

Annex to Paper 2: Feedback from the engagement strands on reserves reporting

Editorial note: No changes have been made to the feedback, however the ordering may have been changed for consistency and in some instances italics, underlining or bold text has been used to help highlight the recommendations made.

Engagement strand - Major Funders & Donors and Government & Public Bodies

Preferred solution (with reasons)

1. Mandate the inclusion of Reserves in accounts across the board, subject to any exemptions that may be introduced for very small charities. The current demarcation of £500k is not helpful. There are more numbers of registered charities in the under £500k category than in the over £500k category, but they are not captured by all the current legislation.
2. Make it mandatory that the narrative note in the TAR regarding the Trustees' calculation of 'free' reserves is backed up by an arithmetical note in the Notes to the Accounts.
3. Plus, if that calculation has changed from the previous year, there should be a narrative in both the TAR and the Notes as to why the Trustees have changed their policy.
4. Introduce clear guidance with worked examples in the SORP as to what should be included in all Reserves calculations, particularly the 'free' reserves.
5. Rewrite some of the paragraphs in the SORP into more user friendly language and include flow charts.
6. Create an agreed place for the Property and Fixed Assets Reserve to be allocated, to avoid confusion in comparability. We would suggest Designated Reserves but it may be that this merits a separate Reserves category on its own.

Engagement strand - Academics and regulators and proxies for the public interest

Preferred solution (extract from the discussion provided)

There is a need for much better explanation by charities of how they have come to their reserves figure and the importance of this for their organisation.

trustees, even of these larger charities, did not understand the difference between reserves and unrestricted funds. Unrestricted funds that are tied up in fixed assets (especially functional ones), for example, could not quickly be liquidated in an emergency.

We consider the following to be key issues that need to be addressed in the revision of the SORP:

- there is no specific definition of reserves or how they should be calculated in the SORP that is applicable to all charities (paragraphs 1.21 – 1.24)
- the requirements about reserves in the SORP form part of the Trustees' Annual Report rather than the statement of accounts, meaning they are not subject to audit or examination
- requirements about reserves are contained in several different places in SORP, relating to the trustees' annual report, the SOFA and the notes. Charities might benefit from one single set of instructions that takes them step by step through a standard calculation, to increase consistency of reporting.

More important for readers than this number is the narrative explanation of whether it is the right number – what level of reserves has the charity worked out that it needs (and why) and do they have that amount? What does that mean in terms of sustainability/survival or the ability to wind up in an orderly fashion?

- Guidance is proliferated across several locations both within and outside the SORP. This contributes to confusion and uncertainty.
- There is a lack of clarity around specific terms, some of which are used interchangeably. Common examples include:
 - o Free reserves = total unrestricted reserves
 - o Unrestricted reserves = cash
 - o Unrestricted reserves = cash + current assets – current liabilities
 - o Whether free and general reserves are the same or different
 - o Designated reserves are free reserves
 - o A charity should have one reserves policy and stick with it forever
 - o There is only one way to calculate reserves
 - o A reserves target is single number not a range
- Evidence of inadvertent but widespread inconsistency and non-compliance based on current guidance. (e.g. Charity Commission findings)

Suggest the following:

- A plain English, short statement on the purpose of reserves and a reserves policy. Signpost to external guidance on how to set a reserves policy, emphasising that one-size does not fit all.
- A plain English glossary of key terms – endowment, restricted, designated, free (or general but only one term).
- Illustrative guidance on how to how to calculate free reserves, with signposting to external resources as appropriate, recognising there may be more than one calculation.
- State the charity's reserves policy accompanied by a brief narrative covering:
 - o Why the trustees have selected this policy. Emphasise that no-one size fits all and target reserves may be a range.
 - o Current reserves versus target reserves together with an explanation for any significant variance.
 - o How reserves have been calculated, emphasising that there is more than one acceptable approach to calculate reserves and good practice would be to

review the charity's position vis-à-vis 1-3 different approaches (e.g. income-based, risk-based, stress-test)

The SORP should be better at defining what is meant by reserves (particularly free reserves) and how these should be calculated.

