21. Accounting for social investments

Types of social investment and income risk sharing arrangements

21.1. This module applies to all charities making social investments. It explains when an investment is recognised either as a programme related investment or as a mixed motive (mixed purpose) investment. FRS 102 does not deal with accounting for social investments and therefore this module explains how social investments must be measured and disclosed when accounts are prepared using this SORP.

21.2. A wide range of terms are in current use to describe a developing variety of investment structures and other contractual arrangements that can be used to carry out or fund charitable activities. These investments and arrangements can take a number of contractual and legal forms such as repayable loans, non-repayable loans (quasi equity), concessionary loans, equity investments, property letting, and performance-related income or profit-sharing arrangements or partnerships.

21.3. A charity making or in receipt of social investments or undertaking complex contractual arrangements needs to consider carefully the nature of the arrangement and account for the substance of the arrangement.

21.4. 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.

21.5. Reference must be made to the SORP module ‘Balance sheet’, which sets out the classification and disclosures required for financial investments and liabilities, and to the SORP module ‘Recognition of income, including legacies, grants and contract income’, which sets out the basis for income recognition including profit sharing arrangements.

How the SORP defines social investment

21.6. This SORP uses the term ‘social investment’ to describe programme related investments and mixed motive investments.

21.7. When a programme related investment or mixed purpose investment is held in a subsidiary entity, an associate or joint venture, reference must also be made to the SORP modules ‘Accounting for groups and the preparation of consolidated accounts’, ‘Accounting for associates’ and ‘Accounting for joint ventures’.

21.8. This module sets out:

- programme related investments;
- mixed motive (mixed purpose) investments;
- ethical investment policies;
- social investments in property (land and buildings);
- concessionary loans;
- accounting for guarantees;
- the presentation of social investments in the investing charity's accounts;
- the reclassification of a social investment as a financial investment;
- how to measure social investments;
- impairment of social investments;
- accounting for impairment losses;
- accounting for gains on disposal;
- information to be provided in the investing charity's trustees' annual report; and
- disclosures in the notes to the accounts.

Programme related investments

21.9. A programme related investment is an asset held by a charity that provides investment funding to individuals or organisations in order to directly further the charitable purposes of the investing charity; any financial return obtained is not a primary reason for making the investment.

21.10. A programme related investment is made exclusively to further the charitable aims of the investing charity by funding specific activities or related tangible fixed assets of a third party which, in turn, contribute to the investor's own charitable purposes.

Mixed motive (mixed purpose) investments

21.11. A mixed motive (or mixed purpose) investment is an asset held by a charity that provides funding to individuals or organisations in order to generate a financial return for the investing charity and it also contributes to the investing charity's purposes through the activities or related tangible fixed assets funded by the investment.

21.12. A mixed motive investment can be distinguished from a programme related investment in that the investment is not made wholly to further the investing charity's charitable purposes. The investment is deemed to be 'mixed motive' as neither the investment return nor the contribution to the investing charity's purposes is sufficient on its own to justify the investment decision. The investment is not justified wholly by either the financial return or by the contribution it makes to the investing charity's aims but by the combination of the two.

Ethical investment policies

21.13. Investment decisions may be subject to the ethical, socially responsible or mission related investment policies adopted by a charity. The adoption of ethical, socially responsible or mission related investment policies does not create a separate class of investment asset that is presented separately in a charity's balance sheet. However, investment policies must be explained in the trustees' annual report and the value of investments held in pursuit of particular ethical investment policies may be identified separately in the note to the accounts analysing investments.

Social investments in property (land and buildings)

21.14. Property may be classified as a programme related investment only when it is held specifically to enable a third party to undertake particular activities using the property that contribute to the investing charity's charitable purposes. Property may also be classified as mixed motive investment when it is held for a combination of the financial return it generates and the contribution its use by another charity or third party makes to the investing charity's purposes.

