

# CHARITIES SORP (FRSSE)

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**Accounting and Reporting by Charities:  
Statement of Recommended Practice  
applicable to charities preparing their  
accounts in accordance with the Financial  
Reporting Standard for Smaller Entities  
(the FRSSE) (effective 1 January 2015)**



**OSCr**  
Office of the Scottish **Charity Regulator**



## **Accounting and reporting by charities: the statement of recommended practice (SORP) – scope and application**

### **Introduction**

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1. The Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard for Smaller Entities (the SORP) is issued by the Charity Commission and the Office of the Scottish Charity Regulator in their role as the joint SORP-making body, recognised by the Financial Reporting Council.
2. This SORP provides guidance for charities on how to apply the Financial Reporting Standard for Smaller Entities (referred to as FRSSE in this SORP). It is important for preparers of accounts to make reference as necessary to the FRSSE when preparing accounts and in making required disclosures. The requirements of the FRSSE and law take precedence over the SORP. Therefore should an update to the FRSSE or a change in relevant legislation be made after the publication of this SORP, any of the provisions of this SORP that conflict with the updated FRSSE or relevant legislation cease to have effect.
3. Charities opting to apply the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102) must follow the separate 'SORP applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland'.
4. The accounting policies adopted by charities following this SORP must follow the FRSSE when that standard specifies a particular accounting treatment. Each module of the SORP refers to the accounting treatments and disclosures required by the FRSSE and also identifies any additional disclosures or presentational requirements of this SORP.
5. Where the FRSSE allows an accounting policy choice, the relevant SORP module identifies when the adoption of a particular policy is more appropriate in the circumstances of a charity.
6. This SORP includes charity-specific requirements that are additional to those of the FRSSE. In particular, requirements relating to the trustees' annual report, fund accounting, the format of the statement of financial activities and additional disclosures aimed at providing a high level of accountability and transparency to donors, funders, financial supporters and other stakeholders. The phrase 'this SORP requires' is used to distinguish the additional disclosures required by the SORP which are not specifically required by the FRSSE.
7. Charities preparing their accounts using the FRSSE must refer to that standard and the relevant modules contained in this SORP when selecting their accounting policies for the treatment of particular items, transactions or events in the accounts.
8. This SORP requires that charities must adopt current accounting practice as set out in this SORP to reflect the special factors prevailing or transactions undertaken in the charity sector. The introduction to each of the SORP's modules specifies when this SORP requires a charity to adopt current accounting practice.

## Accounting and reporting by charities

9. For all other transactions that are not specifically dealt with in the FRSSE, charities may follow their existing accounting policies provided that the policy and related disclosures made are consistent with accepted accounting practice. Where a charity undertakes a new transaction for which it has no existing policy and where it is not dealt with in the FRSSE, the FRSSE requires a charity to have regard to current practice in developing its accounting policies.
10. Where a charity undertakes a new transaction for which it has no policy and where it is not dealt with in the FRSSE or this SORP, the FRSSE requires a charity to have regard to FRS 102 in establishing current practice.
11. Before applying this SORP, the following sections should be read which explain the scope and application of this SORP:
  - the scope of the SORP;
  - the effective date of commencement;
  - the intended user of the SORP;
  - objectives of the SORP;
  - the intended user of the trustees' annual report and accounts;
  - how to use the modular SORP;
  - use of the terms 'must', 'should' and 'may';

and also provides:

- an index of the SORP modules; and
- the assurance statement given by the Financial Reporting Council

### Scope of the SORP

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12. All charities preparing accruals accounts in the UK in accordance with the FRSSE must follow the recommendations of this SORP unless an alternative reporting framework or another SORP applies. In the Republic of Ireland, charities established as public guarantee companies are not eligible to apply the FRSSE and therefore should not apply this SORP. For all other charities established in the Republic of Ireland, whilst the application of this SORP is not a legal requirement, it should be referred to as best practice guidance that will be relevant to ensuring a charity's accounts give a 'true and fair' view.
13. This SORP must only be used by charities that are eligible and choose to apply the FRSSE. In the UK, a charity must meet the size criteria that define a small company or small group under the Companies Act 2006. These same thresholds apply to all charities whether or not established as a company. In the Republic of Ireland, non-companies may use the FRSSE and this SORP provided they would, if established as a company, meet the size criteria for a small company set by relevant regulations.

## Accounting and reporting by charities

14. The thresholds that define a small company and a small group are set out in Appendix 3 of this SORP. A charity is also excluded from adopting the FRSSE if it, or a member of its group, undertakes certain insurance, banking or financial service activities. Charities must refer to paragraph 9 of the FRSSE to ensure they do not fall within the category of entities excluded from adopting the FRSSE.
15. In addition, charities must also meet any conditions imposed by this SORP for adopting the FRSSE. In particular, an eligible charity may only adopt the FRSSE when preparing its accounts provided that it does so in conjunction with the recommendations of this SORP.
16. In addition, where a separate SORP exists for a particular class of charities (for example SORPs applicable to Registered Social Housing Providers or to Further and Higher Education Institutions, or Common Investment Funds), those charities should adhere to that SORP which may scope out the option of applying the FRSSE.
17. Charities applying this SORP may also be subject to specific regulations or legal requirements based on how they are constituted or their jurisdiction(s) of formation, operation or registration. For example, charities constituted as companies will need to meet the reporting requirements of company law. Whilst this SORP has been prepared to be consistent with the requirements of company and other relevant law and regulation, charities will need to ensure that any particular accounting requirements and disclosures applicable to them are also met.
18. The accounting recommendations of this SORP do not apply to charities preparing cash-based receipts and payments accounts. Charities preparing cash-based accounts must refer to the regulatory requirements of their jurisdiction(s) of registration regarding the format and content requirements for receipts and payments accounts and the trustees' annual report.
19. Charities not eligible to, or choosing not to, prepare their accounts under the FRSSE must prepare their accounts under FRS 102 and also use the FRS 102 SORP.

### Effective date of commencement

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20. This SORP is applicable to the accounts of relevant charities for reporting periods beginning on or after 1 January 2015. In those jurisdictions where the applicable SORP is specified in regulations, this SORP cannot be adopted until the applicable regulations are made allowing its application.

### The intended user of the SORP

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21. The SORP is developed primarily to assist those involved in the preparation of the accounts and trustees' annual report of a charity. The SORP is also relevant to charity auditors, independent examiners and accountancy practitioners who are involved in the scrutiny of charity accounts or in advising on the application of accounting standards in the context of charities.
22. It is anticipated that users of this SORP will be familiar with accounting concepts, principles and terminology and possess a reasonable knowledge of accepted and current accounting practice.

## Objectives of the SORP

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23. The recommendations of the SORP are intended to achieve the following objectives:
- improve the quality of financial reporting by charities;
  - enhance the relevance, comparability and understandability of the information presented in charity accounts;
  - provide clarification, explanation and interpretation of accounting standards and their application to charities and to sector specific transactions; and
  - assist those who are responsible for the preparation of the trustees' annual report and accounts.

## The intended user of the trustees' annual report and accounts

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24. The objective of the trustees' annual report (the report) and accounts is to provide information about a charity's financial performance and financial position that will be useful to a wide range of stakeholders in assessing the trustees' stewardship and management of charitable funds, and to assist the user of the accounts to make economic decisions in relation to the charity.
25. Although past, current and potential funders, donors and financial supporters of a charity are the primary audience for the financial information contained in a charity's report and accounts, the preparer should also be aware that interest in this information may also extend to a charity's service users and other beneficiaries.
26. The report and accounts should not be viewed simply as a statutory requirement or a technical exercise. The report and accounts, when read together, should help users of the information to understand what the charity is set up to do, the resources available to it, how these resources have been used and what has been achieved as a result of its activities.

## How to use the modular SORP

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27. For a charity to state that it has prepared its accounts in accordance with this SORP, it must adhere to the SORP's requirements for the preparation of both the accounts and the trustees' annual report.
28. The accounts of a charity comprise the following:
- A statement of financial activities (SoFA) which provides an analysis of a charity's income and expenditure and movement in funds in the reporting period.
  - A balance sheet which sets out a charity's assets and liabilities and retained funds at the end of the reporting period.
  - For charities that are companies, an income and expenditure account included either within the SoFA, or as a separate summary income and expenditure account in addition to the SoFA where necessary to meet the reporting requirements of company law.

## Accounting and reporting by charities

- Notes to the accounts that explain the accounting policies, provide more details of how the income and expenditure is made up, and provide extra information about particular assets and liabilities, or about particular funds or transactions; and
  - an optional cash flow statement.
29. The SORP has a number of core modules to which all charities must refer when preparing their accounts and trustees' annual report. Supplementing these core modules, there are additional modules that apply only when a charity:
- undertakes a specific type of transaction;
  - needs to recognise, measure or disclose a specific asset or liability in a particular way;
  - has particular forms of investment; or
  - adopts a particular legal form or group structure.
30. When preparing their accounts, charities must refer to the index of modules to ensure that they identify all of the SORP's recommendations that apply to their transactions, assets and liabilities. This should be done for each reporting period and whenever a charity undertakes a new type of transaction. In particular, charities must select those modules that apply to their specific transactions and circumstances.
31. This SORP provides guidance to charities on the application of the FRSSE and also provides recommendations on accounting and reporting of charity-specific transactions that are not addressed within the FRSSE.
32. The SORP also offers advice on how a charity may disclose particular issues and provides examples or suggested layouts of particular notes which a charity may choose to follow.
33. See the SORP module '[Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors](#)' for details of the SORP compliance statement that a charity must provide within its accounting policy note and the additional disclosures that it must make in the event of a departure from the SORP's provisions.

### Use of the terms 'must', 'should' and 'may'

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34. This SORP uses different terms to distinguish those requirements that must be followed in order to comply with the SORP from other recommendations which charities can opt to follow when preparing the trustees' annual report and accounts.
35. This SORP uses the term 'must' to indicate those elements that are important to the reader of the trustees' annual report that must be included within the report or to identify particular accounting treatments, disclosures or presentational requirements that are likely to affect the ability of the accounts to give a true and fair view if not applied to material transactions or items. Where this SORP states that a recommendation is one which must be followed, non-adherence to that recommendation is a departure from this SORP.

## *Accounting and reporting by charities*

36. This SORP uses the term 'should' for an item in the trustees' annual report or the accounts for those recommendations aimed at advancing standards of financial reporting as a matter of good practice. While charities are encouraged to follow all the SORP's recommendations, a failure to follow a 'should' recommendation with respect to the report or the accounts is not regarded as a departure from this SORP.
37. This SORP uses the term 'may' for an item in the trustees' annual report or an approach to a particular disclosure that a charity may choose to adopt or identifies that an alternative accounting treatment or disclosure of a transaction or event is allowed by the SORP. Charities may choose whether such examples or alternative treatments are adopted at their discretion.



## **Index of SORP modules**

	Paragraph numbers
<b>Core modules</b>	
Trustees' annual report	1.1-1.54
Fund accounting	2.1-2.31
Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors	3.1-3.44
Statement of financial activities	4.1-4.60
Recognition of income, including legacies, grants and contract income	5.1-5.51
Donated goods, facilities and services, including volunteers	6.1-6.32
Recognition of expenditure	7.1-7.42
Allocating costs by activity in the statement of financial activities	8.1-8.14
Disclosure of trustee and staff remuneration, related party and other transactions	9.1-9.32
Balance sheet	10.1-10.91
Accounting for financial assets and financial liabilities	11.1-11.15
Write-down of assets to their recoverable amounts	12.1-12.22
Post balance sheet events	13.1-13.8
Cash flow statement	14.1-14.10
<b>Selection 1: Special transactions relating to charity operations</b>	
Charities established under company law	15.1-15.18
Presentation and disclosure of grant-making activities	16-1-16.25
Retirement benefits	17.1-17.23
<b>Selection 2: Accounting for special types of assets held</b>	
Accounting for heritage assets	18.1-18.33
Accounting for funds received as agent or as custodian trustee	19.1-19.14

**Selection 3: Accounting for investments**

Total return (investments)	20.1-20.12
Accounting for social investments	21.1-21.41
Accounting for charities pooling funds for investment	22.1-22.12

**Selection 4: Accounting for branches, charity groups and combinations**

Overview of charity combinations	23.1-23.5
Accounting for groups and the preparation of consolidated accounts	24.1-24.39
Branches, linked or connected charities and joint arrangements	25.1-25.26
Charities as subsidiaries	26.1-26.7
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**Appendices**

Appendix 1: Glossary of terms

Appendix 2: The Charity Accounting (SORP) Committee

Appendix 3: Thresholds for the UK and the Republic of Ireland

## **FRC's Statement on the Charities SORP (FRSSE)**

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The aim of the Financial Reporting Council (FRC) is to promote high-quality corporate governance and reporting to foster investment. In relation to accounting standards applicable in the UK and Republic of Ireland the FRC's overriding objective is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs. In particular industries or sectors, clarification of aspects of those standards may be needed in order for the standards to be applied in a manner that is relevant and provides useful information to users of financial statements in that industry or sector.

Such clarification is issued in the form of Statements of Recommended Practice (SORPs) by bodies recognised for this purpose by the FRC. The Charity Commission and the Office of the Scottish Charity Regulator (OSCR) in their role as the joint SORP-making body have confirmed that it shares the FRC's aim of high-quality financial reporting and has been recognised by the FRC for the purpose of issuing SORPs for charities.

In accordance with the FRC's Policy and Code of Practice on SORPs the FRC carried out a limited scope review of the SORP focusing on those aspects relevant to the financial statements.

On the basis of its review, the FRC has concluded that the SORP has been developed in accordance with the FRC's Policy and Code of Practice on SORPs and does not appear to contain any fundamental points of principle that are unacceptable in the context of present accounting practices or to conflict with an accounting standard.

22 May 2014

Financial Reporting Council

# 1. Trustees' annual report

## Overview and the purpose of the trustees' annual report

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- 1.1. The FRSSE does not specify any requirements for narrative reporting or for the content of a trustees' annual report by charities. This module specifies this SORP's requirements for a trustees' annual report and its content and applies to all charities adopting this SORP.
- 1.2. The primary purpose of the trustees' annual report (the report) is to ensure that the charity is publicly accountable to its stakeholders for the stewardship and management of the funds it holds on trust. The trustees should consider the information needs of the primary users of their report. These may vary from charity to charity but will normally include funders, donors, financial supporters, service users and other beneficiaries.
- 1.3. The report should be a coherent document that meets the requirements of law and regulation. It should provide a fair, balanced and understandable review of the charity's structure, legal purposes, objectives, activities, financial performance and financial position. Good reporting explains what the charity is set up to do, how it is going about it, and what is achieved as a result of its work. The report should assist the user to make economic decisions in relation to the charity and to assess the charity's progress against its objectives and to understand its plans in relation to its purposes.
- 1.4. For the report to be prepared in accordance with this SORP, charities are required to comply with all the applicable reporting requirements prefixed with a 'must'. This module distinguishes those requirements that all charities must comply with from those more detailed reporting requirements applicable to larger charities subject to audit.
- 1.5. Legal requirements and the requirements of this SORP do not limit the inclusion of other information within the report or the provision of additional information accompanying the accounts (financial statements). A charity may include other relevant material in the report, for example a Chairman's Report, an environmental report, or an impact assessment.
- 1.6. Trustees of charitable companies must also prepare a directors' report as required by company law (see section 18 of the FRSSE). A separate trustees' annual report is not required provided that any statutory directors' report prepared also contains all the information that this SORP requires to be provided in the trustees' annual report.
- 1.7. This module sets out:
  - who is responsible for preparing the trustees' annual report?;
  - reporting by smaller charities;
  - the context for reporting;
  - the content of the trustees' annual report required of all charities;
  - the provision of other information; and
  - the additional content required of larger charities.

## Who is responsible for preparing the trustees' annual report?

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- 1.8. The responsibility for preparing the report rests with the charity's trustees. Although trustees may seek the assistance of the charity's staff or advisers in drafting the report, the trustees must approve the final text of the report.
- 1.9. The report provides important accompanying information to the accounts and therefore should be provided whenever a full set of accounts is distributed or otherwise made available. The report must identify the reporting period (financial year) of the charity to which it relates and the date of its approval. One or more of the charity's trustees must sign and date the report on behalf of the trustees upon their approval of the report.

## Reporting by smaller charities

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- 1.10. The reporting requirements take account of the size of the charity. Less information is required of smaller charities. Smaller charities are those not subject to statutory audit under charity law in their jurisdiction(s) of formation, operation or registration. This module uses the term 'all charities' to identify those elements of the report that both smaller and larger charities must provide.
- 1.11. Smaller charities are encouraged to include some or all of the additional information required of larger charities if the charity trustees consider such additional information relevant to their charity's stakeholders.

## The context for reporting

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- 1.12. The report provides an essential link between a charity's legal purposes and the charity's aims and objectives and the activities it undertakes to achieve them. It should focus on information relevant to the charity's stakeholders and tell the charity's story in a balanced manner, acknowledging both significant successes and failures. Trustees may present the contents of their report in any order and under any headings that they choose.
- 1.13. Good reporting provides a context within which to interpret the accounts and links the activities and achievements reported with the sources of income used to finance them and the expenditure incurred on those activities. A charity's accounts focus on its financial position and financial performance. In isolation this information does not give the user a rounded overview of what has been achieved from the charity's activities and the resources used in their delivery. The report and accounts taken together should provide a picture of what the charity has done (its outputs) or achieved (its outcomes), or what difference it has made (its impact).
- 1.14. Parent charities preparing consolidated accounts must expand their report to include relevant information about their subsidiary undertakings.