An explanation about why their actual reserves differ from their stated policy has benefits but need not be mandatory. Instead to aid good governance in other ways require charity trustees to think about their financial performance and could jump start questions about whether targets were appropriate and achievable or whether they were generating more reserves than needed.

A charity's level of reserves is a key metric both of its sustainability and its effectiveness:

- where reserves are 'too high' it may be taken as an indication by funders that a charity is ineffective and not deserving of financial support; this view has at times created a downward pressure on charity reserves
- where reserves are 'too low' it should be a warning sign about the charity's sustainability; this concern has come more to the fore in recent years following the financial challenges of 2008-2012 and during the Covid-19 crisis

It is not simple, however, to say what is 'too high' or 'too low'. Charities' reserves needs are dependent on several different factors including their size, the type of activity in which they engage, whether they employ staff and so on. For example, a volunteer-run charity that simply gives grants from its income might have very different reserves needs to a charity employing staff to care for vulnerable individuals.

However, as has been emphasised in the recent judgement in the case of Keeping Kids Company, it is not a legal requirement for charities to have reserves. There is no minimum or maximum requirement; it is a matter for the trustees' judgement, acting in the charity's best interests.

Engagement strand - Smaller charities and Independent Examiners

Preferred solution (with reasons)

The glossary definition of reserves from previous SORPs should be reinstated within the glossary or financial review section.

The method by which reserves are calculated should be included in the TAR or notes. This could potentially be sentence effectively summarising the SORP definition. The actual free reserves could then be stated.

If the text from the Scottish legislation provided in the briefing paper was adopted this would satisfy the needs of most readers of a charity's accounts, in particular providing clarity on designations.

These amendments would ensure a clearer reporting of reserves within the accounts. There would be a clear indication of the likely timing of expenditure of designated funds which would allow users to see the impact of this on the reserves available. If free reserves were more clearly shown then the users of the accounts would better understand the availability of funds for the charity.

This clearer reporting of reserves within the narrative of the TAR would negate the need for additional disclosures in this area.

A columnar Balance sheet could be encouraged but could probably not be mandated realistically. We are undecided on the idea of requiring a designated fixed assets column.

Engagement strand – Larger Charities

Preferred solution (with reasons)

Clearer guidance on the calculation of reserves i.e. the balance sheet figure, broken down between restricted, designated, freely available (removing fixed assets or non-recognisable assets) ending up with freely available reserves. A table to this effect should be included in the notes to accounts so everyone can see exactly how the reserves are comprised and this note should include a narrative describing any key features or movements. This note and narrative should be replicated in the TAR (which is not audited) so the benefit is that the reader of the TAR can understand reserves but as the note also exists in the body of accounts, it will have been audited. Further information in the TAR about the reserves policy, charity's approach to reserves etc. will also be very useful

- The group felt that the need to make the case that reserves is in fact an issue, that needed to be considered in the SORP development process, had already been made and that the reserves paper had summarised the position and the case for change.
- The group discussed the lack of consistency with the reporting of reserves both from the calculation and the narrative. The group also noted the issue of how fixed assets and designated funds are treated in reserves and the problems this causes. A group member noted that even large charities and their auditors get it wrong.
- The issue of reserves being reported on a specific date i.e. year-end date and whether there was any merit in considering some kind of average calculation was discussed, noting that reserves will fluctuate from day to day. The group appreciated that reserves would fluctuate during the period but there was a feeling that the practicalities would be difficult to overcome as charity financials tend to be derived from nominal at the end of the year and this is how most software works. It was felt that the reserves narrative could be used to explain performance in the year.
- One member said that in their organisation there is a set band of desired reserves and that the charity need to keep an eye on the level and whether it goes above or below. Once the calculation is accurate and understood, the movement in reserves can and should be captured by narrative.

- The group felt that the TAR should be more prescriptive in terms of reserves and perhaps include a table detailing the reserves. In addition, the group thought that a disclosure note would be helpful and that this would complement the TAR and would also be audited which would help with the accuracy of calculation. The note could have clear rules on calculation, fixed assets and designated funds which would help resolve some of the issues.
- In relation to designated funds the group felt that a clearer definition would help and would also improve comparability. This would also assist trustees in their thinking and planning as this is a tricky area.
- In relation to the narrative reporting it was suggested that the TAR also reports on previous performance of reserves and what action has been taken.
- The issue of liquidity of reserves was discussed and the group agreed that this could be reported in the narrative and that it would help trustees and users of accounts understand the financial position. However, the group were also mindful of the issue of some charities using the cash figure for their free reserves and miscalculating reserves.

