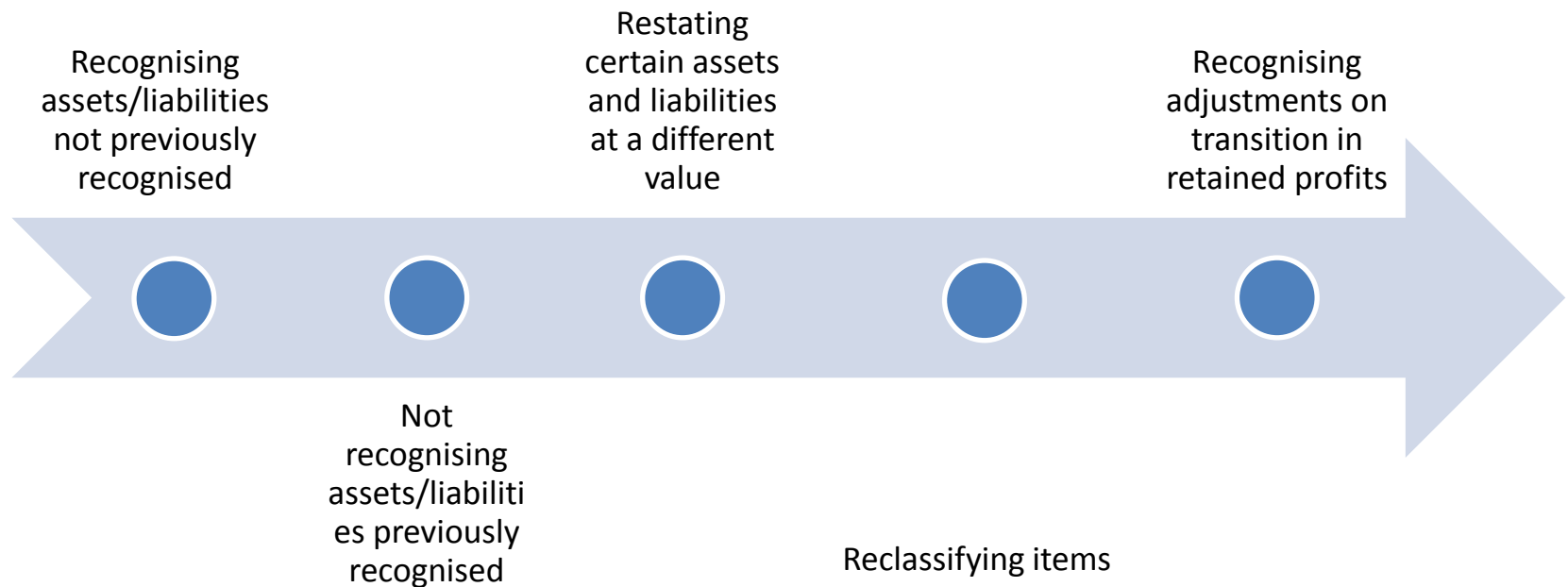
- Definition is based on the charity audit requirements of:
  - Gross income exceeds £500,000 or
  - Gross income exceeds £250,000 and total assets exceed £3.26m
- Charities subject to audit are 'larger charities' and more is required of them by the charities SORP
- Charities not subject to audit are 'smaller charities' which have a baseline of reporting under the SORP



# Proposed changes on Large charities

- Hodgson Report recommendation to raise the audit threshold
- Government consultation Dec14/Jan15
- From 1 April 2015 the plan is to raise threshold to
  - Gross income exceeds £1,000,000 or
  - Gross income exceeds £500,000 and total assets exceed £3.26 m
  - Retain £250,000 threshold for qualified person to be the IE
  - Add some new professional bodies to qualified person list
- Affects around 4,000 charities potentially

# Possible adjustments on transition to FRS102



# PBE Specific issues – FRED 45

see paragraphs 125 to 160 in FRS102

- Concessionary Loans (PBE34.87 to 34:97)
- Property held for the provision of social benefits (Paras16.3A and 17)
- Entity Combinations (PBE34:75 to 34:86)
- Impairment of assets: public benefit considerations (Paras 140 to 148)
- Funding commitments (PBE34:57 to 34:63)
- Incoming resources from non-exchange transactions (PBE34:64 to 34:74)

# Some differences between FRS102 and FRSSE

- FRS102 does not permit changes to Investment Property values to be taken to reserves.
- FRS102 has no 90% benchmark on finance leases
- FRS102 does not require names of Related parties but does require specific aggregate information
- FRS102 has a mandatory accrual on employee benefits
- FRS102 has a widespread use of “Fair value” – could be onerous on financial instruments
- FRS102 assumes a maximum 5 year life on intangible assets
- FRS102 has mandatory cash flow statements
- FRS102 covers more areas.....

# The choice facing small charities in 2015

Adopt the FRSSE knowing it will be withdrawn within 12 months! More change will be needed.

Go the whole way with FRS 102

Return to Receipts and Payments accounts (not available for companies). Adjusting back to accruals in future may be problematic.

## How the FRSSE currently deals with the new financial reporting framework

Follow the FRSSE for the issues it addresses

If FRSSE is silent, use existing accounting policies provide they meet accepted practice (old GAAP)

For new transactions have regard to current practice (FRS 102)

The FRSSE SORP will require current practice (FRS 102) for sector specific issues

The 2015 FRSSE is not really a stand alone standard....old GAAP!

# What might a replacement FRSSE look like?

Probably - new FRSSE will adopt 'measurement' and 'recognition' principles of FRS 102 – creating a single framework

But disclosures in notes will be limited under EU Accounting Directive

Effectively a FRS 102 'lite' ?

Possibly a new section in FRS 102?