## The content of the trustees' annual report required of all charities

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- 1.15. The SORP's requirements that all charities must follow are set out in the following headings:
- objectives and activities;
  - achievements and performance;
  - financial review;
  - structure, governance and management;
  - reference and administrative details;
  - exemptions from disclosure; and
  - funds held as custodian trustee on behalf of others.
- 1.16. The headings used in the report may be amended to fit the preferences of the charity provided the information required by this module is clearly presented in the report.
- 1.17. Larger charities must also refer to the section 'The additional content required of larger charities' for their report to be compliant with the SORP.

### **Objectives and activities**

- 1.18. The report provides information intended to help the user understand how the charity's aims fulfill its legal purposes, the activities it undertakes and what it has achieved. All charities must provide a summary of:
- the purposes of the charity as set out in its governing document; and
  - the main activities undertaken in relation to those purposes.
- 1.19. Charities in England and Wales must also:
- explain the main activities undertaken to further the charity's purposes for the public benefit; and
  - include in their report, a statement confirming whether the trustees have had regard to the Charity Commission's guidance on public benefit.
- 1.20. The report should explain the activities, projects or services identified in the accompanying accounts. As far as practicable, numerical information provided in the report about the resources spent on particular activities should be consistent with the analysis provided in the accounts.

### **Achievements and performance**

- 1.21. The report must contain a summary of the main achievements of the charity. The report should identify the difference the charity's work has made to the circumstances of its beneficiaries and, if practicable, explain any wider benefits to society as a whole.

### **Financial review**

- 1.22. The report must contain a review of the charity's financial position at the end of the reporting period.

## *Accounting and reporting by charities*

- 1.23. The charity must explain any 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.
- 1.24. If, at the date of approving the report and accounts, there are uncertainties about the charity's ability to continue as a going concern, the nature of these uncertainties should be explained.
- 1.25. The report must also identify any fund or subsidiary undertaking that is materially in deficit, explaining the circumstances giving rise to the deficit and the steps being taken to eliminate the deficit.

### **Structure, governance and management**

- 1.26. The report must provide details of:
  - the nature of the governing document (e.g. trust deed, memorandum and articles of association, Charity Commission scheme, Royal Charter, etc.);
  - how the charity is (or its trustees are) constituted (e.g. limited company, unincorporated association, trustees incorporated as a body, charitable incorporated organisation, community benefit society, industrial and provident or friendly society etc.); and
  - the methods used to recruit and appoint new charity trustees, including details of any constitutional provisions for appointment, for example election to post. Where any other person or external body is entitled to appoint one or more of the charity trustees, the report should explain this and give the name of that person or body.
- 1.27. Charities may withhold certain governance and management details where the criteria for exemption from disclosure are satisfied (see 'Exemptions from disclosure').

### **Reference and administrative details**

- 1.28. The report must provide the following reference and administrative information about the charity and its trustees:
  - the name of the charity, which in the case of a registered charity means the name by which it is registered;
  - any other name which the charity uses;
  - the charity registration number(s) for the jurisdiction(s) in which it is registered as a charity and, if applicable, its company registration number;
  - the address of the principal office of the charity and, in the case of a charitable company, the address of its registered office;
  - the names of all those who were the charity's trustees on the date the report was approved or who served as a trustee in the reporting period;
  - where a charity has any corporate trustees, the names of the directors of the body corporate on the date the report was approved; and

## Accounting and reporting by charities

- the names of any trustee for the charity holding the title to property belonging to the charity (for example custodian trustee or nominee) on the date the report was approved; or
- who served as a trustee for the charity in holding the title to property belonging to the charity in the reporting period.

1.29. Charities may withhold certain reference and administrative details where the criteria for exemption from disclosure are satisfied (see 'Exemptions from disclosure').

### Exemptions from disclosure

1.30. On occasions, the disclosure of the names of trustees or of the charity's principal address or the disclosure of the name(s) of any chief executive officer or other senior staff member(s) could lead to that person (or others) being placed in personal danger (e.g. in the case of a women's refuge). In such circumstances, the applicable law and regulations may permit the withholding of these details. Where a report omits the name of a trustee, chief executive officer or senior staff member or the charity's principal address, it should give the reason for the omission.

1.31. Charities in England and Wales may omit the names of those persons and the charity's principal address from their report provided the Charity Commission has given the charity trustees the authority to do this. In Scotland there is also a provision under charity law for such information to be excluded.

1.32. The directors of charitable companies registered in the UK should note that, with the exception of the name of the auditor, or senior statutory auditor in the case of an audit firm (section 506 Companies Act 2006), there is no corresponding dispensation in relation to the disclosure of names.

### Funds held as custodian trustee on behalf of others

1.33. If a charity is, or its trustees are, acting as custodian trustees, the charity must refer to the SORP module '[Accounting for funds received as agent or as custodian trustee](#)'.

### The provision of other information

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1.34. Charities often use other means of providing information, outside of the statutory reporting framework, to provide information about the charity and what the charity is doing. Such information is often tailored to the needs of particular audiences and presented through annual reviews, newsletters and websites. While charity trustees might usefully refer to these other sources of information within their report, such additional information is not a substitute for good statutory reporting.

### The additional content required of larger charities

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1.35. A greater degree of public accountability and stewardship reporting is expected of larger charities. Larger charities in compiling their report must meet the requirements placed on all charities as set out above and also provide the additional information detailed under the following headings:



- objectives and activities;
- achievements and performance;
- financial review;
- plans for future periods;
- structure, governance and management; and
- reference and administrative details.

### **Objectives and activities**

- 1.36. Good reporting provides a coherent explanation of the charity's strategies for achieving its aims and objectives and explains how the activities it undertook contributed to their achievement.
- 1.37. In particular, the report of larger charities must provide an explanation of:
- its aims, including details of the issues it seeks to tackle and the changes or differences it seeks to make through its activities;
  - how the achievement of its aims will further its legal purposes;
  - its strategies for achieving its stated aims and objectives;
  - the criteria or measures it uses to assess success in the reporting period; and
  - the significant activities undertaken (including its main programmes, projects or services provided), explaining how they contribute to the achievement of its stated aims and objectives.
- 1.38. Larger charities in their report should also provide the user with a more detailed understanding of their short-term and longer-term aims and objectives. A charity with longer-term aims and objectives should explain how the aims and objectives set for the reporting period relate to its longer-term aims and objectives. When explaining activities, it is important for the user to understand their scale and the resources used in their delivery; for example, it may be helpful to provide details of the amount spent on, or the number of staff engaged in, undertaking a particular activity.
- 1.39. The report must include an explanation of the use the charity makes of the following:
- Social investment, when this forms a material part of its charitable and investment activities. In particular, the report must provide an explanation of its social investment policies and explain how any programme related investments contributed to the achievement of its aims and objectives.
  - Grant-making, when this forms a material part of its charitable activities. In particular, the report must explain the charity's grant-making policy and explain how its grant-making activities contribute to the achievement of its aims and objectives.

## *Accounting and reporting by charities*

- Volunteers, when their contribution is significant to a charity's ability to undertake a particular activity. The explanation should help the user to understand the scale and nature of the activities undertaken. However, measurement issues, including attributing an economic value to the contribution of general volunteers, prevent the inclusion of their contribution in the statement of financial activities (see the SORP module '*Donated goods, facilities and services, including volunteers*').

1.40. Charities reporting on the contribution of general volunteers may provide:

- an explanation of the activities that volunteers support or help to provide; and
- details of the contribution in terms of volunteer hours or staff equivalents.

### **Achievements and performance**

1.41. Good reporting sets out how well the activities undertaken by the charity and any subsidiaries performed and the extent to which the achievements in the reporting period met the aims and objectives set by the charity for the reporting period. Good reporting provides a balanced view of successes and failures along with the supporting evidence, and demonstrates the extent of performance and achievement against the objectives set and the lessons learned.

1.42. In particular, the report must review:

- the significant charitable activities undertaken;
- the achievements against objectives set;
- the performance of material fundraising activities against the fundraising objectives set;
- investment performance against the investment objectives set where material financial investments are held; and
- if material expenditure was incurred to raise income in the future, the report must explain the effect this expenditure has had, and is intended to have, on the net return from fundraising activities for both the reporting period and future periods.

1.43. The report should provide a balanced picture of a charity's progress against its objectives. For example, it may explain progress by reference to the indicators, milestones and benchmarks the charity uses to assess the achievement of objectives.

1.44. In reviewing achievements and performance, charities may consider the difference they have made by reference to terms such as inputs, activities, outputs, outcomes and impacts, with impact viewed in terms of the long-term effect of a charity's activities on both individual beneficiaries and at a societal level. Charities are encouraged to develop and use impact reporting (impact, arguably, being the ultimate expression of the performance of a charity), although it is acknowledged that there may be major measurement problems associated with this in many situations.

- 1.45. In reviewing its achievements and performance, the charity should include a summary of the measures or indicators used to assess performance when it provides evidence of the achievements in the reporting period. Explaining the outputs achieved by particular activities can be helpful, particularly when numerical targets have been set. Examples of such targets include the number of beneficiaries to be reached by a particular programme, or the number of events or interventions planned as part of an activity. However, information on activities, outputs and outcomes (or impacts) should always be put in the context of how they have contributed to the achievement of the charity's aims and objectives.
- 1.46. The report should comment on those significant positive and negative factors both within and outside the charity's control which have affected the achievement of its objectives and, where relevant, explain how this has affected future plans. These factors might include relationships with employees, service users, beneficiaries and funders and the charity's position in the wider community.

### **Financial review**

- 1.47. The report must also comment on the significant events that have affected the financial performance and financial position of the charity during the reporting period. In particular the report must explain:
- the financial effect of significant events;
  - where the charity holds material financial investments, the investment policy and objectives set;
  - a description of the principal risks and uncertainties facing the charity and its subsidiary undertakings, as identified by the charity trustees, together with a summary of their plans and strategies for managing those risks; and
  - any factors that are likely to affect the financial performance or position going forward.
- 1.48. The financial review should also explain:
- the principal funding sources of the charity in the reporting period and how these resources support the key objectives of the charity;
  - the impact, if any, of a material pension liability arising from obligations to a defined benefit pension scheme or pension asset on the financial position of the charity; and
  - where the charity holds material financial investments, the extent (if any) to which it takes social, environmental or ethical considerations into account in its investment policy.
- 1.49. The review of the charity's reserves should:
- state the amount of the total funds the charity holds at the end of the reporting period;
  - identify the amount of any funds which are restricted and not available for
  - general purposes of the charity at the end of the reporting period;

## *Accounting and reporting by charities*

- identify and explain any material amounts which have been designated or otherwise committed as at the end of the reporting period;
- indicate the likely timing of the expenditure of any material amounts designated or otherwise committed at the end of the reporting period;
- identify the amount of any fund that can only be realised by disposing of tangible fixed assets or programme related investments;
- state the amount of reserves the charity holds at the end of the reporting period after making allowance for any restricted funds, and the amount of designations, commitments (not provided for as a liability in the accounts) or the carrying amount of functional assets which the charity considers to represent a commitment of the reserves they hold; and
- compare the amount of reserves with the charity's reserves policy and explain, where relevant, what steps it is taking to bring the amount of reserves it holds into line with the level of reserves identified by the trustees as appropriate given their plans for the future activities of the charity.

### **Plans for future periods**

- 1.50. The report must provide a summary of the charity's plans for the future, including its aims and objectives and details of any activities planned to achieve them.
- 1.51. The report should explain the trustees' perspective of the future direction of the charity. It should explain, where relevant, how experience gained or lessons learned from past or current activities have influenced future plans and decisions about allocating resources to their best effect.

### **Structure, governance and management**

- 1.52. The report must provide the user with an understanding of how the charity is constituted, its governance and management structures, and how its trustees are trained. In particular, the report must explain:
- the charity's organisational structure and, where relevant, those of its subsidiary undertakings;
  - how the charity makes decisions, for example which types of decisions are taken by the charity's trustees and which are delegated to staff;
  - the policies and procedures for the induction and training of trustees;
  - the arrangements for setting the pay and remuneration of the charity's key management personnel and any benchmarks, parameters or criteria used in setting their pay;
  - if the charity is part of a wider network (for example if it is affiliated with an umbrella group), how, if at all, this impacts on the operating policies adopted by the charity; and
  - relationships between the charity and related parties, including its subsidiary undertakings, and with any other charities and organisations with which it co-operates in the pursuit of its charitable objectives.

## **Reference and administrative details**

1.53. The report must state to whom the trustees' delegate day-to-day management of the charity and from whom trustees are taking advice. In particular, the report must provide:

- the name of any chief executive officer or other senior management personnel to whom the charity trustees delegate day-to-day management of the charity on the date the report was approved or who served in such a position in the reporting period in question; and
- the names and addresses of any other relevant organisations or persons providing banking services or professional advice to the charity, including its solicitors, auditor and investment advisers.

1.54. Certain details may be withheld where the criteria for exemption from disclosure as set out in the 'Exemptions from disclosure' are met.

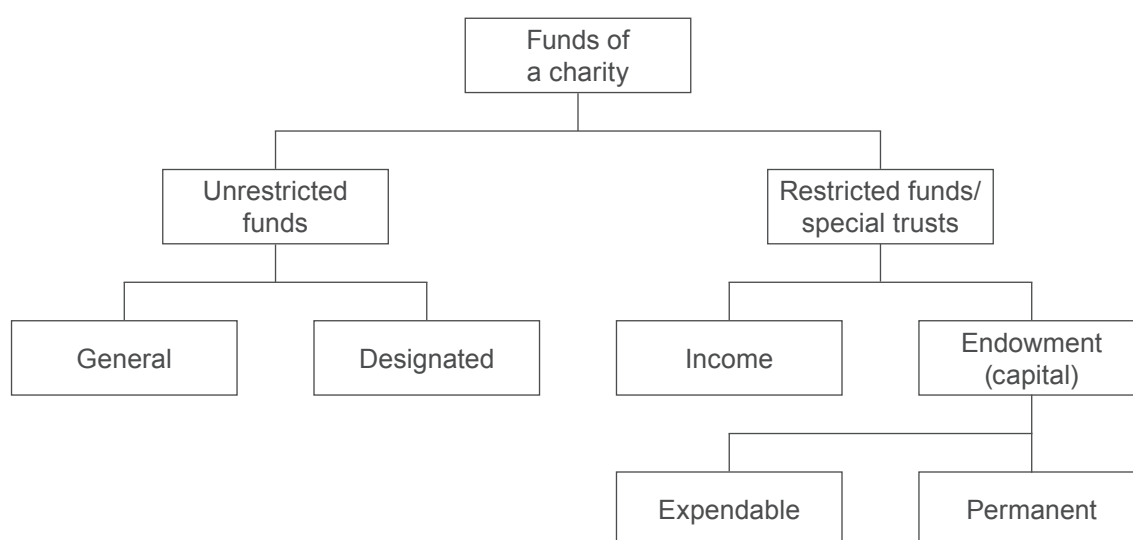
## 2. Fund accounting

### Introduction

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- 2.1. The FRSSE does not deal with fund accounting by charities. This module sets our current practice for the analysis and presentation of a charity's funds which applies to charities adopting this SORP.
- 2.2. Accounting for the particular charitable funds held by a charity is a key feature of charity accounting. Each class of fund has unique characteristics in trust law. Fund accounting distinguishes between two primary classes of fund: those that are unrestricted in their use, which can be spent for any charitable purposes of a charity, and those that are restricted in use, which can only be lawfully used for a specific charitable purpose.
- 2.3. The proper administration of individual charitable funds is essential if charity trustees are not to act in breach of trust.
- 2.4. Restricted funds (also known as special trusts in England and Wales) are further analysed between restricted income funds and endowment funds (also known as capital funds). Figure 1 sets out these classes of fund diagrammatically. This differentiation of funds is an essential feature in the presentation of a charity's statement of financial activities (SoFA) and balance sheet.

**Figure 1: The classes of charitable funds**



- 2.5. This module sets out:
  - general principles of fund accounting;
  - transfers between funds; and
  - fund disclosures in the notes to the accounts.

## General principles of fund accounting

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- 2.6. A prerequisite of fund accounting is an understanding of the different classes of funds a charity may hold on trust. A charity may hold both unrestricted and restricted funds. Income generated by the investment of a particular fund's assets accrues to that fund unless the terms of the initial gift provide otherwise, for example in the case of permanent endowment. Similarly, any Gift Aid amount recovered on a donation forms part of that gift and is an addition to the same fund as the initial donation unless the donor or the terms of the appeal have specified otherwise.

### **Unrestricted funds**

- 2.7. Unrestricted funds are spent or applied at the discretion of the trustees to further any of the charity's purposes. Unrestricted funds can be used to supplement expenditure made from restricted funds. For example, a restricted grant may have provided part of the funding needed for a specific project. In this case unrestricted funds may be used to meet any funding shortfall for that project.
- 2.8. Trustees may choose during the reporting period to set aside a part of the unrestricted funds to be used for a particular future project or commitment. By earmarking funds in this way, the trustees set up a designated fund that remains part of the unrestricted funds of the charity. This is because the designation has an administrative purpose only and does not legally restrict the trustees' discretion in how to apply the unrestricted funds that they have earmarked. Identifying designated funds may be helpful when explaining the charity's reserve policy and the level of reserves it holds.

### **Restricted funds**

- 2.9. Funds held on specific trusts under charity law are classed as restricted funds. The specific trusts may be declared by the donor when making the gift or may result from the terms of an appeal for funds. The specific trusts establish the purpose for which a charity can lawfully use the restricted funds. It is possible that a charity may have several individual restricted funds, each for a particular purpose of the charity.
- 2.10. In certain circumstances the donor may express a form of non-binding preference as to the use of the funds, which falls short of imposing a restriction in trust law. In which case the charity will include the funds as part of its unrestricted funds. To respect these non-binding donor wishes, trustees may decide to designate those funds to reflect the purposes which the donor had in mind.
- 2.11. Some trustees have the power to declare special trusts over unrestricted funds. Where such a power is available to the trustees and they use it, the assets affected will form part of the restricted funds as a special trust. The trustees' discretion to apply that fund will then be legally restricted.