Engagement strand- Professional and technical group A

Preferred solution (with reasons)

In relation to the definition of 'free' reserves, we recommend that:

- The glossary of terms includes a definition of reserves and that those reserves are described in the glossary and elsewhere in the SORP as 'free' reserves or some such similar term. This will ensure that 'free' reserves are not confused with other reserves/ illiquid unrestricted funds and that the charity, its trustees and other stakeholders understand that the charity has access to these reserves.
- The definition of 'free' reserves should be sufficient to enable a charity to calculate these accurately based on items included in its financial statements. While members of the Strand have not reached agreement on where a charity should disclose the calculation of its reserves, members do agree that the calculation should be included within the TAR and financial statements document. Some members of the Strand favoured disclosure of the calculation in the TAR, others favoured disclosure within the financial statements, different views being expressed on how any financial statement disclosure should be tackled.
- Designated funds and off-balance sheet commitments cannot be excluded from a charity's calculation of its 'free' reserves and should therefore fall within the scope of the charity's policy on holding reserves, should it have one.
- Consideration is given to dispensing with the term 'designated funds' and instead charities are required to explain the role their 'free' reserves play in future plans. This will help charities to create a narrative whereby charities consider their future financial sustainability.
- The charity regulators should consider updating their reserves guidance to coincide with the next edition of the Charities SORP.

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Narrative reporting about reserves in the TAR

We believe that all charities should have to apply the full Charities SORP requirements in respect of reporting any policy on holding reserves and the value of reserves held at the balance sheet date, regardless of any future tiering. This will help to ensure all charity's correctly identify their reserves and can therefore report accurately on related matters. For example, accurate information about the value of reserves held is a necessary part of ensuring a charity can report accurately on its future financial sustainability.

Paragraph 1.48 (larger charities requirements) describes how a charity should calculate its reserves. However, we do not think this is sufficient to enable charities, including smaller charities, to do this accurately. The development of a formal definition of reserves for the glossary (as mentioned above) and the development of a table to support a charity's calculation of its reserves (with its unrestricted funds as a starting point) could be used to support any reporting about a charity's reserves and related matters. There would also be merit in exploring how a numerical disclosure about a charity's reserves links with or is cross-referenced to the funds note in the financial statements.

Members of the Strand who favour the disclosure of how a charity's reserves are calculated within the TAR supported this on the grounds of proximity to narrative disclosures about reserves and the wider financial review, this would also avoid any concerns about FRS 102 requirements on the publication of comparatives.

Members who favoured any new numerical disclosure about a charity's reserves being included in the financial statements believe it would be helpful for the disclosure to be covered by the 'true and fair' view and be subject to a higher degree of scrutiny than if it were included in the TAR. Two specific points were raised in relation to disclosure within the financial statements:

- While members of the Strand understand that some auditors and independent examiners will check any numbers in the TAR more rigorously than required, this cannot be relied upon.
- Any numerical disclosure within the financial statements may also need to be accompanied by information about any specific plans a charity has to use its 'free' reserves to support the 'true and fair' view. This raises the broader question about how to balance the content of a reserves note in the financial statements with the narrative reporting requirements on reserves within the financial review section of the TAR.

The inclusion of a definition of reserves in the glossary and the development of a reserves calculation would require a rationalisation of the wording in paragraph 1.48 to remove any duplication.

If, as part of the BEIS consultation on corporate governance and audit reform, the UK Government decides to treat the largest charities as PIEs, there will be increased disclosure requirements for those charities falling within the PIEs regime around their

financial sustainability. The disclosures would be more onerous than for non-PIE charities but would still need to be proportionate and tailored to ensure that they are relevant to charities. Any additional requirements for PIE charities would likely need to be dealt with in separate guidance rather than within the Charities SORP.