21.15. Property used by a charity to provide goods or services or used for its own administrative purposes must be presented within tangible fixed assets (property, plant and equipment). Similarly, property that is let out to further the lessor charity's own purposes by providing a service to a charity's own beneficiaries must also be accounted for within tangible fixed assets.

21.16. Property that is held primarily to generate rental income and/or for its capital appreciation must be accounted for as investment property.

21.17. A mixed use property used in part by the charity to provide goods or services and for its own administrative purposes and in part to generate rental income must be apportioned between tangible fixed assets and investment property. However, if such an apportionment is impractical, the whole property must be classed as a tangible fixed asset.

21.18. A charity that decides to occupy a property partly to carry out its own activities, and partly lets it to a charity or third party which undertakes activities that further the landlord charity's purposes, should apportion it between tangible fixed assets and mixed motive investment. However, if such an apportionment is impractical, the whole property must be classed as a tangible fixed asset.

Concessionary loans

21.19. A programme related investment or mixed motive investment may be made in the form of a concessionary loan to a third party interest free or at below prevailing market rates. Concessionary loans are not made solely to achieve a financial return. Concessionary loans are made wholly or in part to advance charitable purposes for the benefit of a charity's beneficiaries.

Accounting for guarantees

21.20. A charity may, as part of its strategy for programme related investments or mixed motive investments, provide loan guarantees to facilitate the financing of activities undertaken by third parties. All such guarantees must be recognised by the charity making a guarantee as either a provision or a contingent liability depending upon the circumstances that exist as at the reporting date. A charity receiving a guarantee discloses the guarantee as a contingent asset when an inflow of economic benefits is probable. If it is virtually certain that the guarantee will be called upon it is no longer contingent and the income receivable is recognised.

The presentation of social investments in the investing charity's accounts

21.21. Programme related investments must be disclosed either as a separate line on the face of the balance sheet or identified as a separate class of investment in the notes to the accounts, depending on the materiality of the holding.

21.22. Mixed motive investments must be disclosed either as a separate line on the face of the balance sheet or identified as a separate class of investment in the notes to the accounts, depending on the materiality of the holding.

The reclassification of a social investment as a financial investment

21.23. If a programme related investment ceases to be held primarily to further the charitable aims of the investing charity, it must be reclassified as a financial investment, or investment property, or a mixed motive investment, as appropriate. Similarly, if a mixed motive investment ceases to be held to a significant extent for the contribution it makes to the investor's charitable aims, it must be reclassified as a financial investment or investment property, as appropriate.

21.24. However, if the failure of the investment to contribute to the charitable purposes and aims of the investing charity is only temporary, a social investment should not be reclassified; instead, it should be subject to a review for impairment.

21.25. A financial investment acquired to generate a financial return must not be subsequently reclassified as a social investment as the initial decision to make the investment was based wholly on commercial considerations. Similarly, where financial investments are selected on ethical or mission-based criteria, the investments must not be classified as social investments as they are held primarily for financial return. However, the notes to the accounts may be used to identify the amounts of investments held which were selected using ethical or mission-based criteria.

How to measure social investments

21.26. Charities making (or receiving) concessionary loans repayable on demand or within one year should not adjust the carrying amount of the loan to reflect the below prevailing market rates of interest being charged. However, for loans repayable in more than one year, a charity making (or receiving) concessionary loans must opt to either:

- initially recognise and measure the loans at the amount received or paid, with the carrying amount adjusted in subsequent years to reflect repayments and any accrued interest and adjusted if necessary for any impairment; or
- measure such loans initially at their fair value and subsequently at their amortised cost using the effective interest method (this would effectively treat the concessionary element of the loan as a financing cost or interest income, as applicable). For more information on the use of the effective interest method, refer to section 11 of FRS 102.

21.27. The same accounting policy for the measurement of concessionary loans must be applied to concessionary loans both made and received.