- 2.12. Restricted funds fall into one of two sub-classes: restricted income funds or endowment funds. Restricted income funds are to be spent or applied within a reasonable period from their receipt to further a specific purpose of the charity, which is to further one or more but not all of the charity's charitable purposes. Alternatively, the restricted fund may be an endowment. Trust law requires a charity to invest the assets of an endowment, or retain them for the charity's use in furtherance of its charitable purposes, rather than apply or spend them as income (see 'Endowment funds' below).
- 2.13. When a tangible fixed asset is funded through an appeal or by way of a grant or donation, the accounting treatment of the asset acquired will depend on the circumstances of each case. In deciding whether the asset is categorised as restricted or unrestricted, trustees should consider whether the terms of the gift:
- require the charity to hold the tangible fixed asset acquired on an on-going basis for a specific purpose; or
  - are met once the specified asset is acquired, so allowing the charity to use the asset acquired on an unrestricted basis for any charitable purpose.
- 2.14. In some circumstances the trustees may be able to settle a tangible fixed asset on trust for a specific purpose implied by the appeal, provided this is consistent with the charity's governing instrument. Where this happens, the trustees' decision is legally binding and the asset is an addition to the restricted funds.
- 2.15. In maintaining the accounting records, charities must separately identify each restricted fund and the income received and expenditure made from each restricted fund.
- 2.16. Costs charged to a restricted fund relate to the activities undertaken to further the specific charitable purposes the fund was established to support. These costs include both direct and support costs associated with the activities undertaken by the restricted fund(s). In addition to a reasonable allocation of support costs, other costs associated with raising, investing and managing the restricted funds should normally be charged to the fund to which the cost relates. Expenditure attributable to a restricted fund may still be charged to it even if there is an insufficient balance on that fund at the time. However, expenditure should only be charged to a restricted fund in deficit when there is a realistic expectation that future income will be received to cover the shortfall, for example when a decision has been made to invite donations to that restricted fund.

### **Endowment funds**

- 2.17. A gift of endowment, where there is no power to convert the capital into income, is known as a permanent endowment fund. A permanent endowment fund must normally be held indefinitely. Where trustees have the power to convert endowment funds into income, such funds are known as expendable endowments. A gift of expendable endowment provides the trustees with a power to convert all or part of it into income.
- 2.18. Expendable endowment is distinguishable from income funds in that there is no actual requirement to spend or apply the capital unless, or until, the trustees decide to spend it. If the trustees exercise the power to spend or apply the capital of the expendable endowment, the relevant funds become unrestricted funds or restricted income funds depending on whether the terms of the gift permit expenditure for any of the charity's purposes, or only for specific purposes.



## *Accounting and reporting by charities*

- 2.19. The income generated from endowment funds held for investment must be spent on furthering its charitable purposes unless the charity exercises a power of accumulation or a charity in England and Wales has invested the endowment on a total return basis (see the SORP module 'Total return (investments)') under the provisions of section 104A of the Charities Act 2011 as amended by the Trust (Capital and Income) Act 2013 or an Order of the Charity Commission made under section 105 of the Charities Act 2011. If there is no restriction as to the use of the income, the income is an addition to unrestricted funds. It is possible that a charity may have several endowment funds; the income from each endowment being restricted to a particular purpose.
- 2.20. The concept of permanence does not mean that a charity must keep holding the assets in the endowment funds in the form that they were initially given. The investments or property held within an endowment fund can be changed. For example, a charity could sell a particular equity investment and reinvest the proceeds in a different financial asset, or it might use the proceeds from the sale of endowed freehold land and buildings to purchase a new freehold property which will then form part of the endowment.
- 2.21. In some cases the permanent endowment's trusts will require the retention of a specific asset for the charity's own use, for example, a building. It follows that an endowed asset may be capable of depreciation or impairment. Trustees that use income funds to build, erect, extend or improve a building on land which is an endowment asset should note that the default position is that the value of the enhancement to the asset will form part of the endowment in the absence of evidence to the contrary.

### **Accounting for expenses related to endowment**

- 2.22. A charity cannot use permanent endowment as if it were income, for example to make payments or grants to third parties. Trust law only permits expenses to be charged to permanent endowment when incurred in the administration or protection of the investments or property of the endowment, for example:
- fees incurred in managing the investment of the endowment;
  - the costs of valuation fees and expenses incurred in connection with the sale of endowed land;
  - the cost of improvements to land held as an endowment investment; or
  - the loss of value due to depreciation or impairment of an endowed property.
- 2.23. If the endowment has insufficient funds to meet the expenses that can be charged to it, or the terms of the trust of the endowed gift prohibit the charging of expenses, then the expenses must be charged to income funds. Other expenses must normally be charged to income funds.

### **Accounting for the investment return on income and endowment funds**

- 2.24. The return on investment is made up of the income derived from the investment (interest, dividends, royalties or rents) and any gain or loss in the market value of the investment. If a charity sells an investment, a gain or loss on the carrying amount of the asset is realised upon its disposal. Where a charity retains an investment, an unrealised gain or loss on the carrying amount of the investment may arise at the balance sheet date.

- 2.25. For unrestricted funds and restricted income funds, trust law requires both the income and any investment gain or loss to be allocated to the fund holding the investment. Where the charity has a number of individual restricted income funds, any investment income and gain or loss on investments must be allocated to the individual restricted funds holding the investment.
- 2.26. Trust law applies different rules to endowment funds. In the case of endowment, trustees cannot add the income from investments to the endowment capital except where they have a power to invest on a total return basis (see the SORP module 'Total return (investments)') or exercise a power of accumulation. Instead, the income from the investment is allocated to either unrestricted funds or a restricted income fund depending on the terms of the gift. However, any gain or loss on investment is attributed to the endowment capital. If a charity has several invested endowments, any gain or loss on investments must be allocated correctly to each individual endowment.

### Transfers between funds

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- 2.27. The transfer line in the SoFA is used to record transfers between funds. The total transfers recorded between classes of fund in the reporting period must always net to nil. A transfer may be made for several reasons, including:
- to transfer assets from unrestricted funds to finance a deficit on a restricted fund;
  - to transfer the value of tangible fixed assets from restricted to unrestricted funds when the asset has been purchased from a restricted fund donation but is held for a general and not a restricted purpose;
  - where restricted funds have been lawfully released and transferred to unrestricted funds;
  - where the trustees have exercised a power to declare a special trust over a gift initially recognised as unrestricted; or
  - where charity law permits the proceeds of restricted funds to be spent for an alternative purpose (such as the *cy près* procedures in England and Wales), for example the alternative use of the proceeds of a failed appeal, or the alternative use of excess of funds raised from an appeal.

### Fund disclosures in the notes to the accounts

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- 2.28. For the proper administration of charitable funds, the accounting records of a charity must identify the transactions for each of the funds held. This SORP requires that items recorded in the SoFA must be analysed between unrestricted funds, restricted income funds and endowment funds. The information for endowment funds provided in the SoFA should combine the presentation of permanent and expendable endowment.
- 2.29. This SORP requires that the notes to the accounts must provide information on material individual fund balances, movements in the reporting period and the purposes for which the funds are held. The notes must differentiate unrestricted funds (both general and designated), restricted income funds, permanently endowed funds and expendable endowments. Table 1, 'Outline summary of fund movements' gives an example of how the movements in material funds may be shown.

## Accounting and reporting by charities

2.30. In particular, this SORP requires that notes to the accounts must disclose:

- a summary of the assets and liabilities of each category of fund of the charity, if not provided by presenting this information in a columnar balance sheet;
- details of the purposes and trust law restrictions imposed on each material individual fund;
- details of the movements on material individual funds in the reporting period, reconciling the opening and closing fund balance (small funds with similar purposes may be aggregated);
- details of the reasons for any material transfers between different classes of funds;
- where endowment has been converted to income, details of the amount(s) converted and the legal power for its conversion;
- where the trustees have a power to invest permanent endowment on a total return basis, the details of the movements in the value of unapplied total return for the reporting period (refer to the SORP module 'Total return (investments)'); and
- details of the planned use of any material designated funds, explaining the purpose of the designation.

2.31. In deciding on the most suitable form of presentation, the charity should consider:

- the complexity of the fund structure; and
- the need for any separate fund statement(s) or note(s) to agree with the charity's SoFA and balance sheet.

**Table 1: Outline summary of fund movements**

Fund name	Fund balances brought forward	Income	Expenditure	Transfers	Gains and losses	Fund balances carried forward
	£	£	£	£	£	£
Fund 1						
Fund 2						
Fund 3						
Other funds						
<b>Total funds</b>						

### **3. Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors**

#### **Introduction**

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- 3.1. This module explains how accounting standards, policies, concepts and principles are applied by charities adopting the FRSSE. Charities adopting this SORP should also refer to section 2 of the FRSSE.
- 3.2. Accounting policies provide the basis on which the accounts are prepared and explain the accounting treatment of material transactions or items in the accounts. The concept of materiality is an important consideration when selecting accounting policies. Materiality relates to the financial information provided in the accounts and an item is material when its omission or misstatement could influence the economic decisions that users make on the basis of those accounts.
- 3.3. This module sets out:
- what are accounting standards, policies, concepts and principles?;
  - length of the reporting period;
  - presentation currency;
  - going concern;
  - prudence;
  - accruals;
  - materiality;
  - offsetting;
  - prior period adjustments;
  - selection of accounting policies;
  - compliance with the SORP; and
  - disclosure of accounting policies, changes in estimation techniques and prior period adjustments.

#### **What are accounting standards, policies, concepts and principles?**

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- 3.4. Accounting standards set out the basis for recognising and measuring assets, liabilities, income and expenses and for their disclosure in accounts. Charities preparing accounts in accordance with the FRSSE and this SORP will normally, in so doing, meet the relevant legal requirements for their accounts to give a true and fair view of their financial position and activities.

## *Accounting and reporting by charities*

- 3.5. Accounting policies are the principles, bases, conventions, practices and rules by which transactions and items are recognised, measured and presented in the accounts. The accounting policies adopted by a charity using the FRSSE must follow the requirements of that accounting standard unless the effect of not following a particular requirement would be immaterial, or in special circumstances, where to do so would conflict with the legal obligation for the accounts to give a 'true and fair' view.
- 3.6. The SORP supplements the FRSSE and has been developed in the light of the special factors prevailing or transactions undertaken within the charity sector.
- 3.7. Charities using the FRSSE must prepare their accounts on the accruals basis of accounting. In certain jurisdictions, it is a legal requirement for charities preparing their accounts on an accruals basis to adhere to the methods and principles of this SORP. Charities should refer to the guidance issued by the charity regulator in their jurisdiction(s) of registration to find out whether they are subject to a legal requirement to follow this SORP.
- 3.8. Accounting policies are supplemented by estimation techniques where judgement is required to establish the monetary amounts of assets, liabilities, gains and losses included in the accounts.
- 3.9. Charity accounts must be prepared on a timely basis and be presented in a way that makes financial information understandable to users who have a reasonable knowledge of charity financial management and/or accounting and a willingness to study the information with reasonable diligence.
- 3.10. The accounts must present financial information that is relevant, reliable, comparable and understandable. Information should not be excluded simply because it is complicated; however, the preparer should also balance the cost of obtaining information with the benefit it provides both internally to management and externally to funders and other stakeholders.
- 3.11. Transactions and events must also be accounted for with prudence and presented in a way that represents their substance and not merely their legal form. This will require the exercise of judgement and may on occasion dictate the disclosure of more information than specifically recommended in this SORP.

### Length of the reporting period

- 3.12. All charities must prepare a set of accounts annually and they should normally have a 12-month reporting period. If the accounts are prepared for a shorter or longer reporting period, this SORP requires that a charity must disclose:
  - that the reporting period is for less than or more than 12 months;
  - the reason for the shorter or longer reporting period;
  - the legal authority it has for the change to its reporting period; and
  - the fact that the comparative amounts presented in the accounts (including the related notes) are not entirely comparable.

## Presentation currency

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- 3.13. The presentation currency is the currency in which the accounts are denominated. A charity should normally prepare its accounts in the currency of the jurisdiction of its administration unless it operates predominantly by generating and spending its cash in a different currency. Where a charity operates predominantly in a different currency, it should prepare its accounts in that currency.

## Going concern

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- 3.14. Charities normally prepare their accounts on the basis of being a going concern. However, when preparing accounts, the FRSSE requires that trustees must assess whether there are significant doubts about the charity's ability to continue as a going concern. Any material uncertainties, of which the trustees are aware in making their assessment, must be disclosed. Where the period considered by the trustees in making this assessment has been limited to a period of less than one year from the date of approval of the accounts, that fact shall be stated. Accounts must not be prepared on a going concern basis if the trustees determine after the balance sheet date either that they intend to liquidate the charity or to cease its activities, or that they have no realistic alternative but to do so.

## Prudence

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- 3.15. The preparation of accounts may involve the exercise of the judgments in making the estimates required under conditions of uncertainty. Prudence requires that a degree of caution is exercised in making judgments to ensure that gains and assets are not overstated and liabilities are not understated. However it is not necessary to exercise prudence where there is no uncertainty. Nor is it appropriate to use prudence as a reason to understate deliberately assets or gains or overstate liabilities or losses.

## Accruals

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- 3.16. Accounts, with the exception of cash flow information, must be prepared on the accruals basis of accounting. Hence, all income and charges relating to the financial year must be brought into the accounts without regard to the date of payment or receipt.

## Materiality

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- 3.17. The FRSSE and this SORP set certain accounting treatments and disclosures in the context of their materiality. Charities, in preparing their accounts, should therefore give particular consideration to material items or transactions as their omission or misstatement could influence economic decision-making by the user of the accounts and any assessment of the stewardship of charitable funds. An omission or misstatement of a material item may result in the accounts failing to give a 'true and fair view'.

## Accounting and reporting by charities

- 3.18. Materiality needs to be considered in the context of the accounts and depends on:
- the size of the item or error;
  - the nature of the item or error;
  - the impact of its omission or misstatement on the reported gross income or total expenditure and net assets; and
  - the impact of its omission or misstatement on particular analysis headings within the statement of financial activities, balance sheet and, where applicable, statement of cash flows and on the disclosures made in the notes to the accounts.
- 3.19. Charities should only disclose accounting policies that apply to material items or transactions. Charities should avoid providing unnecessary information for non-material items or transactions.
- 3.20. Although the FRSSE and this SORP need only be applied to material items or transactions, it is inappropriate to make, or leave uncorrected, immaterial departures from this SORP to achieve a particular presentation of an entity's financial position, financial performance or cash flows.
- 3.21. This SORP specifies when a charity must always consider a particular item or transaction material, for example the disclosure of related party transactions. Also, as a matter of emphasis, SORP modules may make particular reference to materiality.

### Offsetting

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- 3.22. In determining the aggregate amount of any item in the accounts, a charity must not offset assets and liabilities, or income and expenses, unless required or permitted by the FRSSE or this SORP. Offsetting does not include making provisions for the write-down of stock or for bad debts. Similarly, a charity reports any gains and losses on the disposal of its fixed assets by deducting the carrying amount of the asset and related selling expenses from the proceeds of the disposal.

### Prior period adjustments

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- 3.23. Prior period adjustments must be accounted for by restating the comparative figure for the preceding period in the primary statements and notes and adjusting the opening balance of funds for the cumulative effect. The cumulative effect of the adjustments must also be noted at the foot of the statement of financial activities.
- 3.24. This SORP sets out the accounting treatment(s) and the disclosures required in the notes to the accounts that apply to charities preparing their accounts using the FRSSE.
- 3.25. Charities preparing their accounts, under the FRSSE must apply the relevant requirements of that standard and the recommendations of this SORP.

### Selection of accounting policies

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- 3.26. Charities preparing their accounts using the FRSSE must refer to that standard and the relevant modules contained in this SORP when selecting their accounting policies for the treatment of particular items, transactions or events in the accounts.

## Accounting and reporting by charities

- 3.27. This SORP requires that charities must adopt current accounting practice as set out in this SORP to reflect the special factors prevailing or transactions undertaken in the charity sector. The introduction to each of the SORP's modules specifies when the SORP requires a charity to adopt current accounting practice.
- 3.28. For all other transactions that are not specifically dealt with in the FRSSE, charities may follow their existing accounting policies provided that the policy and related disclosures made are consistent with accepted accounting practice. Where a charity undertakes a new transaction for which it has no existing policy and where it is not dealt with in the FRSSE, the FRSSE requires a charity to have regard to current practice in developing its accounting policies.
- 3.29. Where a charity undertakes a new transaction for which it has no policy and where it is not dealt with in the FRSSE or this SORP, the FRSSE requires a charity to have regard to FRS 102 in establishing current practice.
- 3.30. In special circumstances a charity may conclude that compliance with a particular provision of the FRSSE or this SORP would conflict with the requirement for the charity's accounts to give a true and fair view. In such instances the charity must depart from that provision to the extent necessary to give a true and fair view.
- 3.31. If there is a doubt whether applying the provisions of the FRSSE or this SORP would be sufficient to give a true and fair view, adequate explanation must be given in the notes to the accounts of the transaction or arrangement concerned and the treatment adopted.
- 3.32. Accounting policies and estimation techniques must be consistent with the requirements of the FRSSE, this SORP and relevant legislation. Where this permits a choice, a charity must select the policies and techniques most appropriate to its particular circumstances for the purpose of giving a true and fair view.
- 3.33. Accounting policies must be applied consistently within the same accounts and from one financial year to the next. Accounting policies must be reviewed regularly to ensure that they remain the most appropriate to the charity's particular circumstances for the purpose of giving a true and fair view. Following a change in accounting policy, the amounts for the current and corresponding periods must be restated on the basis of the new policies.