The reporting of reserves in the financial statements

The Strand discussed the following options for a numerical disclosure of a charity's reserves in the financial statements:

- A new note to the financial statements.
- A new primary financial statement, perhaps to include funds as well as reserves.
- Disclosure at the bottom of the balance sheet.
- Presentation as part of the balance sheet.

Of those Strand members who would prefer to see any numerical disclosure in the financial statements rather than the TAR, there was no consensus and no majority for any particular option. The following points were discussed in relation to the above options:

- Commentary on a new note. This is perhaps the most straightforward way of introducing a numerical disclosure in the financial statements. It may also be the simplest solution from the perspective of software providers.

However, there is concern that if a reserves note is required it would logically fall towards the end of the accounts, due to relating to the bottom half of the balance sheet, and therefore would not be seen.

Additionally, this approach would create three places in the accounts where reserves are mentioned making it more challenging for users' of the TAR and financial statements. These three places would be the TAR; the accounting policies note; and then the reserves note.

If this approach is taken, members of the Strand agree that such a note would need to be prominent.

- Commentary on a new primary statement. In relation to having a separate primary statement, it was suggested that the statement of funds should also be a primary statement and that this and a statement of reserves would be more relevant to some charities than the statement of cashflows. A combined statement of funds and reserves primary statement could also be considered.

Either option would be a radical change of approach but would address concerns about the prominence of a potential reserves note and the current perceived lack of prominence of the funds note.

However, it would need to be established if introducing one or two new primary statements would be commercially viable for software providers to incorporate into

their accounting software. It is therefore important to engage with software providers in early course.

The primary statement approach would be a non-starter without the support of the FRC. However, there are parallels with the introduction of a statement of changes in equity to company accounts when FRS 102 was implemented.

- Disclosure below the balance sheet. Some members of the Strand were strongly opposed to the primary statement approach on the grounds it would give undue prominence to a charity's reserves. In order to strike a balance between having a note or a primary statement, another suggestion made was the inclusion of a note below the balance sheet which reported the value of a charity's reserves. It was at this point in the Strand's discussion that the idea of abandoning the use of designated funds was raised. The concept of designated funds is considered by Strand members to 'muddy the waters' as it is not helpful in facilitating a charity's proper consideration of how it intends to use its reserves and remain financially sustainable. This approach and the approach set out below could facilitate the inclusion of the numerical calculation of a charity's reserves in the TAR.
- Presentation as part of the balance sheet. 'Free' reserves could be presented as a separate line item on the balance sheet as an element of a charity's unrestricted funds. De facto designated funds could be shown separately or in total (with an accompanying note). De facto designated funds collectively could be described instead as 'other unrestricted funds'. This would not necessarily mean striking another sub-total before arriving at the balance sheet total, as charities reporting an unrestricted pensions reserve or unrestricted revaluation reserve in addition to unrestricted funds already have to do this. N.B. Charitable companies would still be required to report a revaluation reserve with a credit balance on the face of the balance sheet.

Engagement strand- Professional and technical group B

Preferred solution (with reasons)

- The requirements to report on reserves should apply to all charities although the level of complexity could differ depending on the size of the charity.
- There should be a definition of reserves and supporting examples.
- There should be a note to the accounts calculating reserves and a reconciliation agreeing this to accounting reserves.

In support of the recommendations- observations made were:

- The guidance in the current SORP is unclear and difficult for trustees to understand. This is borne out by the Charity Commission review of reserves policies in 2018 which highlighted the disclosure of the level of reserves was not done well.
- There is no clear definition of reserves in the current SORP. This is confusing for preparers of the trustees' annual report and leads to inconsistencies from year to year and between charities.