Consider FRED59/ Draft amendments to FRS 102 small entities and other minor amendments – Feb15 comments before 30 April 2015

# Possible timeline for FRSSE replacement ?

Implementation of new  
EU Accounting  
Directive -2014/15

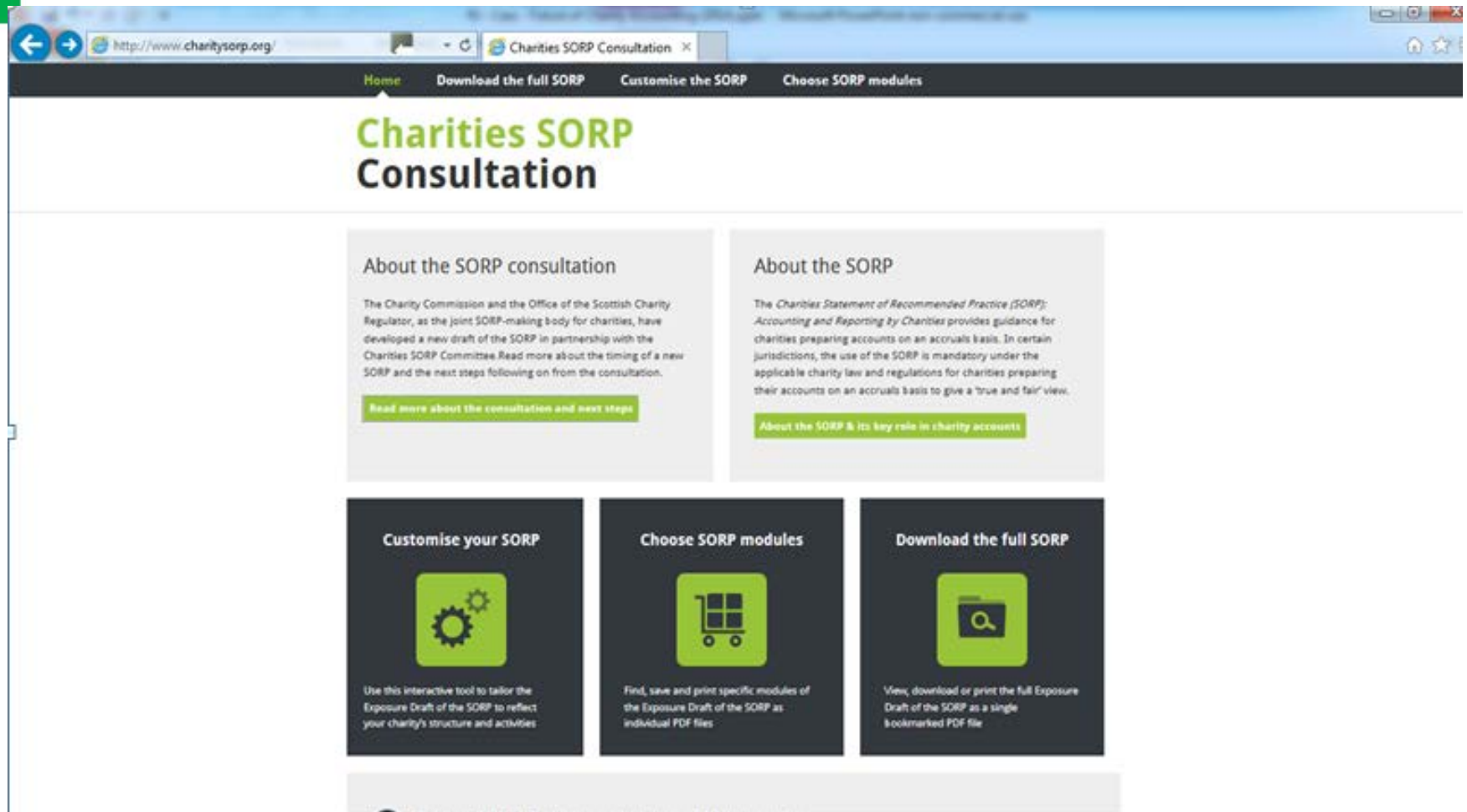
FRC modify existing  
FRSSE with Small  
charity SoRP for one  
year only  
2014/15

Revision of the SORP  
for replacement  
standard in 2015/16?  
See FRED59 plus  
consultation by SoRP  
Cttee June to  
Sep2015?

Mandatory application  
for accounting periods  
starting 1 January  
2016

# New Framework....2 new SORPs

## www.charitysorp.org





# SORP micro-site


- Dedicated site: [www.charitysorps.org](http://www.charitysorps.org)
- Micro-site is the location for:
  - free SORPs and modules
  - ‘Customise your SORP’
  - 3 help-sheets
  - Order hard copy SORPs
  - Future SORP Committee arrangements
  - Two FRS 102 model examples added
  - Two FRSSE model examples added in 2015
  - Background to the changes
  - Mapping of the previous SoRP



# Charities SoRP – Items most likely to.....

- Income (Almost) virtually certain
- Paid Annual Leave accrual
- FRS102 treatment of defined benefit pension scheme
- Goods for resale
- Concessionary Loans at Fair Value
- Other financial instruments
- Extended credit on contracts
- Cash flow data if required

.....require adjustment if FRS 102 adopted?!

- 
- My contact details
    - [Kenbrewco@gmail.com](mailto:Kenbrewco@gmail.com) 07748 758345
  - Useful Websites
    - <http://www.charity-commission.gov.uk/>
    - [www.charitycorp.org](http://www.charitycorp.org)
    - [www.frc.org.uk](http://www.frc.org.uk)
    - [www.charitytrends.org](http://www.charitytrends.org)