### Compliance with the SORP

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- 3.34. For a charity to state that its report and accounts are compliant with this SORP, both its trustees' annual report and its accounts must be prepared fully in accordance with the reporting and accounting recommendations of this SORP. To state that their accounts have been prepared in accordance with this SORP, a charity must:
- consider those SORP modules that apply to the activities, transactions and circumstances of the reporting charity;
  - comply with applicable format requirements and accounting treatments specified by this SORP and provide those disclosures that this SORP specifies 'must' be provided;



## Accounting and reporting by charities

- make any additional disclosures required by the FRSSE; and
  - only depart from the requirements if this SORP if necessary for the accounts to give a true and fair view.
- 3.35. This SORP uses the term ‘must’ to indicate those recommendations that are likely to affect the ability of the accounts to give a true and fair view if not applied to material transactions or items. Where the SORP states that an item is always material or the recommendation is one which ‘must’ be followed, non-adherence to that recommendation is a departure from this SORP.
- 3.36. The SORP also identifies particular recommendations that ‘should’ be followed. These recommendations are aimed at advancing standards of financial reporting as a matter of good practice. While charities are encouraged to follow all the SORP’s recommendations, a failure to follow a ‘should’ recommendation is not regarded as a departure from this SORP.
- 3.37. Where the SORP states that a particular accounting treatment or disclosure ‘may’ be adopted, this provides an illustration of an approach to a particular disclosure that a charity may choose to adopt or identifies that an alternative accounting treatment or disclosure of a transaction or event is allowed by the SORP. Charities may choose whether such examples or alternative treatments are adopted at their discretion.

### Disclosure of accounting policies and changes in estimation techniques and prior year adjustments

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- 3.38. The notes to the accounts must, in order to comply with the Application of Financial Reporting Requirements (FRS 100) and the FRSSE, state whether the accounts were prepared:
- in accordance with this SORP;
  - in accordance with the FRSSE; and
  - in accordance with applicable charity and/or company law in the jurisdiction(s) of registration.
- 3.39. The FRSSE also requires that the notes to the accounts must provide:
- a description of each material accounting policy followed;
  - details of any changes to the accounting policies to those followed in the preceding period including a brief explanation of why each new accounting policy is thought more appropriate and, where practicable, an indication of the effect of the change on the results for the current period;
  - where practicable, the effect of prior period adjustments on the results for the preceding period; and
  - where the effect of a change to an estimation technique is material, a description of the change and, where practicable, the effect on the results for the current period.

## *Accounting and reporting by charities*

- 3.40. The FRSSE also requires that where the trustees are aware of any material uncertainties as to whether the charity is a going concern, this concern must be disclosed. In addition, where the period considered by the trustees in making their assessment of whether the charity is a going concern has been limited to a period of less than one year from the date of approval of the accounts, that fact must also be stated.
- 3.41. In addition, the FRSSE requires that where there has been a material departure from the requirements of the FRSSE or relevant legislation, the notes to the accounts must:
- state that there has been a departure from the requirements of the FRSSE or relevant legislation and that the trustees have concluded that the departure is necessary to give a true and fair view;
  - state why the treatment prescribed would not give a true and fair view;
  - state the treatment required by the FRSSE or relevant legislation and a description of the treatment adopted; and
  - provide a description of how the position shown in the accounts is different as a result of the departure (which should be quantified where practicable).
- 3.42. Where charities have made a material departure from a recommendation of this SORP, FRS 100 requires that the notes to the accounts must provide:
- a brief description of how the accounts depart from the recommended practice set out in the SORP;
  - the reasons why the treatment adopted is judged more appropriate to the charity's particular circumstances; and
  - brief details of any disclosures required by this SORP that have not been provided, and the reasons why they have not been provided.
- 3.43. The effect of a departure from a SORP need not be quantified, except in those rare cases where such quantification is necessary for the accounts to give a true and fair view.
- 3.44. If a material departure from the requirements of the FRSSE is also a departure from the requirements of this SORP, a combined note may be provided.

## 4. Statement of financial activities

### Introduction

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- 4.1. Whilst the FRSSE sets out the format of a profit and loss account prepared under company legislation, it does not deal with how this format is adapted for charities where current practice is to present a Statement of Financial Activities (SoFA) which combines the presentation of an income and expenditure accounts and a statement of other recognised gains and losses in single statement. Nor does the FRSSE address the presentation of charitable funds within the SoFA. The structure, format and headings of the SoFA (when prepared on an activity basis) set out in Table 2 applies to all charities adopting this SORP.
- 4.2. The FRSSE requires corresponding amounts for the previous reporting period must be shown for each item presented in the Statement of Financial Activities (SoFA). This SORP requires that corresponding amounts for the total funds of a charity must be presented on the face of the SoFA. The corresponding amounts presented for the separate classes of funds, if any, held by a charity may be presented either on the face of the SoFA or prominently in the notes to the accounts.
- 4.3. The column in Table 2 headed 'Further details' provides references to later sections of this module that set out those activities and transaction(s) falling within each of the SoFA's headings.
- 4.4. The statement of financial activities (SoFA) is a single accounting statement that includes all income, gains, expenditure and losses recognised for the reporting period. It provides the user with an analysis of the income and endowment funds received and the expenditure by the charity on its activities, and presents a reconciliation of the movements in a charity's funds for the reporting period.
- 4.5. The SoFA should be prepared with the needs of the charity's stakeholders in mind (see the SORP module '[Accounting and reporting by charities – the statement of recommended practice \(SORP\) scope and application](#)'). Charities reporting on an activity basis should ensure that those activities reviewed in the trustees' annual report are also reported on the face of the SoFA or in the notes to the accounts.
- 4.6. This SORP requires expenditure to be reported on an activity basis to show how the charity has used its resources to further its charitable aims for the public benefit. However, charities below the charity audit threshold may opt to report their charity's expenditure in a different way, for example by the nature of expenditure rather than on an activity basis.

Table 2: Statement of financial activities

	Unrestricted funds	Restricted funds	Endowment funds	Total funds	Prior period total funds	Further details
	£	£	£	£	£	£
<b>Income and endowments from:</b>						
Donations and legacies						A1
Charitable activities						A2
Other trading activities						A3
Investments						A4
Other						A5
<b>Total</b>						
<b>Expenditure on:</b>						
Raising funds						B1
Charitable activities						B2
Other						B3
<b>Total</b>						
<b>Net income/(expenditure)</b>						
<b>Transfers between funds</b>						C
<b>Other recognised gains/ (losses):</b>						
Gains/(losses) on revaluation of fixed assets						D1
Gains/(losses) on investment assets						D2
Actuarial gains/(losses) on defined benefit pension schemes						D3
<b>Net movement in funds</b>						
<b>Reconciliation of funds:</b>						E
Total funds brought forward						
<b>Total funds carried forward</b>						

4.7. The module is divided into two parts as follows:

- **Presentation of information:**
  - structure of the SoFA – all charities;
  - accounting for exceptional items;
  - structure of the SoFA – charities below the audit threshold; and
  - structure of the SoFA – all charities reporting on an activity basis.
- **Line headings used in the statement of financial activities:**
  - A1 Income from donations and legacies;
  - A2 Income from charitable activities;
  - A3 Income from other trading activities;
  - A4 Investment income;
  - A5 Other income;
  - Analysis of income in the notes to the accounts;
  - B1 Expenditure on raising funds;
  - B2 Expenditure on charitable activities;
  - B3 Other expenditure;
  - Analysis of expenditure in the notes to the accounts;
  - C Transfers between funds;
  - D1 Gains/(losses) on revaluation of fixed assets;
  - D2 Investment gains/(losses);
  - D3 Actuarial gains/(losses) on defined benefit pension schemes; and
  - E Reconciliation of funds.

## Presentation of information

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### Structure of the SoFA – all charities

- 4.8. This SORP requires that a charity's statement of financial activities (SoFA) must:
- adopt the same format in subsequent reporting periods unless there are special reasons for a change that is explained in the notes to the accounts;
  - provide corresponding amounts for the total funds presented on the face of the SoFA; and
  - omit any line of the SoFA where there is nothing to report in both the current and previous reporting period.
- 4.9. The columns of the SoFA must be used to distinguish restricted income funds, which may only be spent for a particular purpose of the charity, from unrestricted funds, which can be spent on any of its purposes, and endowment funds. Endowment funds are restricted funds which either cannot be spent (permanent endowment) or where there is no actual requirement to spend or apply the capital unless, or until, the trustees decide to spend it (expendable endowment).
- 4.10. All of the charity's income and expenditure, transfers and other recognised gains and losses must be analysed between the classes of funds, but a charity will not necessarily have funds of all three classes.
- 4.11. If a class of funds would not be considered material, it may be combined with another class of funds and shown as a single combined funds column. If a single combined total funds column is used, the heading must be changed to 'all unrestricted and restricted funds' or 'all unrestricted, restricted and endowed funds' as appropriate. Where a single column approach is followed the summary of fund movements must include an analysis for each class of fund for each row in the SoFA together with a total that corresponds to the total shown in the SoFA. For more information refer to the SORP module '[Fund accounting](#)'.
- 4.12. A charity may vary the order in which it presents headings within the income and expenditure sections of the SoFA to meet its own presentational needs. Some charities may also find it informative to their users to insert additional subtotals.
- 4.13. A charity may add additional columns to the SoFA to present material funds or activities on the face of the statement rather than in the notes. Any additional analysis of this type provided on the face of the SoFA must make clear the class of fund (unrestricted, restricted or endowment) in the column title. In providing additional information, a balance needs to be struck between the provision of additional information and the resulting complexity of the statement.

### Accounting for exceptional items

- 4.14. The FRSSE uses the term 'exceptional items' to describe amounts arising from events or transactions that are part of a charity's ordinary activities but are exceptional by virtue of their size or incidence.

- 4.15. The disclosure of exceptional items must be made either in the notes or by the insertion of an additional line within the relevant activity heading on the face of the SoFA when necessary for the presentation of a true and fair view of a charity's financial activities. For example, exceptional items that should be disclosed separately are a material fraud or the loss of a material tangible fixed asset. An adequate description of each exceptional item must be given to enable its nature to be understood.
- 4.16. The FRSSE also requires that costs of a fundamental reorganisation or restructuring that has a material effect on the nature and focus of a charity's activities should be separately disclosed on the face of the SoFA.

#### **Structure of the SoFA – smaller charities below the charity audit threshold**

- 4.17. The analysis of income and expenditure by activity is encouraged for all charities preparing accruals accounts. However, charities not subject to statutory audit are not required to report their income and expenditure on an activity basis and may adopt an alternative approach to their analysis.
- 4.18. This analysis may be based on the nature of the income and expenditure. For example, expenditure could be analysed by salary-related costs, premises-related costs, interest expenses, transport costs and grants made. Alternatively, the headings used by the charity to record expenditure in its own accounting records could be used.
- 4.19. Where an alternative approach to analysis is adopted, this SORP requires that charities must disclose in their SoFA:
- total income of the charity;
  - a relevant analysis of the components of income;
  - total expenditure of the charity;
  - a relevant analysis of the components of expenditure;
  - net income/expenditure;
  - gains/(losses) on investments (where applicable);
  - transfers between funds;
  - gains on the revaluation of fixed assets (where applicable);
  - actuarial gains/(losses) on any defined benefit pension scheme (where applicable);
  - net movement in funds;
  - total funds brought forward from the previous reporting period; and
  - total funds carried forward at the end of the reporting period.
- 4.20. If a material component of income or expenditure is not presented on the face of the SoFA, the nature and amount of the item must be disclosed in the notes to the accounts.

4.21. Charities preparing their accounts using a natural or alternative basis of analysis must also provide those disclosures required by other modules relevant to the charity. For example, a charity must disclose any remuneration, benefits or expenses paid to trustees and any related party transactions.

### **Structure of the SoFA – all charities reporting on an activity basis**

4.22. This SORP requires that larger charities above the charity audit threshold (see Appendix 3, '[Thresholds for the UK and the Republic of Ireland](#)') and those smaller charities opting to report on an activity basis must classify their income and expenditure by activity.

4.23. Income must be analysed according to the activity that produced the resources. Expenditure must be analysed by the nature of the activities undertaken.

4.24. Where relevant to the understanding of material activities, the expenditure analysis headings should enable the user of the accounts to understand the relationship with income derived from the activity. For example:

- a charity selling donated goods through a shop could use the description 'Shops' within row A3 ('Income from other trading activities') and row B1 ('Expenditure on raising funds');
- a charity running a care home could use the description 'Residential care fees' within row A2 ('Income from charitable activities') and 'Residential care costs' in row B2 ('Expenditure on charitable activities');
- an arts charity providing a mix of paid-for and free services could use the description 'Admission fees for galleries and exhibitions' within row A2 ('Income from charitable activities') and use the heading 'Operation of art gallery and touring exhibitions to schools and community' in row B2 ('Expenditure on charitable activities'); and
- an endowed grant-making charity mainly making grants to advance education could use the description 'Investment income' within row A4 ('Investment income') and 'Grants to education and research institutions, student bursaries and other grants' in row B2 ('Expenditure on charitable activities').

4.25. In most cases, it will be clear which activity generated the income or expenditure. Expenditure shared between two or more activities should be apportioned between them on a reasonable, justifiable and consistent basis (see the SORP module '[Allocating costs by activity in the statement of financial activities](#)').

## **Line headings used in the statement of financial activities**

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### **A: Income and receipt of endowment**

#### *A1: Income from donations and legacies*

4.26. Donations and legacies include all income received by the charity that is, in substance, a gift made to it on a voluntary basis. A donation or legacy may be for any purpose of the charity (unrestricted funds) or for a particular purpose of the charity (restricted income funds or endowment funds).



## *Accounting and reporting by charities*

4.27. Donations and legacies do not provide any significant benefit to the donor in return for their payment other than the knowledge that the charity must use the gift to further its purposes. Income from donations and legacies includes:

- donations and gifts made by individuals and corporations, including any related tax refund or Gift Aid claimed on gifts made by individuals but excluding goods donated for resale;
- legacies receivable by the charity;
- grants of a general nature provided by government and charitable foundations which are not conditional on delivering certain levels or volumes of a service or supply of charitable goods;
- membership subscriptions and sponsorships where these are, in substance, donations rather than payment for goods or services; and
- donated goods for the charity's own use or distribution and donated services and facilities.

### *A2: Income from charitable activities*

4.28. Income from charitable activities includes income earned both from the supply of goods or services under contractual arrangements and from performance-related grants which have conditions that specify the provision of particular goods or services to be provided by the charity. To fall within this analysis heading, the activities specified by the contractual terms or grant conditions must be undertaken for the charitable purposes of the charity.

4.29. Income from charitable activities includes:

- the sale of goods and services as part of the charitable activities of the charity (also known as primary purpose trading), whether the sale is intended to make a profit or is at or below cost;
- contractual payments from government or public authorities and other parties which fund the provision of particular goods or services, for example the provision of care;
- the sale of goods or services made or provided by the beneficiaries of the charity;
- performance-related grants where the income is conditional on delivering certain levels or volumes of a service or supply of goods;
- ancillary trades connected to primary purpose trading; and
- the letting of non-investment property in furtherance of charitable purposes.

### *A3: Income from other trading activities*

4.30. Income from other trading activities includes income earned from both trading activities to raise funds for the charity and income from fundraising events. To fall within this analysis heading, the income must be received in exchange for supplying goods and services in order to raise funds for the charity. While selling donated goods is legally considered to be the realisation of a donation in kind, in economic terms it is similar to a trading activity and should therefore be included in this analysis heading.

4.31. Income from other trading activities includes:

- income from non-charitable trading activities, including non-charitable trading activities of subsidiary entities consolidated into group accounts;
- membership subscriptions and sponsorships where the recipient is not a beneficiary and where these are, in substance, a payment for goods or services;
- income from fundraising events such as jumble sales, firework displays and concerts by the charity (or by volunteers working under the charity's management direction) or its agents;
- shop income from selling donated and bought-in goods;
- income from letting and licensing arrangements for property held primarily for functional use by the charity but temporarily surplus to operational requirements; and
- income from sponsorships and social lotteries which cannot be considered pure donations.

*A4: Investment income*

4.32. Investment income is earned from holding assets for investment purposes and includes dividends, interest, and rents from investment property. Where income from investments is material, it must be presented as a separate heading on the face of the SoFA.

4.33. While income must be presented gross in the SoFA before the deduction of any costs incurred, it is often not practicable for charities to identify the investment management costs incurred within collective investment schemes, such as unit trusts or common investment funds, prior to the distribution of income. Where it is not practicable to identify the investment management costs incurred within the scheme with reasonable accuracy, the investment income should be reported net.

*A5: Other income*

4.34. Other income represents income that cannot be reported under the other analysis headings provided within the SoFA. Other income may also include the conversion of endowment funds into income with the equivalent offsetting reduction to endowment funds shown as a deduction under other income in the 'Endowment funds' column. This approach may be helpful in those jurisdictions that include such items in the calculation of gross income for audit threshold purposes. Alternatively, a conversion of endowment funds into income may be included under the heading 'Transfers between funds'.

4.35. The conversion of endowment into income includes:

- capital funds released to an income fund from expendable endowment; and
- the release of funds to income from the 'unapplied total return fund' held within the permanent endowment fund where a charity has authority to adopt a total return approach to investment.