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- The distinction between reserves and free reserves is not clearly highlighted in the current SORP which is not helpful to users of the SORP.
 - Reserves are important to all charities regardless of size, not only due to the current times of uncertainty, but also since the reserves are an important figure for the users of the accounts to understand. Full transparency over this figure as well as the policy is required for all sizes of charities, given the importance of this to the charities liquidity position as well as the going concern assessment.
 - COVID has possibly pushed reserves higher up the agenda of trustees now than they may have been before. Some charities have benefitted from increases to reserves (e.g. NHS charities) although some donations have been for particular causes so there may not necessarily been an increase in free reserves. This has highlighted the lack of understanding by trustees of reserves, generally and 'free reserves'.
 - Whilst the Trustees' Annual Report should not drive good governance and should instead (amongst other things) give visibility on a charity's governance, there is no doubt that the need to report in the TAR does focus some charities' minds.
 - Understanding reserves is key to understanding a charity's accounts.
 - There should be one reserves policy requirement for all charities. The requirements for reserves policies under 1.48 which currently only applies to larger charities should be widened to all charities, whilst appreciating that the level of disclosures may vary on size and complexities.
 - A definition of reserves could be included in the SORP and guidance regarding this definition should be linked to explaining the liquidity position of the charity, to going concern disclosures and future developments.
- be clear about 'reserves' and 'free reserves' explaining the effect on free reserves of designated funds and reserves which can only be realised by disposing of tangible fixed assets or programme related investments. In contrast to this more prescribed approach, it was thought by 1 member that grant funders do not always expect that fixed assets be designated and that there are some situations where fixed assets can be included in free reserves.
- The guidance on reserves should not be overly technical and complicated. One opinion was that there should be a more fluid approach
 - Providing worked examples of reserves calculations would be helpful.
 - Reinstate requirement that charities provide an explanation about why their actual reserves differ from stated reserves policy.
 - Paragraph 1.22 to be amended to say 'The charity must explain the policy it has for holding reserves and state the amounts of those reserves and why they are held. If the trustees have decided that holding reserves is unnecessary, the report must disclose this fact and provide the reasons behind this decision.'

- The effect on reserves of pension liabilities and loans secured on fixed assets should be explained in the trustees' annual report. This should form part of the reserves section.
- Including a requirement to provide a reconciliation of the reserves/free reserves calculation to the total in the accounts.
- Including provisions that require disclosure regarding the reconciling items in the reconciliation described above.
- Paragraph 10.91 can be confusing and could be amended as follows:
"A charity may choose to disclose the amount held as free reserves under a sub-heading of its unrestricted funds provided that this amount is positive."
- A definition in the glossary would assist in terms of clarity and consistency in application in an area which clearly has caused some confusion in recent years.
- The glossary definition of a designated fund should be amended as follows:
Designated funds continue to count as part of the unrestricted funds of the charity, but the trustees should (rather than "may choose to") exclude designated funds from the calculation of the charity's reserves.
- Changes to the reporting requirements should be carefully worded to avoid terms that might be considered only for the accountants.

Engagement strand - Trustees

Preferred solution (with reasons)

Options considered were:

- Option 1: provide clearer guidance and consistent definitions
- Option 2: provide more tools and templates to assist trustees in the reporting of reserves
- Option 3: link the setting and reporting of reserves to other disclosures
- Option 4: include information on reserves in the financial notes
- Option 5: more narrative information
- Option 6: any other options identified by the strand

In a very broad ranging and technical discussion and in trying to achieve consensus the following recommendations were supported by the strand: Recommendation: Adopt option 1: provide clearer guidance and consistent definitions. As identified in the Trustee Engagement Strand's recommendations at the end of phase 1, more could be done to simplify the terminology used within the SORP and to ensure definitions are used consistently throughout the document.

As previously recommended, the strand could promote a 'think non-financial trustee' approach to developing the next SORP in plain English with greater clarity, consistency and cross referencing of definitions and terminology used. For example, a reminder that all funds must still be used to further charitable objects could

reinforce the understanding that 'free' does include certain requirements under charity law.

There was a passionately held opinion by a minority of strand partners that the terms used within the SORP relating to reserves should be overhauled in some instances and replaced with language more easily understood by the average trustee (see points above). However, this was countered with the desire to retain terms that many will be familiar with and the observation that as the trustee role is a significant responsibility, trustees should be prepared and expected to understand some of the basic concepts relating to the performance of those duties (such as understanding basic technical terminology – legal and financial).

As such, the strand does not recommend changing the terms used, but that new terms should be introduced within the reporting framework (such as liquidity and capital) and clearer, comprehensive and consistent definitions (and glossary) are used and produced in plain English to help trustees understand the terms used within the SORP.