21.28. When a programme related investment or mixed motive investment takes the form of ordinary or preference shares, it must be measured at the reporting date:

- at its fair value, if this can be measured reliably; or
- if its fair value cannot be measured reliably, at its cost less impairment.

21.29. The bid price must be used to measure fair value for accounting purposes of shares that are traded in an active market. When quoted prices are unavailable, the price of recent transactions of identical investments may provide evidence of their fair value, provided that there has not been a significant change in economic circumstances since those transactions. Prices may need to be adjusted if the last transaction price is not a good estimate of fair value, for example if the transaction was as a result of a forced sale.

21.30. If neither the market price nor recent transaction prices provide a reliable estimate of fair value, then cost less impairment should be used.

21.31. If the contribution made by a programme related investment or mixed purpose investment to the investor's charitable purposes is reduced significantly, for example due to a change in the activities financed by the investment, then the classification of the asset must be reviewed. When necessary, the asset must be reclassified appropriately in the balance sheet and/or the notes to the accounts to reflect the purpose of the investment.

21.32. Programme related investments or mixed motive investments that are measured at cost or amortised cost must be assessed for objective evidence of impairment at the end of each reporting period.

Impairment of social investments

21.33. If there is objective evidence of impairment, for example a default on repayments due or evidence of significant financial difficulty in the entity in which the investment has been made, then an immediate impairment loss must be recognised in the statement of financial activities (SoFA). The impairment is measured on the same basis as other investments or financial assets.

Accounting for impairment losses

21.34. An impairment loss arising on a programme related investment should be recognised as a cost within 'expenditure on charitable activities' in the SoFA.

21.35. In the case of a mixed motive investment, the loss should be recognised as an investment impairment in the 'gains/(losses) on investments' line in the SoFA.

21.36. Any reversal of a previous impairment must be credited to the heading in the SoFA that was initially charged with the impairment. The reversal of an impairment charge must not result in an asset's carrying amount exceeding its carrying amount prior to its initial impairment.

Accounting for gains on disposal

21.37. Any gain on the disposal of a programme related investment is recognised as 'other income' in the SoFA after offsetting any prior impairment loss.

21.38. Any gain on the disposal of a mixed purpose investment is recognised in the 'gains/(losses) on investments' line in the SoFA after offsetting any prior impairment loss.

Information to be provided in the investing charity's trustees' annual report

21.39. This SORP requires that larger charities that are subject to statutory audit must include an explanation of the charity's policy for the use of programme related investments and mixed motive investments in the trustees' annual report when such holdings are material. The report must also explain the investment's performance in relation to the objectives set by the trustees. Further guidance is provided in the SORP module 'Trustees' annual report'.

Disclosures in the notes to the accounts

21.40. This SORP requires that the accounting policy note must disclose:

- the measurement bases used for programme related investments and mixed motive investments; and
- any other accounting policies that are relevant to understanding these transactions in the accounts.

21.41. This SORP also requires that the notes to the accounts must present programme related investment and mixed motive investment as separate classes of investment in the relevant note, if not separately disclosed on the balance sheet, and disclose:

- those details required by the SORP module 'Balance sheet' for the relevant classes of fixed asset into which the investment falls;
- details and amount of any guarantee made to or on behalf of a third party;
- the name of the entity or entities benefiting from those guarantees; and
- an explanation as to how the guarantee furthers the charity's aims.

21.42. The applicable disclosures set out in the SORP module 'Accounting for financial assets and financial liabilities' must also be made.

21.43. Section 34 of FRS 102 sets out the accounting treatment and disclosures relating to concessionary loans. Charities must disclose:

- the carrying amount of concessionary loans made or received (multiple loans made or received may be disclosed in aggregate, provided that such aggregation does not obscure significant information);
- the terms and conditions of concessionary loan arrangements, for example the interest rate, any security provided and the terms of repayment;
- the value of any concessionary loans which have been committed but not taken up at the reporting date; and
- separately amounts payable or receivable within one year and amounts payable or receivable after more than one year.