## *Accounting and reporting by charities*

4.36. This heading should also include all other sources of income unless the amount is sufficiently material as to require its presentation as a separate SoFA heading. Other income may include:

- a gain on the disposal of a tangible fixed asset held for the charity's own use;
- a gain on the disposal of a programme related investment;
- any royalties from the exploitation of intellectual property rights; and
- any other income not falling into the other income categories.

### *Analysis of income in the notes to the accounts*

4.37. Unless analysed on the face of the SoFA, this SORP requires that the notes to the accounts must provide an analysis of the material components of income included within each analysis heading of the SoFA. Amounts for similar activities should be aggregated so as to provide an analysis of:

- donations and legacies, distinguishing between the types of gift receivable, for example the amount of donations, grants of a general nature and legacies;
- income from charitable activities, identifying the nature of the activities undertaken and the income produced;
- income from other trading activities, identifying the nature of the trading or fundraising activity and income produced;
- investment income, analysed according to each class of investment shown on the balance sheet or in the investment note to the accounts; and
- the nature and amount of other income receivable.

4.38. Where applicable, this SORP requires that the notes to the accounts must give the amount and reason for the conversion of all or part of any endowment fund converted into income in the reporting period.

## **B: Expenditure**

### *B1: Expenditure on raising funds*

4.39. Expenditure on raising funds includes all expenditure incurred by a charity to raise funds for its charitable purposes. It includes the costs of all fundraising activities and events, non-charitable trading activities and the sale of donated goods. However, any costs incurred in providing goods or services as a charitable activity must not be included in this heading, even if a charge is made for their provision.

4.40. Expenditure on raising funds includes those costs incurred in:

- seeking donations, grants and legacies;
- operating membership schemes and social lotteries;
- staging events, including the performance fees, licence fees and other related costs;
- contracting with agents to raise funds on behalf of the charity;
- operating charity shops selling donated and/or bought-in goods;

## *Accounting and reporting by charities*

- operating a trading company undertaking non-charitable trading activities;
- advertising, marketing and direct mail materials, including publicity costs not associated with educational material designed wholly or mainly to further the charity's purposes; and
- investment management costs.

4.41. Investment management costs include the costs of:

- portfolio management;
- obtaining investment advice;
- administration of the investments;
- costs of licensing intellectual property; and
- rent collection, property repairs and maintenance charges.

4.42. Where investment management costs are material, they should be presented as a separate heading on the face of the SoFA.

4.43. Costs associated with acquiring and disposing of investments would normally form part of the acquisition cost of the investment or reduce the return on disposals. These costs are therefore not part of investment management costs. Where investment managers deduct management fees from investment income, the charity should report the gross investment income before fees and report the management fees charged in this cost category. However, charities are not expected to prorate investment management fees charged to a collective investment scheme to identify the notional cost attributable to its own holding in the scheme.

4.44. Investment management costs associated with endowment fund investments should generally be charged to the endowment fund in the SoFA. Further guidance on the charging of investment management costs to endowment funds is provided in the SORP module '[Fund accounting](#)'.

4.45. Fundraising costs may be incurred in starting up a new source of future income such as legacies, or in developing a supporter database. In most cases these start-up costs should not be carried forward as prepayments or deferred expenditure. Instead, such costs are charged to the SoFA as incurred. Charities that have an existing accounting policy of capitalising the data capture costs of internally developed databases may continue to use that policy. However, charities adopting current practice should note that data capture costs of an internally developed database must not be capitalised. The costs of a database that has been purchased or donated to the charity can be capitalised where it is sufficiently certain that it will generate economic benefits, for example in generating income, and the resulting database has a readily ascertainable cost or value.

4.46. Charities may choose to expand the analysis provided within this heading, for example by identifying separately 'Expenditure on raising donations and legacies' (A1), 'Expenditure on other trading activities' (A3) and 'Investment management costs' (A4) either in the SoFA or by way of an explanatory note.

*B2: Expenditure on charitable activities*

- 4.47. Expenditure on charitable activities includes all costs incurred by a charity in undertaking activities that further its charitable aims for the benefit of its beneficiaries, including those support costs and costs relating to the governance of the charity apportioned to charitable activities. Costs involved in negotiating contracts or grants that require the charity to provide specific charitable services should also be regarded as part of the cost of carrying out that activity.
- 4.48. Additional sub-headings should be added to the analysis of charitable activities to identify the significant charitable activities undertaken which have been reviewed in the trustees' annual report. The sub-headings used should reflect the nature of the activity undertaken.
- 4.49. On occasions, a subsidiary entity may undertake activities specifically to further the purposes of a parent charity rather than as a fundraising activity. Expenditure incurred by a subsidiary on activities that fall within the parent charity's purposes should be analysed as charitable activity when consolidated accounts are prepared.
- 4.50. Charities may carry out their activities through a combination of direct service provision and the grant funding of third parties to undertake work that contributes to the charity's aims or programme of work. The cost of charitable activities presented in the SoFA includes the costs of both direct service provision and the payment of grants. Charities making grants must refer to the SORP module '[Presentation and disclosure of grant-making activities](#)', which sets out the particular disclosures required for grant-making in the notes to the accounts.

*B3: Other expenditure*

- 4.51. Other expenditure includes all expenditure that is neither related to raising funds for the charity nor part of its expenditure on charitable activities. Where an amount is material or its presentation on the face of the SoFA is necessary for an understanding of a charity's financial performance, an additional sub-heading should be used.

*Analysis of expenditure in the notes to the accounts*

- 4.52. This SORP requires that the notes to the accounts must provide a relevant analysis of the activities included within each expenditure heading provided on the face of the SoFA. The analysis provided should aggregate the cost of similar activities and provide the user of the accounts with an understanding of the charity's main activities.
- 4.53. This SORP also requires that the analysis must give details of the support costs charged to an activity and the cost of grant funding to third parties that have been included within the cost of charitable activities. The total provided within the analysis must reconcile with the amounts presented within the relevant expenditure headings of the SoFA. This information may, for example, be presented in a tabular format (see Table 3).

**Table 3: Analysis of expenditure on charitable activities**

Activity or programme	Activities undertaken directly	Grant funding of activities	Support costs	Total
	£	£	£	£
Activity 1				
Activity 2				
Activity 3				
<b>Total</b>				

### **C: Transfers between funds**

- 4.54. All transfers between the different classes of funds must be shown in the transfer row of the SoFA. The transfer line must always net to nil. Refer to the SORP module 'Fund accounting' for more information.
- 4.55. The transfer row may also be used to record the conversion of endowment funds (including the release of any unapplied total return where a total return approach to investment is adopted) into income. Alternatively, charities may choose to present the conversion of endowment funds in row A5 ('Other income').

### **D: Other recognised gains/(losses)**

#### *D1: Gains/(losses) on the revaluation of fixed assets*

- 4.56. This heading includes gains or losses on the revaluation of property, plant and equipment used by a charity, and heritage assets and intangible assets. This heading should not be used when adjusting for a reversal in a previous charge for impairment.

#### *D2: Investment gains/(losses)*

- 4.57. This heading is used to record any gains and losses on investment assets (including investment properties). This SORP allows charities to present realised and unrealised gains and losses as a single row in their SoFA. In particular, this approach will be necessary where a charity adopts 'mark to market' or a continuous revaluation approach in relation to its investment portfolio.

#### *D3: Actuarial gains/(losses) on defined benefit pension schemes*

- 4.58. This heading is used to record actuarial gains or losses on defined benefit pension schemes.
- 4.59. Charities which operate defined benefit pension schemes must refer to the SORP module 'Retirement benefits', which provides recommendations on the recognition of pension costs, assets and liabilities and their disclosure in the accounts.

### **E: Reconciliation of funds**

- 4.60. This SORP requires that the opening and closing balances for each class of fund must be shown with the difference reconciled by the movement in funds in the reporting period. The closing fund balances presented in the SoFA must agree with the equivalent totals shown in the 'Funds of the charity' section on the balance sheet.

## **5. Recognition of income, including legacies, grants and contract income**

### **Introduction**

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- 5.1. Income is the inflow of economic benefits to a charity from the activities that it undertakes. Income is an inflow of resources that results in an enhancement to the charity's assets or a decrease in its liabilities.
- 5.2. Charities that provide goods or service under contract (exchange transactions) should refer to section 4 of the FRSSE. Aside from the recognition of government grants and gifted tangible fixed assets, the FRSSE does not deal with the recognition of income from non-exchange transactions (including gifts, donations and legacies). This SORP requires charities to adopt current accounting practice for the recognition of income from non-exchange transactions. This module of the SORP reflects current accounting practice for non-exchange transactions. Charities should also have regard to paragraphs 34.64 to 34.74 of section 34 of FRS 102 and Appendix B to section 34 of FRS 102 when developing their accounting policies for the recognition of non-exchange transactions.
- 5.3. This module sets out:
  - understanding the nature of income;
  - general rules for income recognition;
  - general principles for recognising income from donations and grants;
  - identification of terms and conditions;
  - performance-related conditions;
  - other terms and conditions that limit the recognition of income;
  - deferring income where conditions that limit recognition are not met;
  - terms and conditions that do not prevent recognition;
  - recognising income from legacies;
  - income from donated goods, facilities and services;
  - income from contracts for the supply of goods and services;
  - income from membership subscriptions;
  - income from interest, royalties and dividends;
  - settlement of insurance claims; and
  - disclosures and notes to the accounts.

## Understanding the nature of income

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- 5.4. There are two broad categories of income: income from exchange transactions (contract income) and income from non-exchange transactions (gifts). It is important for charities to distinguish between the two as they are recognised differently in a charity's accounts.
- 5.5. Income from exchange transactions is received by the charity for goods or services supplied under contract. The income the charity receives is approximately equal in value to the goods or services supplied by the charity to the purchaser. The essential feature of income from a non-exchange transaction is that the charity receives value from the donor without providing equal value in exchange.
- 5.6. Income from non-exchange transactions (gifts) are donations of money, goods, facilities or services which are given freely to the charity by a donor. Grants are a form of non-exchange transaction where the grant-maker awards a grant without receiving equal value in exchange. However, even though grants are classified as non-exchange transactions, a grant may be presented as income from charitable activities where the payment is made to secure the provision of particular goods or services.
- 5.7. A donation or grant that can be used for any purpose of the charity is unrestricted income. However, a donation or grant may be restricted to a specific purpose of a charity. A restriction may result from a specific appeal by the charity, or from the decision of the grant-maker or donor to support a specific purpose of the charity rather than making funds available for the charity's general use. Simply because a grant is restricted to a particular purpose of the recipient charity does not mean it should be recognised as a performance-related grant. Restricted grants that are not subject to performance-related conditions are included within the SoFA heading 'Income from donations and legacies'.
- 5.8. Transactions must be accounted for and presented in accordance with their substance and not simply their legal form. Charities must therefore consider the substance of any conditions attaching to donations or grants and to the substance of any contractual terms when determining their entitlement to income. Similarly, the substance of any restriction placed on the use of income must be considered when determining whether or not income is presented as restricted funds in a charity's accounts. In particular, a charity should consider:
  - Whether entitlement to income is subject to fulfilling performance-related conditions. Performance-related conditions distinguish a contract or performance-related grant from an unconditional gift or grant.
  - The terms of a donation or grant that impose a restriction on use which is narrower than the general purposes of the charity. Terms placed on gifts that limit a charity's discretion over how income must be used are presented as restricted income in the accounts.



## Accounting and reporting by charities

- The terms of a contract may limit payments to amounts expended by the charity on purposes specified in the contract and restrict the charity's use of any surplus. Income that is restricted by contractual terms may be presented as restricted in the accounts if the restrictions are in substance the same as would apply to a restricted donation or grant.
- The terms of a gift that require it to be held as endowment that must be invested and not spent. Material endowment funds must be presented as a separate class of restricted funds.

### General rules for income recognition

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- 5.9. 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. This SORP requires that 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 – income is recognised when there is sufficient certainty of receipt (receipt is more likely than not);
  - Measurement – the monetary value or amount of the income can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.
- 5.10. All income must be reported gross when raised by the charity (or by volunteers working at the charity's direction) or its agents. Any fee charged for fundraising by a third party and deducted from the amount collected before it is remitted to the charity must not be offset against fundraising income recognised in the accounts but be reported as a fundraising expense. However, in the case of individuals not employed by, or contracted by, the charity who are acting on a purely voluntary basis and outside of the charity's control, the charity recognises the net amount remitted.

### General principles for recognising income from donations and grants

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- 5.11. This SORP requires charities to adopt current practice when accounting for income from non-exchange transactions. Income from donations or grants is recognised when there is evidence of entitlement to the gift, receipt is probable and its amount can be measured reliably.
- 5.12. In the case of a grant, evidence of entitlement will usually exist when the formal offer of funding is communicated in writing to the charity. However, some grants will contain terms or conditions that must be met before the charity has entitlement to the resources.
- 5.13. In the case of a donation, entitlement usually arises immediately on its receipt. However, some gifts may include terms or conditions which must be met before the charity is entitled to the resources.

## Identification of terms and conditions

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- 5.14. Charities need to identify donations or grants that are subject to terms or performance-related conditions or other conditions that must be met before there is unconditional entitlement to the gifted resources.
- 5.15. Not all terms or conditions attaching to a grant or donation prevent its recognition as income. A term or condition that simply restricts the use of a grant or donation does not affect a charity's entitlement to the gift and recognition of income. However, a restriction does affect how the gift or grant is reported in the accounts. For more information refer to the SORP module '[Fund accounting](#)'.
- 5.16. When accounting for grants and donations, charities should identify:
- those donations and grants that are subject to performance-related conditions; and
  - other terms or conditions that may prevent income recognition.

## Performance-related conditions

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- 5.17. Grant funding agreements may contain conditions that specify the services to be performed by a charity in receipt of a grant. For example, the grant may be in the form of a service level agreement where the conditions for payment are linked to the achievement of a particular level of service or the units of output delivered. The performance-related conditions contained in a funding agreement might, for example, specify the number of meals provided or the opening hours of a facility used by beneficiaries. Income must only be recognised to the extent that the charity has provided the specified goods or services as entitlement to the grant only occurs when the performance-related conditions are met.
- 5.18. Although performance-related conditions can apply to any form of gift, in practice it is unusual to see performance-related conditions apply to donations.
- 5.19. A restriction on the use of a grant or donation to a particular purpose or activity of a charity does not create a performance-related condition. A restriction creates a requirement that limits or directs the purpose for which a resource may be used but it does not require a specific level of performance or output from the recipient charity.
- 5.20. It is important at the outset of any arrangement that the charity identifies whether the funding agreement is a performance-related grant or a contract. This is important because the consequence of non-compliance with performance-related conditions and the liability for non-performance of a contract differ. The law of contract provides for the buyer to seek costs, damages and recompense for any failure or breach of contract by the seller, whereas a breach of grant conditions may lead to a partial or full repayment of the grant when repayment terms apply to the grant.

## Other terms and conditions that limit the recognition of income

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- 5.21. Performance-related conditions are not the only conditions that may apply to donations and grants. For example, a grant may be conditional on a charity obtaining matched funding, or subject to a successful planning consent. Meeting these conditions would not be wholly within the control of the recipient charity and the outcome of the specified event is uncertain. The charity would not have unconditional entitlement to the income until these conditions were met.
- 5.22. Donor imposed conditions may also specify the time period over which the expenditure of resources on a service can take place. Specification of a time period may amount to a pre-condition for use that limits the charity's ability to spend a grant or donation until it has performed the activity related to the specified time period. For example, a condition might specify the provision of a number of training weeks or the completion of a number of work placements in a particular period.
- 5.23. Time-related conditions may be implied. For example, when a multi-period grant is approved and is to be paid on the basis of agreed annual budgets, the charity may not be entitled to spend part or all of that income in advance of its budgeted year(s) without the further prior approval of the grant-maker.

## Deferring income where conditions that limit recognition are not met

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- 5.24. Where terms and conditions have not been met or uncertainty exists as to whether the recipient charity can meet the terms or conditions otherwise within its control, the income should not be recognised but deferred as a liability until it is probable that the terms or conditions imposed can be met.
- 5.25. A grant that is subject to performance-related conditions received in advance of delivering the goods and services required by that condition, or is subject to unmet conditions wholly outside the control of the recipient charity, is accounted for as a liability and shown on the balance sheet as deferred income. Deferred income is released to income in the reporting period in which the performance-related or other conditions that limit recognition are met.
- 5.26. When income from a grant or donation has not been recognised due to the conditions applying to the gift not being wholly within the control of the recipient charity, it should be disclosed as a contingent asset if receipt of the grant or donation is probable once those conditions are met.

## Terms and conditions that do not prevent recognition

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- 5.27. When meeting terms or conditions are within the charity's control and there is sufficient evidence that they have been or will be met, then the income must be recognised. Terms or conditions such as the submission of accounts or certification of expenditure are administrative requirements and would not prevent the recognition of income.

- 5.28. A donation or grant without conditions should not be deferred even if the resources are received in advance of the expenditure on the activity funded by them. The timing of the related expenditure is at the discretion of the charity and the income cannot be deferred simply because the related expenditure has not been incurred. For example, where a donation or grant is given specifically to provide a fixed asset or a fixed asset is donated (a gift in kind), the charity is normally entitled to that income when it is receivable. At this point, all of the income must be recognised in the SoFA and not deferred over the life of the asset.
- 5.29. Similarly, a condition that allows for the recovery by the donor of any unexpended part of a grant does not prevent recognition. Instead, a liability to any repayment is recognised when repayment becomes probable.