Recommended to adopt option 2: provide more tools and templates to assist trustees in the reporting of reserves as identified in the Trustee Engagement Strand's recommendations at the end of phase 1, alongside the production of the next SORP, consideration and resources should be dedicated to delivering supporting documents, templates and models to support compliance and better annual reports and accounts.

Developing a decision-tree or flow chart for trustees to discuss and agree their approach to reserves would be useful. It could be suitably tailored to encapsulate issues arising from income, operational and/or organisational complexity and risk. This could help promote a more consistent application of reserves reporting. It is noted that the regulators already produce a range of supporting documents to help trustees, however given the inconsistency of reserves reporting (amongst other things) it would appear these aids are not having the intended impact. A different approach is required that is easier for trustees to access, understand and apply.

One approach to improve understanding and reporting of reserves by trustees could be to better explain the 'why' of reserves. For example, the issue of whether and how much a charity should build up reserves should be linked to the overall strategy and financial management of the charity. The wider risks, operational complexity and income volatility will therefore help to inform board discussion about the target level and appropriateness of reserves in helping to counter the risks identified. This helps move reserves policies beyond the three/six months cul-de-sac and helps trustees articulate a more nuanced approach that is better suited to the challenges and opportunities of the charity.

Recommendation: Strongly review the benefits of applying option 3: link the setting and reporting of reserves to other disclosures and expand disclosures to include the liquidity of a charity. The concept of reserves is different to that of liquidity, but they both provide an important insight into the financial health of a

charity (and going concern). As mentioned above, reserves (retained profits) can be held for many reasons including: to buy fixed assets; expand; pay debt; increase staff; or invest in financial assets to improve the sustainability of a charity etc. This is not same as liquidity – freely available cash or cash in financial institutions that is freely available. The financial information relating to both concepts should be clearly disclosed in the annual report and accounts. These disclosures should encapsulate the trustees' thinking supporting their chosen approach to reserves and issues of liquidity (linked to volatility of income, interest rates, inflation, reputation, etc) capital and risk to provide a more balanced and comprehensive representation of the charity's financial health and performance.

Recommendation: Balance the benefits of option 4 and the possibility of reducing the length of the financial notes (proposals to be discussed at a later date): include information on reserves in the financial notes. Without wishing to add to the length and complexity of the financial notes (which we note are to be discussed at a later date), the strand recognises the benefit of adding information relating to reserves, liquidity and capital within the financial notes to aid the better understanding, calculation and reporting of reserves (both as a figure and as a policy approach).

Recommendation: Reconsider the value of option 5: more narrative information. Additional information should be included within the SORP that demonstrates the trustees' thinking, approach and decision making with regards to the build-up (or otherwise of reserves), for what they will be applied and an explanation as to why there may be a gap between a target figure and the actual stated figure. The placement and status of such information – whether in the TAR or elsewhere within the audited or independently examined financial statements – needs to be evaluated. As recommended in the strand's phase 1 report, consideration should be given to a requirement to report on cash balances and forecasts as well as reserves.

Recommendation: The strand strongly urges the next SORP to further develop the presentation of the balance sheet and to assess the benefits of adopting a different approach to assessing the financial health of a charity that goes beyond reserves. The strand identified two further options for consideration by the SORP Committee. Firstly, the balance sheet should be further developed to make it easier for readers to understand where money has been spent and income generated. Secondly, the approach adopted by the USA might be a more worthwhile and impactful approach with merits for the UK and Republic of Ireland charity sector. For instance, reviewing the SORP to consider how charity reserves are comparable to accumulated earnings and capital in a company. For example, earnings are retained as part of an organisation's risk assessment but also to fund capital projects and expansion. Fund accounting, including better use of designation, should be able to accommodate this.

Final observations: The strand noted in its discussions that there could be some foreseeable issues with introducing a new focus on liquidity or reporting of reserves in terms of the level of external scrutiny applied to attesting the veracity of the information presented. That there may need to be some reworking of the TAR and the financial notes in order to avoid duplication and repetition. Also, the timing of the reporting of grant income may require additional thought as a result of any changes.

It is however, acknowledged that the topic of grants/income recognition is scheduled for a later meeting.