### Recognising income from legacies

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- 5.30. For accounting purposes, entitlement to a legacy cannot arise without the charity knowing of both the existence of a valid will and the death of the benefactor. Those charities with databases of current donors may well have information about an individual donor's intention or decision to leave a gift to them in their will and charities may also employ agents or carry out their own research to review publicly available information on recent deaths including the granting of probate. Charities having such information should use this information when developing their accounting policy for recognising income from legacies. For accounting purposes, evidence of entitlement to a legacy exists when the charity has sufficient evidence that a gift has been left to them and the executor is satisfied that the property in question will not be required to satisfy claims in the estate.
- 5.31. Of itself, establishing entitlement is insufficient to recognise legacy income. The recognition of the gift is also affected by the probability of receipt and the ability to estimate with sufficient accuracy the amount receivable.
- 5.32. Receipt of a legacy must be recognised when it is probable that it will be received. Receipt is normally probable when:
- there has been grant of probate;
  - the executors have established that there are sufficient assets in the estate, after settling any liabilities, to pay the legacy; and
  - any conditions attached to the legacy are either within the control of the charity or have been met.

## Accounting and reporting by charities

- 5.33. Charities which receive a significant number of legacies in a reporting period and have detailed historical information on the settlement of legacies may apply an estimation technique in measuring the value of legacies that are recognised to allow for potential variation in settlement values and the risk of a will being contested. For example, where a charity has numerous immaterial legacies by using a portfolio approach the charity may estimate the monetary value of the income that may be received from legacies to which they are entitled, by applying a formula or mathematical model. However, a portfolio approach is unsuitable for material legacies or when a charity only receives legacies infrequently, as these should be considered individually. When a portfolio approach is not adopted, charities must recognise a legacy when the executors have determined that a payment can be made following the agreement of the estate's accounts, or on notification by the executors that payment will be made.
- 5.34. Where a payment is received from an estate or is notified as receivable by the executors after the reporting date and before the accounts are authorised for issue but it is clear that the payment had been agreed by the executors prior to the end of the reporting period, then it should be treated as an adjusting event and accrued as income if receipt is probable.
- 5.35. In some cases, a charity may have entitlement to a legacy but there is uncertainty as to the amount of the payment. For example, the legacy may be subject to challenge or the charity's interest may be a residual one. If the interest of the charity in a pecuniary or residuary legacy cannot be measured reliably, details of the legacy should be disclosed as a contingent asset until the criteria for income recognition are met. Where a legacy is subject to the interest of a life tenant, the legacy would not be recognised as income until the death of the life tenant.
- 5.36. If it is doubtful that full settlement of a legacy debtor will be received, then an adjustment is made to reduce the amount of the legacy debtor and legacy income rather than charging the adjustment as expenditure in the SoFA.

### Income from donated goods, facilities and services

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- 5.37. Goods, facilities and services donated to a charity must be recognised as income when the criteria for their recognition are met. However, issues can arise in measuring the fair value of donated goods and services. Charities that have received donations of goods, facilities or services, including the services of volunteers, must refer to the separate SORP module '[Donated goods, facilities and services, including volunteers](#)', which sets out the requirements for the recognition, measurement and disclosures of these income sources.

### Income from contracts for the supply of goods and services

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- 5.38. Income earned from the sale of goods and services under contract is normally classified as unrestricted funds because it is not a gift and so cannot be restricted by trust law and any surplus may normally be spent on any purpose of the charity.

## *Accounting and reporting by charities*

- 5.39. However, if a contract specifically requires all income received under it to be spent on a particular purpose of the charity and any unspent income to be returned to the funder or only applied for that particular purpose, then in substance, the income may be regarded as restricted. If contract income is presented as restricted then all relevant disclosures required for a restricted fund must be made.
- 5.40. Section 4 of the FRSSE sets out principles for the recognition of income arising from exchange transactions. Entitlement to the income arises as the charity obtains the right to consideration in exchange for its performance under the contract. Usually, entitlement to income occurs with the supply of goods to the buyer. Income is measured at the amount of the consideration receivable which will usually be the contract price, net of discounts and value added tax. If there is a significant risk of a default in the payment and that amount is material to income, then it will be necessary to adjust the amount of income recognised.
- 5.41. Where a contract for services has distinguishable phases or stages in its delivery, it may be appropriate to recognise income for each phase provided the value of each phase can be reliably estimated. Where a contract involves the provision of a service or a number of services that form a single project that runs across different reporting periods, it should be accounted for as a long-term contract if the effect of such contracts in aggregate is material. Charities should refer to Appendix III of the FRSSE for more information on the practical considerations arising when accounting for long-term contracts.
- 5.42. Where the obligations under a contract are performed gradually over time, revenue should be recognised as the contract activity progresses to reflect performance. The income recognised should reflect the right to receive payment by reference to the value of the work performed. A charity must select a method to measure the stage of completion of a service contract that provides the most reliable estimate of the right to receive payment for the work performed. Possible methods include:
- the proportion of costs incurred for work performed to date compared with the total estimated costs to completion; or
  - surveys of the work performed; or
  - completion of a physical proportion of the service contract work.
- 5.43. It may also be appropriate to recognise income based on the time spent in providing a service as a proportion of the total time to be spent to fulfil the contract when this provides the most reliable estimate of a charity's entitlement.
- 5.44. Where income is received in advance, then a charity may not have entitlement to the income until the goods or services have been provided. For example, where a charity sells gift vouchers, the income should be deferred until such time as the goods or services have been provided or the voucher has expired. Income received in advance should be deferred until the charity becomes entitled to it.
- 5.45. Where the effect of the time value of money is material to reported income, the amount of income recognised must be adjusted to the present value of the expected cash inflows to be received. The unwinding of the discount is credited to the SoFA as finance income from the transaction and if reporting on an activity basis shown under the same heading as the related income.

## Income from membership subscriptions

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5.46. Membership subscriptions received by a charity may be in the nature of a gift, or the member may buy a right to services or other benefits. When the substance of the subscription is that of a gift, the income and any associated Gift Aid or other tax refund should be recognised on the same basis as a donation. If the subscription purchases the right to services or benefits, the incoming resource should be recognised as income from charitable activities.

## Income from interest, royalties and dividends

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5.47. This SORP requires:

- income from interest, royalties and dividends to be recognised when receivable;
- royalties and income from the exploitation of intellectual property rights to be recognised when receivable in accordance with the substance of the relevant agreement; and
- dividends to be recognised when the shareholder's right to receive payment is established.

## Settlement of insurance claims

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5.48. This SORP requires that an insurance claim must be recognised when a charity has established its entitlement to the reimbursement of the insured loss, the receipt of that reimbursement is virtually certain and its amount can be measured reliably. Receipt is usually regarded as virtually certain when an offer of settlement is received from the insurer.

5.49. A charity must recognise the amount of the insurance reimbursement either as an item of other income or by offsetting it against the related expense heading in the SoFA. The amount reimbursed through an insurance claim is recognised as an addition to the fund that initially suffered the insured loss.

## Disclosures and notes to the accounts

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5.50. This SORP requires that all charities must:

- explain in the notes to the accounts the accounting policies adopted for the recognition of each material category of income; and
- analyse income in the SoFA using the headings required by the SORP module '[Statement of financial activities](#)'.

5.51. This SORP also requires that when a charity has deferred income, the notes to the accounts should explain the reasons why income is deferred and should analyse the movement on the deferred income account, identifying income deferred in the current year and the amounts released from previous reporting periods.

## 6. Donated goods, facilities and services, including volunteers

### Introduction

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- 6.1. The donation of goods, facilities and services to a charity provides an economic resource for use by the charity to further its aims and objectives.
- 6.2. This module applies to all charities reporting under the FRSSE that have received donated goods, facilities or services in the reporting period.
- 6.3. With the exception of a gift of a tangible fixed asset and government grants, the FRSSE does not deal with the accounting treatment of non-exchange transactions (including gifts, donations and legacies). This SORP requires charities to adopt current accounting practice for the recognition of income from non-exchange transactions. This module of the SORP reflects current accounting practice for non-exchange transactions. Charities should also have regard to paragraphs 34.64 to 34.74 and Appendix B to section 34 of FRS 102 when developing their accounting policies for the recognition of non-exchange transactions.
- 6.4. This module deals with how goods, facilities and services donated to charities are recognised, measured and disclosed in their accounts and sets out:
  - **income recognition criteria;**
  - **measurement bases;**
  - **accounting for donated facilities and services, including volunteers;**
  - **accounting for donated goods and services capitalised as tangible fixed assets;**
  - **accounting for donated goods for distribution to beneficiaries;**
  - **accounting for donated goods for resale; and**
  - **disclosures in the notes to the accounts.**
- 6.5. Income is recognised by a charity in its accounts for goods, facilities and services donated to it once the income recognition criteria set out in paragraph 6.7 are met. When measuring the value of donated goods, facilities and services, practical considerations may impact on the measurement bases adopted. For example, although goods donated for sale are normally recognised at the point of receipt, practicability may dictate that they are recognised only on their sale. Before undertaking a valuation, the charity should consider the materiality of the donations received and whether the cost involved in undertaking a valuation is justified by the benefits to the users of the accounts in terms of their better understanding the resources available to the charity and to the charity itself from having this financial information.
- 6.6. Commercial discounts offered in the normal course of trade should not be recognised or disclosed as a donation in charity accounts as they are an inducement to the customer to make a purchase by lowering the price paid.



## Income recognition criteria

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- 6.7. Donated goods, facilities and services must be recognised as income when the following criteria are met:
- Entitlement – control over the expected economic benefits that flow from the donation has passed to the charity and any performance-related conditions attached to the donation have been fully met.
  - Probable – income is recognised when there is sufficient certainty of receipt (receipt is more likely than not).
  - Measurement – the fair value or value to the charity of the donated item can be measured reliably.
- 6.8. Donated goods, facilities and services are unlikely to be subject to performance-related conditions which would result in the deferral of income until those conditions are met. A restriction on the use of a donation does not prevent its recognition as income.

## Measurement bases

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- 6.9. The FRSSE specifies that donated tangible fixed assets are recognised at their current value (i.e. the lower of replacement cost and recoverable amount). This SORP requires that other donated goods must be measured at their fair value, unless it is impractical to measure reliably the fair value of donated item(s).
- 6.10. When there is no direct evidence of fair value for an equivalent item, a value may be derived from:
- the cost of the item to the donor; or
  - in the case of goods that are expected to be sold, the estimated resale value after deducting the cost to sell the goods.
- 6.11. If it is impractical to measure the fair value of goods donated for resale or if the costs of valuation outweigh the benefit to users of the accounts and the charity of this information, the donated goods must then be recognised when they are sold.
- 6.12. The terms of a gift may require the charity to make on-going use of the donated item, so preventing its sale. In such instances, there may be costs involved in removing such a restriction before the asset could be sold. This would be reflected in a lower assessment of the fair value amount than if the use of that asset was not so restricted.
- 6.13. The cost of any stock of goods donated for distribution to beneficiaries is deemed to be the fair value of those gifts at the time of their receipt. If the goods held are to be distributed freely or for a nominal consideration, then the carrying amount should be subsequently adjusted for any loss of service potential.

## **Accounting for donated facilities and services, including volunteers**

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- 6.14. This SORP requires that facilities and services donated for its own use which it would otherwise have purchased must be included in the charity's accounts when received, provided the value of the gift can be measured reliably.
- 6.15. Measuring donated services using fair value would not be practical as such services cannot be resold and the use of fair value may result in an overstatement of the value of the donation to the charity. Donated facilities and services are therefore measured and included in accounts on the basis of the value of the gift to the charity.
- 6.16. Value to the charity is the amount that the charity would pay in the open market for an alternative item that would provide a benefit to the charity equivalent to the donated item. Value to the charity may be lower than, but cannot exceed, the price the charity would pay in the open market for the item.
- 6.17. Donated facilities and services that are consumed immediately must be recognised as income, with an equivalent amount recognised as an expense under the appropriate heading in the statement of financial activities (SoFA).
- 6.18. Facilities such as office accommodation or services supplied by an individual or an entity as part of their trade or profession can usually be reasonably quantified and must be included in a charity's accounts.
- 6.19. Charities often rely on the contribution of unpaid general volunteers in carrying out their activities. However, placing a monetary value on their contribution presents significant difficulties. For example, charities might not employ additional staff were volunteers not available, or volunteers might complement the work of paid staff rather than replace them. These factors, together with the lack of a market comparator price for general volunteers, make it impractical for their contribution to be measured reliably for accounting purposes. Given the absence of a reliable measurement basis, the contribution of general volunteers must not be included as income in charity accounts.
- 6.20. However, it is important that the user of the accounts understands the nature and scale of the role played by general volunteers. Charities must include a description of the role played by general volunteers and provide an indication of the nature of their contribution in a note to the accounts.

## **Accounting for donated goods and services capitalised as tangible fixed assets**

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- 6.21. Goods donated for on-going use by a charity in carrying out its activities are recognised as tangible fixed assets with the corresponding gain recognised as income from donations within the SoFA. Donated vehicles, plant or furniture are recognised as tangible fixed assets when their current value exceeds the threshold for capitalisation set by the charity's accounting policy.

## Accounting and reporting by charities

- 6.22. If donated services are used in the construction of a tangible fixed asset, the value of services donated will only form part of the construction cost of the asset when the value to the charity of the donated services can be measured reliably. For example, the services donated by a firm of building or electrical contractors would be valued because these services would normally be provided as part of the donor's trade.
- 6.23. In common with any other tangible assets, donated goods held as tangible fixed assets must be subject to depreciation and an assessment made at the reporting date of whether there is any indication that the asset should be written down to its recoverable amount.

### Accounting for donated goods for distribution to beneficiaries

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- 6.24. This SORP requires that donated goods held by the charity for distribution to its beneficiaries should be recognised as stock, with the corresponding income recognised within donations and measured at its fair value.
- 6.25. It may be necessary when valuing the donation to consider any restriction on the sale of the asset or the factors that may reduce the fair value of the asset, such as proximity to a product expiry date or the availability of lower-cost substitutes for the donated item, for example a generic version of a drug. Donated goods held in stock for distribution must be assessed at the reporting date for any indication that the asset should be written down to its recoverable amount.
- 6.26. In the reporting period in which the stocks are distributed, they are recognised as an expense and appropriately analysed as expenditure in the SoFA. The expense recognised is the carrying amount of the stocks at the point of distribution.
- 6.27. If it is impractical to assess the value of donated stock held for distribution at the time of receipt, or if the costs involved in undertaking the valuation of donated stock outweigh the benefit to the users of the accounts and to the charity of having this financial information, the value to the charity of the gift must be recognised as a component of donations when it is distributed, with an equivalent amount recognised as charitable expenditure.

### Accounting for goods donated for resale

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- 6.28. In accepting donated goods for resale, the charity is receiving a gift in kind on trust for conversion into cash to fund the charity's activities. Where practicable, this SORP requires that donated goods for resale are measured at fair value on receipt, which is the expected proceeds from sale less the expected costs of sale.

## Accounting and reporting by charities

- 6.29. Charities accepting goods for resale under the UK retail gift aid scheme are acting as agent in selling the goods on behalf of the donor and are in law entitled only to an administration fee until such time as the donor waives their entitlement to the sale proceeds. Charities which have historical data may use an estimation technique to recognise income from such arrangements from the point of sale, for example, by applying a formula or mathematical model to estimate the likely amount of the donations that will result from their subsequent sale. Income may be recognised from the point of sale where this reflects the substance of the transaction provided the income recognised is adjusted to reflect the risk that some sales will not result in a donation. Where a donor does not waive their entitlement to the sale proceeds, the administration fee is analysed as 'Income from other trading activities' in the SoFA.
- 6.30. Estimating the fair value of donated goods for resale is often impractical because of the volume of low-value items received or the absence of detailed stock control systems or records. In such circumstances, donated goods for resale are not recognised on receipt. Instead, the value to the charity of the donated goods sold is recognised as income when sold. The proceeds of sale are categorised as 'Income from other trading activities' in the SoFA.
- 6.31. If recognised at fair value on receipt, the value of the donated goods for resale should be treated as a component of 'Income from other trading activities' with the corresponding stock recognised in the balance sheet. On its sale the value of the stock is charged against 'Income from other trading activities' and the proceeds of the sale are also recognised as 'Income from other trading activities'.

### Disclosure in the notes to the accounts

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- 6.32. This SORP requires that all charities receiving donated goods, facilities or services must disclose in the notes to the accounts:
- the accounting policy for the recognition and valuation of donated goods, facilities and services;
  - the nature and amounts of donated goods, facilities and services receivable from non-exchange transactions recognised in the accounts, for example, seconded staff, use of property etc.;
  - any unfulfilled conditions or other contingencies attaching to resources from non-exchange transactions that have not been recognised in income; and
  - an indication of other forms of resources from non-exchange transactions from which the charity has benefited but not recognised in its accounts, for example the contribution of unpaid general volunteers.

## 7. Recognition of expenditure

### Introduction

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- 7.1. Expenditure is the amount of a charity's resources that have been spent or otherwise used up in carrying out its activities. An expense results in either a decrease in a charity's assets or an increase in its liabilities.
- 7.2. Examples of an expense include cash spent to purchase goods or services, the depreciation charge on tangible fixed assets, and incurring a liability when goods and services are purchased on credit.
- 7.3. Liabilities can result from exchange transactions that are contractual, for example the purchase of goods or services or the employment of staff. Liabilities can also arise from non-exchange transactions, such as making grants or other funding commitments to further a charity's purposes for which the charity receives no other benefit in return.
- 7.4. This module applies to all charities preparing their accounts under the FRSSE. Charities should also refer to section 11 of the FRSSE which deals with accounting for provisions and contingent liabilities. The FRSSE does not deal specifically with accounting for funding commitments such as the promise of grant funding. This SORP therefore requires charities to adopt current accounting practice for the recognition of funding commitments. This module of the SORP reflects current accounting practice for funding agreements. Charities should also have regard to paragraphs 34.57 to 34.63 and Appendix B to section 34 of FRS 102 when developing their accounting policies for the recognition of funding commitments.
- 7.5. This module sets out:
  - general rules for the recognition of liabilities and expenditure;
  - rules on measurement of liabilities;
  - principles for recognising liabilities from constructive obligations;
  - conditions that limit the recognition of a funding commitment;
  - accounting for liabilities arising from performance-related grants;
  - provisions for liabilities;
  - treatment of commitments not recognised as provisions or liabilities;
  - accounting for onerous contracts; and
  - disclosure of provisions and funding commitments in the accounts.

## General rules for the recognition of liabilities and expenditure

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- 7.6. Liabilities arise from legal or constructive obligations that commit the charity to expenditure. This SORP requires that a liability and related expenditure must be recognised when all of the following criteria are met:
- Obligation – a present legal or constructive obligation exists at the balance sheet date as a result of a past event.
  - Probable – it is more likely than not that a transfer of economic benefits, often cash, will be required in settlement.
  - Measurement – the amount of the obligation can be measured or estimated reliably.
- 7.7. A legal obligation arises when a charity enters into a binding contract or there is a statutory requirement to make a payment. When a charity enters into a contract for the supply of goods or services, expenditure is recognised once the supplier of the goods or services has performed their part of the contract.
- 7.8. A constructive obligation arises as a result of a charity's actions when it indicates to other parties that it accepts particular responsibilities and thereby creates a valid expectation on their part that the charity will meet them.

## Rules on measurement of liabilities

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- 7.9. A liability must be measured at the best estimate of the amount required to settle the obligation at the balance sheet date.
- 7.10. A provision (a liability of uncertain timing or amount) must also be measured at the best estimate of the amount required to settle the obligation at the balance sheet date. When a charity accrues a provision in the reporting period that it will settle over several years, the future payments have a reduced value in today's terms (known as its present value). Where this adjustment would be material, the payments required to settle the obligation should be discounted to their present value. If the future payments have been adjusted for risk then a discount rate equivalent to the market rate on relevant government bonds may be used.
- 7.11. The unwinding of the discount must be treated as a financing cost in the statement of financial activities (SoFA). It should be allocated to the appropriate expenditure heading. For example, the unwinding of a discount resulting from a grant liability should be allocated to charitable expenditure.

## Principles for recognising liabilities from constructive obligations

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- 7.12. Charities frequently provide services or make grants to their beneficiaries on a non-contractual basis. Although a charity's commitments to provide services or grants are not always legally binding under contract, a liability can still arise if the charity has no realistic alternative to settling an obligation resulting from a commitment it has made. However, not all commitments to provide future services or funding will result in a charity recognising a constructive obligation as a liability or provision.

## Accounting and reporting by charities

- 7.13. A charity may make general statements or policy statements about their future intentions, for example the aim of relieving famine in a particular location or improving the quality of care provided to a particular group of people. Such statements can be communicated in a variety of ways, including mission statements, setting out future plans within a trustee's annual report or simply making a general policy statement. Statements such as these do not create a constructive obligation as discretion is retained by the charity as to their implementation.
- 7.14. This SORP requires charities to recognise liabilities arising from funding commitments and constructive obligations. Evidence of a constructive obligation exists where:
- the commitment made by the charity is specific, for example a promise is made to provide particular goods, services or grant funding;
  - this commitment is communicated directly to particular beneficiaries or grant recipients; and
  - there is an established pattern of practice that indicates to the recipients of services or funding that the charity will meet its commitment.
- 7.15. It follows that a charity's decision to provide funding does not create a constructive obligation that must be recognised as a liability unless that decision has been communicated to those affected before the reporting date. The commitment must be communicated in a sufficiently specific manner as to create a valid expectation on the recipient's part that the charity will discharge its responsibilities.
- 7.16. The formal written offer of a grant indicates to the recipient that it is probable that settlement will take place. In such circumstances, the charity cannot realistically withdraw from its commitment and so it is unlikely to have a realistic alternative but to meet the obligation. However, the recognition of any resulting liability would be dependent on any conditions attaching to the commitment.

### Conditions that limit the recognition of a funding commitment

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- 7.17. Funding commitments can be made which give the funder the discretion to avoid future expenditure based on their assessment of whether the conditions attached to the commitment will be met by the recipient.
- 7.18. The award of a grant is a non-exchange transaction. A charity awards a grant to further its own charitable purposes but without creating a contractual relationship with the recipient. The award of a grant is recognised as a liability only when the criteria for a constructive obligation are met, payment is probable, it can be measured reliably and there are no conditions attaching to its payment that limit its recognition.
- 7.19. Where a grant commitment is payable over a period of more than one year, a liability must be recognised for the full amount of the constructive obligation unless conditions apply to payments falling due after the reporting date. Where payments for later years are subject to performance-related conditions, the donor charity may be able to legitimately withdraw from its commitment if a particular condition attaching to the grant is not met.

## Accounting and reporting by charities

- 7.20. Where a condition remains within the control of the donor charity, then the donor charity retains the discretion to avoid the expenditure and therefore a liability must not be recognised. For example, where a commitment is made to provide grant funding over a number of years, future payments may be subject to a review by the donor charity which gives it discretion to terminate the funding agreement. Provided the review condition has been communicated to the recipient as part of the funding agreement and the review has substance, then a constructive liability is unlikely to arise for payments relating to periods subsequent to the review date.
- 7.21. Alternatively, when there is no condition attaching to the grant that enables the donor charity to realistically avoid the commitment, a liability for the full funding obligation must be recognised.
- 7.22. Not all terms attaching to a funding commitment create a condition that gives a donor charity discretion to withdraw from its funding obligation. For example, a term in a grant offer that seeks to relieve the donor charity from a future obligation in the event of a lack of funds at a future settlement date would not normally prevent the recognition of a liability if payment is probable. The liability would only be derecognised (reversed) if a future event requires the funding offer to be rescinded. The reversal of the balance sheet provision must be recognised in the SoFA and deducted from the heading to which the expenditure was originally charged.
- 7.23. Grant commitments may contain conditions that are outside the control of the donor charity. For example, a charity may promise a grant payment on the condition that the recipient finds matching funding. When a condition falls outside the control of the donor charity, a liability arises and expenditure must be recognised if the payment of the grant is probable.
- 7.24. Certain grants may contain specific conditions that closely specify a level of output or service to be performed by the recipient of the grant. These are termed performance-related grants.

### Accounting for liabilities arising from performance-related grants

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- 7.25. The key characteristic of a performance-related grant is that the amount of the grant payable to the recipient is determined by the extent of their performance in meeting the conditions set out in the grant agreement.
- 7.26. The payment of a performance-related grant is conditional on the grant recipient delivering a specified level of service or units of output. For example, the payment might be conditional on the number of meals provided or the usage or opening hours of a facility. In such cases the grant-maker will often have negotiated the nature of services to be provided. The liability and expenditure arising from performance-related grants must be recognised to the extent that the recipient of the grant has provided the specified service or goods.



- 7.27. A grant that is restricted to a particular purpose does not create a performance-related condition, as the payment of the grant is not conditional on the achievement of a specified level of service or outputs by the recipient. Similarly, a grant that funds a project over a number of years is not recognised as a performance-related grant simply because the funding obligation is to be met over an extended period of time.

### Provisions for liabilities

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- 7.28. A charity must recognise a liability for a legal or constructive obligation as a provision when either the timing or the amount of the future expenditure required to settle the obligation is uncertain.
- 7.29. Charities must distinguish separately on the balance sheet provisions for liabilities. The expenditure related to a provision must be charged to the appropriate heading in the SoFA.
- 7.30. The amount recognised as a provision should be the best estimate of the expenditure required to settle or to transfer it to a third party at the reporting date.
- 7.31. Charities must review the best estimate of a provision at the reporting date and adjust it appropriately. If a transfer of resources is no longer needed to settle the obligation, the amount of the provision no longer required should be reversed, with a corresponding credit to the expenditure heading in the SoFA against which the provision was originally charged.
- 7.32. If the settlement date of a provision results in the time value of money being material to the amount recognised, the provision must be recognised at the present value of the expected settlement amount. If the future payments have been adjusted for risk then a discount rate equivalent to the market rate on relevant government bonds may be used. Appendix III to the FRSSE provides an illustrative example of discounting for a provision.

### Treatment of commitments not recognised as provisions or liabilities

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- 7.33. Not all funding commitments are recognised as liabilities or provisions and so it is important that charities disclose the existence of unrecognised commitments and explain how these will be funded. For example, a grant offer may have been made but there is uncertainty as to whether the recipient charity will be able to proceed with its proposal. If it becomes clear that the payment is possible but not probable, then a liability for the commitment should not be recognised. Instead, the funding commitment should be disclosed as a contingent liability. Further guidance on accounting for contingent liabilities is provided in the SORP module '[Balance sheet](#)'.
- 7.34. A charity may intend to use unrestricted funds held at the reporting date to meet a funding commitment and may decide to designate a portion of unrestricted funds for this purpose. This SORP permits the use of a designation on the balance sheet to identify that portion of unrestricted funds that have been set aside to meet the commitments. However, activities that are to be wholly financed from future income must not form part of such a designation.

## Accounting for onerous contracts

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- 7.35. Situations may arise where the unavoidable costs of fulfilling a contract exceed the expected economic benefit derived from it. In such circumstances, a charity must recognise these irrecoverable costs. An onerous contract may arise, for example, when a charity leases a property which it subsequently leaves unused and the property cannot be sub-let to recover the charity's costs.
- 7.36. Routine purchase orders and contracts which can be cancelled by agreement without paying compensation should not be regarded as onerous. However, a charity must make a provision for a material loss-making contract which cannot be cancelled without the payment of compensation. If a charity identifies a contract as onerous, it must make an immediate provision for the unavoidable loss. This provision is the lower of the costs involved in completing the contract and the cost of any compensation payable as result of withdrawing from the contract.
- 7.37. However, a charity may choose to provide a level of service to its beneficiaries over and above the minimum requirements of a contract as part of its charitable activities. Any additional costs incurred in providing a level of service above contractual requirements do not create an onerous contract even when these costs cannot be recovered. Costs that are incurred on a discretionary basis from which the charity can withdraw should be excluded from any assessment of whether a contract is onerous.
- 7.38. A contract entered into on a full cost recovery or cost plus margin basis is only likely to become onerous if unavoidable costs arise in meeting the contract which cannot be recovered under the terms of the contract.

## Disclosure of provisions and funding commitments in the accounts

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- 7.39. This SORP requires that charities must analyse the expenditure resulting from recognised funding commitments and provisions across the appropriate heading(s) in the SoFA and provide in the notes to the accounts:
- a reconciliation of the movements in provisions and funding commitments showing:
    - the carrying amount at the beginning of the reporting period;
    - additions during the reporting period;
    - amounts charged against the provision during the reporting period;
    - unused amounts reversed during the reporting period; and
    - the carrying amount at the end of the reporting period;
  - a brief description of the nature of the provision or commitment made and the expected amount and timing of any resulting payments.

## *Accounting and reporting by charities*

- 7.40. If unrestricted funds have been designated to fund a commitment on the face of the balance sheet, this SORP requires that the notes to the accounts must disclose:
- the nature of any amounts designated; and
  - if not explained in the trustees' annual report, the likely timing of that expenditure.
- 7.41. In addition, charities using this SORP should also disclose for any funding commitment that is not recognised as a liability or provision:
- details of the commitment made;
  - the time frame of that commitment;
  - any performance-related conditions attached to that commitment; and
  - details of how the commitment will be funded.
- 7.42. Comparative information for prior periods is not required by this SORP for any of the disclosures set out in this section.

## **8. Allocating costs by activity in the statement of financial activities**

### **Introduction**

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- 8.1. This module applies to all charities that prepare their statement of financial activities (SoFA) on an activity basis. This SORP requires larger charities above the statutory audit threshold for charities in their jurisdiction(s) of registration to report on an activity basis. The FRSSE does not address presenting a SoFA on an activity basis or the allocation of costs to activities in that statement. This module therefore reflects current practice that must be adopted by charities when allocating costs to the expenditure categories of the SoFA.
- 8.2. This SORP also requires that the SoFA must distinguish between expenditure incurred on charitable activities which contribute to furthering the charity's aims and purposes, and those undertaken to raise funds. Further analysis of significant activities included within these broad categories must be provided either on the face of the SoFA or in the notes to the accounts.
- 8.3. The activity analysis must be on a full cost basis. Full cost is made up of the total of the direct costs and shared costs, including support costs, involved in undertaking each reported activity. This module sets out:
- **general principles for reporting activities;**
  - **identification of support costs;**
  - **methods of allocating costs to activities;**
  - **accounting for costs shared between fundraising and charitable activities; and**
  - **disclosures required in the notes to the accounts.**

### **General principles for reporting activities**

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- 8.4. A charity's SoFA or related notes should provide an analysis of a charity's significant activities in a way that is relevant to both the charity and the users of its accounts.
- 8.5. Significant activities are those which, due to their scale or importance, are key to the charity in meeting its aims and objectives. The analysis of activities should provide an understanding of how a charity raises its funds and uses them to further its purposes. For example, charitable activities may be analysed according to services provided, projects or programmes undertaken, or by the particular aims or objectives taken forward.
- 8.6. The activities reported should also be consistent with the significant activities noted in the trustees' annual report. The narrative provided by the trustees' annual report should help the user of the accounts to understand the nature of those significant activities and what has been achieved as a result of the expenditure incurred on them.

## Identification of support costs

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- 8.7. While some costs relate directly to a single activity, the cost of certain central or regional support functions may be shared across more than one activity undertaken by the charity. For example, governance costs, payroll administration, purchasing, budgeting and accounting, information technology, personnel (human resources), building management services and finance are functions that are likely to support more than one area of activity. These costs must be apportioned across the activities that the function supports in order to arrive at the full cost for each reported activity including relevant restricted funds unless prohibited by the terms of a gift.

## Methods of allocating costs to activities

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- 8.8. To ensure that the accounts present the costs of activities fairly, charities should ensure that the method(s) of cost allocation adopted are reasonable and consistently applied. In attributing costs to activities, the following principles must be applied:
- Direct costs attributable to a single activity must be allocated directly to that activity (for example the salary cost of someone solely employed on a particular activity or the cost of running a vehicle used wholly for a particular activity).
  - Shared costs which contribute directly to more than one activity must be apportioned between those activities (for example the cost of a staff member whose time is divided between a fundraising activity and working on a charitable project).
  - Support costs which are not attributable to a single activity must also be apportioned between the activities being supported.
- 8.9. The method(s) of apportionment adopted by a charity should be reasonable and be consistent between reporting periods unless circumstances change. Charities should also balance the benefits of greater accuracy with the costs involved when selecting methods of apportioning costs. Examples of bases for apportionment that may be applied include:
- usage of a resource or activity in terms of time taken, capacity used, requests made or other measure;
  - per capita, based on the number of people employed within an activity;
  - floor area occupied by an activity; or
  - time, where staff duties span more than one activity.

## Accounting for costs shared between fundraising and charitable activities

- 8.10. Information about the aims, objectives and projects of a charity is frequently provided in the context of mail shots, websites, public fundraising collections and telephone fundraising. In determining whether costs are shared, a distinction should be drawn between:
- publicity or information costs involved in raising the profile of the charity which is associated with fundraising; and
  - educational publicity or information to further the charity's aims and objectives.
- 8.11. For publicity or information to be regarded as charitable expenditure, it must be provided for an educational purpose. In the context of a fundraising activity, in order to achieve an educational purpose the information supplied must fulfill the following educational criteria:
- be targeted at beneficiaries or others who can use the information to further the charity's purposes;
  - be information on which the recipient can act in an informed manner to further the charity's purposes; and
  - be related to other educational activities or objectives undertaken by the charity.
- 8.12. For example, a health education charity might target high-risk beneficiary groups or medical professionals when distributing its fundraising material and, as part of the same mailing, also supply information on health risks and symptom recognition. The health information supplied would be charitable expenditure because it is targeted at beneficiaries or others who could act on the information and has been distributed by the charity as part of its health education activity. The shared cost of producing and distributing the information should therefore be fairly apportioned between the fundraising and charitable activities. If the educational criteria had not been met then all relevant costs would be attributed to fundraising activities.

## Disclosures required in the notes to the accounts

- 8.13. This SORP requires that charities reporting on an activity basis must disclose:
- details of the accounting policy adopted for the apportionment of costs between activities and any estimation technique(s) used to calculate their apportionment;
  - the total amount of support costs incurred in the reporting period;
  - an analysis of material items or categories of expenditure included within support costs, with the total amount of governance costs incurred separately identified (refer to Appendix 1, '[Glossary of terms](#)', for the definition of governance costs); and
  - the amount of support costs apportioned to each of the charity's significant activities as disclosed in the SoFA or in the notes to the accounts.
- 8.14. The information required for support costs and their apportionment may be provided in a tabular format (see Table 4).

Table 4: Analysis of support costs

Support cost (examples)	Raising funds	Activity 1	Activity 2	Activity 3	Total	Basis of allocation
	£	£	£	£		
Governance	x	x	x	x	x	Text describing method
Finance	x	x	x	x	x	Text describing method
Information Technology	x	x	x	x	x	Text describing method
Human Resources	x	x	x	x	x	Text describing method
<b>Total</b>	x	x	x	x	x	

## **9. Disclosure of trustee and staff remuneration, related party and other transactions**

### **Introduction**

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- 9.1. A charity's accounts should inform the user and help them to assess a charity's financial performance and position, and the stewardship exercised by its trustees over the charitable funds held.
- 9.2. Section 15 of the FRSSE sets out the disclosure required for related party transactions. This SORP extends those requirements to provide additional information about remuneration and other transactions relevant to the assessment of stewardship which charities adopting this SORP must provide.
- 9.3. The disclosure of certain transactions is important for stewardship purposes to provide assurance that the charity is operating for the public benefit and that its 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.
- 9.4. A transaction involving a trustee or other related party must always be regarded as material regardless of its size. A charity must make the same disclosures for de facto trustees (see Appendix 1, '[Glossary of terms](#)') as for trustees.
- 9.5. This module sets out:
  - disclosure of trustees' remuneration and benefits;
  - disclosure of trustees' expenses;
  - transactions with related parties that require disclosure;
  - transactions with related parties that do not require disclosure;
  - disclosure of related party transactions;
  - disclosure of audit, independent examination and other financial service fees;
  - disclosure of ex-gratia payments; and
  - disclosure of staff costs and emoluments.