Discussion

As trustees are both preparers and users of annual reports and accounts, the strand approached discussions by balancing clarity with whether the options would make life easier for trustees in adopting and applying the SORP requirements. In discussing the complex issue of reserves, it was noted that:

- The technical language used can be confusing and does not easily translate for those trustees who do not have a financial background (for example 'free reserves', restricted, designated and endowments). This is not aided by a lack of consistency in the use and definitions of terms within the SORP (and its supporting documents). One strand partner suggested the following changes in terminology: i) Unrestricted reserves should be changed to 'General Charitable Reserves' (income or capital) as per the objects and powers clauses of the governing document; ii) Designated reserves should be changed to 'Set Aside' (determined by the trustees) or 'Semi Restricted Reserves'; iii) Restricted reserves (capital or income) should include all endowments and bequests etc that are currently restricted, but shown elsewhere except in the case of a Section 80 Order issued by the Charities Commission for England and Wales under the Charities Act 2011; iv) Free reserves should be deleted on the basis that the balance sheet would, like the SoFA, show balances in columns: 'General Charitable/Set Aside or Restricted' and the 'Net Current Assets / Working Capital /Charity's Liquidity', for example, would immediately show the monies available to be spent; v)
 - The current Charity Commission's approach to reserves should be changed to ask what is the charity's liquidity situation and what is the policy to invest or spend any excess monies?; and vi) If charities wish to "set aside" monies to cover say, the dissolution of the charity, redundancy costs and the like, then those monies - cash type reserves should be shown as "set aside" reserves / monies.
- The use of plain English would be helpful, building on the 'think non-financial trustee first' principle outlined in previous papers of the strand.
- For all the guidance available to help trustees (produced by regulators and other bodies, see Appendix 1) calculate and report on reserves, the practice and communication of them continues to be inconsistent. A different approach needs to be identified and promoted in order to improve the standard and quality of reserves reporting. Linked to this is the fact that some terms may be used interchangeable, when they actually mean different things. Clarity and consistency of definitions are key.
- A focus on liquidity, capital (though it appreciated this term may not sit comfortably within the charity context) and risks might be more relevant than reserves, thereby better combining the financial data with the narrative information presented in the annual report and accounts (such as the TAR).

- Currently, the debate on reserves tends to focus on measurement and disclosure of the funds themselves. How they are held, and their realisability, i.e., the top half of the balance sheet, is less clear. The balance sheet analysis needs to be further developed: at the moment different strands of financial activity are clearly identified within the SoFA like ‘different coloured ribbons which then get plaited into something less easily recognised’. The current SORP requires (2.29) “a summary of the assets and liabilities of each category of fund if not provided by ... a columnar balance sheet”, though it is suggested that this may require additional thinking to ensure the information is clearly identifiable (as opposed to fears that such a presentation may appear cluttered); The balance sheet should be linked to the SoFA.
- The trustees’ thinking and decision making regarding the reserves policy needs to be better and more clearly articulated (‘show the workings out’ not just the number) and linked to the future plans of the charity. This is linked to a need for better trustee understanding and oversight of a charity’s financial management and planning.
- The reserves calculation should be fairly straightforward; however, it can regularly be reported incorrectly within annual reports and accounts (sometimes there are two different figures with no explanation as to why);
- There is a recognition that a base line level of reserves to support the ‘winding up with dignity’ of a charity may be the starting point for board discussions and reserves disclosure, though the final figure may be higher or lower than that due to other organisational plans and priorities. A ‘target figure’ may be a useful approach to improve thinking and application, however, further thought might be required to decide whether the “terminal reserve” or “liquidity reserve” should be an allowable designation and thereby be excluded from free reserves (designated reserves should be for “other organisational plans” with specific end dates);
- Within the sector and those supporting charities there can be confusion over the guidance from regulators and others relating to reserves (e.g., you need three/six months of capital in your reserves for winding up operations). This does not help trustees to undertake a balanced discussion about reserves which includes liquidity, income volatility, operational model, strategy and risk; and
- An acknowledgment that not every charity will have the ability or flexibility to build up reserves, but that this position could be articulated in the reserves policy (which could include having a negative reserves target figure).