## Disclosure of trustees' remuneration and benefits

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- 9.6. Most trustees are volunteers who give their time and expertise without charge. 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, either directly by the charity or by a related entity, including a subsidiary, joint venture or associate of the charity.
- 9.7. This SORP requires that charities must disclose in the notes to their accounts that either:
- none of the trustees have been paid any remuneration or received any other benefits from an employment with their charity or a related entity; or
  - one or more of the trustees has been paid remuneration or has received other benefits from an employment with their charity or a related entity.
- 9.8. Section 17 of the FRSSE sets out the disclosures required by company law in relation to directors' remuneration. This SORP expands on these aggregate disclosures so that information is presented in charity accounts for each individual trustee who received remuneration or other benefits in the financial year. In particular, this SORP requires that the following information must be provided:
- the legal authority under which the payment was made (for example a provision in the governing document of the charity, an Order of the Court, or the charity regulator for the jurisdiction(s) of registration);
  - the name of the remunerated trustee;
  - details of why the remuneration or other employment benefits were paid;
  - the amount of remuneration paid;
  - the amount of any pension contributions paid by the charity for the reporting period; and
  - the amount of any other benefit, for example any termination benefits, private health cover or the provision of a vehicle.
- 9.9. If a trustee receives remuneration or other benefits from their employment with the charity in addition to their trusteeship, the note may distinguish between remuneration and benefits received as a trustee, if any, from that received for other services or other employment with the charity.

## Disclosure of trustees' expenses

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- 9.10. Trustees may incur costs in fulfilling their duties, for example in travelling to meetings or visiting charity facilities or activities to understand or monitor what is taking place. The reimbursement of properly incurred expenses is not considered a payment for goods or services or the remuneration of a trustee, nor does it count as any kind of personal benefit.

## Accounting and reporting by charities

- 9.11. Trustee expenses include the reimbursement by a charity of costs incurred by its trustees in carrying out their duties and similar payments made by a charity direct to third parties on their behalf. For example, a charity may purchase travel tickets or pay for accommodation used by its trustees when carrying out their duties.
- 9.12. This SORP requires that all charities must disclose either:
- that no trustee expenses have been incurred; or
  - that one or more of the trustees has claimed expenses or had their expenses met by the charity.
- 9.13. If expenses have been incurred, this SORP also requires that charities must disclose:
- the total amount of expenses reimbursed to trustees or paid directly to third parties;
  - the nature of those expenses (for example travel, subsistence, accommodation, entertainment etc.); and
  - the number of trustees reimbursed for expenses or who had expenses paid by the charity.

### Transactions with related parties that require disclosure

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- 9.14. A decision by a charity to enter into any transaction must be made in the charity's own interests and for the benefit of its beneficiaries. The disclosure of related party transactions is an important element of transparency in financial reporting because:
- related parties may enter into transactions that unrelated parties would not;
  - transactions between related parties may not be made at the same amounts or on the same terms as those between unrelated parties; and
  - the existence of the relationship may be sufficient to affect the transactions of the charity with other parties.
- 9.15. Users of the accounts need to be able to assess whether the relationship between the charity and the other party or parties to a transaction may have been influenced by interests other than those of the charity. Disclosing related party transactions also shows how far, if at all, the reported financial position and activities may have been affected by such transactions.
- 9.16. Related party disclosures are dealt with in section 15 of the FRSSE. Related parties include a charity's trustees and their close family members and those entities which they control or in which they have a significant interest. Entities related to a charity include any subsidiary, joint venture or associate of the charity. Appendix 1, '[Glossary of terms](#)' provides a full definition of persons or entities that must be regarded as a related party for disclosure purposes. This SORP extends the definition provided in the FRSSE to include all persons and institutions that are deemed to be connected with a charity or a trustee in charity law.

- 9.17. In considering a possible related party relationship, a charity must assess the substance of the relationship and not merely its legal form. For example, if a person has significant influence over a charity's decision-making or if a charity acts on their instructions, then that person must be treated as related to the charity.
- 9.18. This SORP requires all transactions between a charity and a related party must be disclosed subject to the exemptions set out in the following paragraphs.

### Transactions with related parties that do not require disclosure

- 9.19. Paragraph 15.7 of the FRSSE sets out certain transactions that do not require disclosure as a related party transaction. These include pension contribution paid into a pension fund, emoluments in respect of services as an employee, transactions with providers of finance in the course of their business and transactions with a customer, supplier, franchiser, distributor or general agent. However, this SORP does require the disclosure of pension contributions and emoluments when payments are made in respect of a trustee or other related party. Similarly, this SORP requires the disclosure of transactions between the members of a group controlled by a charity must be disclosed even if the subsidiary is wholly owned or controlled.
- 9.20. The following transactions involving trustees or other related parties need not be disclosed unless there is evidence to indicate that they have influenced the charity's activities or use of resources:
- Donations to the reporting charity from a trustee or a related party provided the donor has not attached conditions which would, or might, require the charity to alter significantly the nature of its existing activities if it were to accept the donation. Examples of conditions that make the donation a transaction that must be disclosed include: requiring the charity to purchase goods or services from a specified supplier; making an interest bearing loan to the charity; or requiring that payments be made to a specified third party.
  - Services provided on a voluntary basis to a charity as an unpaid general volunteer by a trustee or other related party.
  - Contracts of employment between the charity and its employees (except where the employee is a trustee or other related party).
  - Contributions by the charity to a pension fund for the benefit of employees (except where the employee is a trustee or other related party).
  - The purchase from the charity by a trustee, or other related party, of minor articles which are offered for sale on the same terms as they are offered to the general public, for example a small purchase made from a charity shop.
  - The provision of services to a trustee or other related party where the services are received on the same terms as they are received by other beneficiaries of the charity. Examples include the use of a village hall by members of its committee of management as inhabitants of the area of benefit.
  - The payment or reimbursement of out-of-pocket expenses where the trustee acts as agent for charity (but certain details of trustee expenses must be disclosed – see '[Disclosure of trustees' expenses](#)' above).

- The amount of any expenses waived by a trustee need not be disclosed unless the amount is material in the context of a charity's total expenditure.

### Disclosure of related party transactions

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- 9.21. If there have been no related party transactions in the reporting period that require disclosure, this SORP requires that this fact must be stated.
- 9.22. The FRSSE requires that charities that have one or more related party transactions must disclose:
- the names of the transacting related parties;
  - a description of a relationship between the parties;
  - a description of the transactions;
  - the amounts involved;
  - any other elements of the transactions necessary for an understanding of the accounts;
  - the amounts due to or from related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date; and
  - amounts written off in the period in respect of debts due to or from related parties.
- 9.23. Paragraph 15.6 of the FRSSE allows charities to disclose related party transactions on an aggregated basis (aggregation of similar transactions by type of related party) unless disclosure of an individual transaction, or connected transactions, is necessary for an understanding of the impact of the transactions on the accounts of the reporting charity or is required by law.

### Disclosure of audit, independent examination and other financial service fees

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- 9.24. This SORP requires that charities must disclose in the notes to the accounts the amounts payable to their auditor or independent examiner, analysed between fees payable for:
- statutory audit or independent examination;
  - assurance services other than audit or independent examination;
  - tax advisory services; and
  - other financial services, for example consultancy, financial advice or accountancy services.

## Disclosure of ex-gratia payments

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- 9.25. An ex-gratia payment is a payment (or the waiver of a right to an asset) which the trustees have no legal obligation or legal power to make from a charity's funds but which they believe they have a moral obligation to make. For the purposes of disclosure, occasional gifts of small and inexpensive items such as flowers or chocolates should not be regarded as ex-gratia payments.
- 9.26. This SORP requires that charities must disclose details of all ex-gratia payments made including those where the charity has obtained the authority of the Court, the Attorney General or the charity regulator for the jurisdiction(s) of registration to sanction the payment or waiver. Charities may aggregate payments of a similar nature where this does not impact on the understanding of the arrangement. For each payment (or in aggregate) the notes to the accounts must:
- provide an explanation of the nature of the payment;
  - state the legal authority or reason for making the payment; and
  - state the amount of the payment (or value of any waiver of a right to an asset).

## Disclosure of staff costs and emoluments

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- 9.27. This SORP requires that charities reporting on an activity basis must provide details of their total staff costs for the reporting period, analysed between:
- wages and salaries;
  - social security costs;
  - employer's contribution to defined contribution pension schemes;
  - the operating costs of defined benefit pension schemes (excluding pension finance costs related to defined benefit pension schemes); and
  - other forms of employee benefits.
- 9.28. In addition, the note must state the amount of any redundancy or termination payments relating to the reporting period.
- 9.29. The information provided for staff costs and emoluments must also include any expenditure on staff working for the charity whose contracts are with and are paid by a related party.
- 9.30. This SORP requires that all charities must disclose the average head count (number of staff employed) during the reporting period. Charities may also provide details of the average number of full-time and part-time staff for the reporting period together with an estimate of the equivalent number of full-time staff. Further analysis of staffing according to the number of staff engaged in particular activities of the charity may also be provided where this information helps the user of the accounts understand how staff are deployed.

## *Accounting and reporting by charities*

9.31. This SORP also requires that all charities must disclose:

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

9.32. The trustees of charities, particularly larger charities (charities subject to charity audit), should give consideration to the information needs of their funders and other stakeholders in making their accounting disclosures. For example, it may be helpful to provide details of the remuneration and other benefits received by the charity's Chief Executive officer or highest paid staff member, or alternatively a charity may choose to disclose the amount of remuneration and other benefits paid to its key management personnel on an individual basis.

## 10. Balance sheet

### Introduction

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- 10.1. All charities preparing accruals accounts must prepare a balance sheet at the end of each reporting period which gives a true and fair view of their financial position. The balance sheet provides a snapshot statement of a charity's assets and liabilities and how these are represented by the different classes of funds held by a charity.
- 10.2. The objective of the balance sheet is to show the resources available to the charity and whether these are available for all purposes of the charity or have to be used for specific purposes because of legal restrictions placed on their use.
- 10.3. The FRSSE sets out the format of the balance sheet required by company law which must be adapted for the additional presentational requirements of charities. This module sets out the format and content of a charity's balance sheet and the additional disclosures that must be provided by charities adopting this SORP.
- 10.4. This module sets out:
- structure of the balance sheet;
  - fixed assets – headings, classification and disclosures;
  - current assets – headings, classification and disclosures;
  - liabilities – headings, classification and disclosures; and
  - funds of the charity – classification and disclosures.
- 10.5. Each section explains:
- what items are included in each heading of the balance sheet;
  - the recognition principles and the measurement methods used for balance sheet items; and
  - the information that must be, or should be, provided in the notes if not shown on the face of the balance sheet.
- 10.6. For information on the recognition and measurement of financial assets and liabilities charities must refer to the SORP module '[Accounting for financial assets and financial liabilities](#)'.

### Structure of the balance sheet

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- 10.7. Table 5 sets out the format of a charity's balance sheet and the headings used to present its assets, liabilities and funds. A charity's balance sheet must:
- adopt the same format in subsequent reporting periods unless there are special reasons for a change that are explained in the notes; and
  - provide corresponding amounts for the previous reporting period for each heading disclosed in the balance sheet.

Table 5: Balance sheet

Note ref.		Total funds	Prior year funds	Further details
		£	£	
	<b>Fixed assets:</b>			A
	Intangible assets			A1
	Tangible assets			A2
	Heritage assets			A3
	Investments			A4
	<i>Total fixed assets</i>			
	<b>Current assets:</b>			B
	Stocks			B1
	Debtors			B2
	Investments			B3
	Cash at bank and in hand			B4
	<i>Total current assets</i>			
	<b>Liabilities:</b>			C
	Creditors: Amounts falling due within one year			C1
	<i>Net current assets or liabilities</i>			
	<i>Total assets less current liabilities</i>			
	Creditors: Amounts falling due after more than one year			C2
	Provisions for liabilities			C3
	<i>Net asset or liabilities excluding pension asset or liability</i>			
	Defined benefit pension scheme asset or liability			C4
	<b>Total net assets or liabilities</b>			
	<b>The funds of the charity:</b>			D
	Endowment funds			D1
	Restricted income funds			D2
	Unrestricted funds			D3
	Revaluation reserve			D4
	Pension reserve			D5
	<i>Total unrestricted funds</i>			
	<b>Total charity funds</b>			



## Accounting and reporting by charities

- 10.8. If there is a nil amount for a particular balance sheet heading in the current reporting period, a corresponding amount for the reporting period must still be disclosed unless that amount is also nil. If the amount for both the current and previous reporting periods is nil, then the heading should be omitted from the balance sheet.
- 10.9. The balance sheet must be signed by one or more trustees, each of whom has been authorised to do so by the trustee body, and must specify the date the accounts, including the balance sheet, were approved by the trustee body.
- 10.10. Where necessary to give a true and fair view, additional information must be provided in an additional heading or sub-heading in the balance sheet or given in a note to the accounts. Charities may choose to analyse the items included in any balance sheet heading in greater detail either on the face of the balance sheet or in a related note. The balance sheet may also be presented in a columnar format that analyses balance sheet items by class of fund: unrestricted, restricted income and endowment.
- 10.11. Where the corresponding amount for the previous reporting period is not comparable due to a change in accounting policy it must be adjusted if material to the balance sheet and the reason for the adjustment explained in the notes to the accounts.
- 10.12. The sections that follow are cross-referenced to the analysis headings shown in Table 5.

### A: Fixed assets – headings, classification and disclosures

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- 10.13. Fixed assets provide an economic benefit to the charity on an on-going basis (i.e. for more than one reporting period) through their ability to:
- generate income and/or gains; and/or
  - contribute to furthering the charity's objectives.
- 10.14. Charities that hold or have received donated fixed assets in the reporting period must refer to the SORP module '**Donated goods, facilities and services, including volunteers**'.

#### **Disclosure in the notes applying to all classes of fixed assets**

- 10.15. For each class of fixed assets, the following analysis of their cost or valuation must be provided in the notes to the accounts:
- cost or valuation at the beginning of the reporting period;
  - acquisitions during the reporting period;
  - revaluations during the reporting period;
  - disposals during the reporting period;
  - transfers to or from that class of item during the reporting period; and
  - cost or valuation at the end of the reporting period.

10.16. The following analysis must also be provided for each class of fixed assets that is subject to depreciation:

- the cumulative amount of depreciation or impairment provided at the beginning of the reporting period;
- amount adjusted on disposal;
- amount of depreciation provided in the reporting period;
- amount of any write down of assets in the reporting period;
- amount of any reversals in the reporting period of amounts previously written off;
- amount of any transfer or other adjustment in the reporting period; and
- the cumulative amount of depreciation and amounts written off at the end of the reporting period.

10.17. This SORP also requires that the carrying amount for each class of fixed assets must also be provided at the beginning and end of the reporting period.

### **A1: Intangible fixed assets**

10.18. Intangible fixed assets are non-financial fixed assets that do not have physical substance but are identifiable and are controlled by the charity through custody or legal rights. Intangible fixed assets include goodwill purchased on the acquisition of a business and/or purchased intangible assets such as concessions, patents, licences, trademarks and similar rights. Although such assets lack physical substance they provide an on-going economic benefit to the charity.

10.19. The cost of internally generated goodwill or intangible assets such as brands and logos must not be capitalised and are written off as expenditure as incurred. Expenditure on research must always be written off, but the costs incurred in the development phase of an internal project may in certain circumstances be recognised as an intangible asset.

10.20. The criteria for the recognition of development costs as an intangible asset are rigorous and involve a demonstration of technical and financial feasibility of the development asset. For more information refer to section 6 of the FRSSE.

10.21. Intangible fixed assets must be measured at their historical cost and not revalued. The residual value of intangible fixed assets is nil when calculating the charge for depreciation unless reliable evidence exists to the contrary. Depreciation on intangible fixed assets must be charged as an expense to the relevant statement of financial activities (SoFA) category reflecting the use of the asset.

10.22. Capitalised goodwill and intangible assets must be depreciated on a straight-line (or a more appropriate) basis over their useful economic lives. If the useful life of the asset cannot be reliably measured, it must be presumed to be less than five years. The useful economic life must be reviewed at each reporting date and revised as necessary but must not exceed twenty years from the date of acquisition.

## *Disclosures*

10.23. The FRSSE requires that the notes to the accounts must disclose:

- the amount of negative goodwill on the balance sheet and the period(s) in which it is being written back shall be disclosed; and
- the period chosen for depreciation goodwill and the reason for choosing that period.

10.24. In addition, this SORP requires that the notes to the accounts:

- explain the accounting policies adopted for goodwill and intangible assets, including the measurement basis adopted, the depreciation rates and methods used and, where relevant, the policies for the recognition of any capitalised development expenditure; and
- provide an analysis reconciling the opening and closing carrying amounts of each class of intangible asset held.

## **A2: Tangible fixed assets**

10.25. Tangible fixed assets, such as land and buildings, plant, vehicles and equipment, are assets that have physical substance and are used for the provision of goods or services by the charity or to support their provision on a continuing basis.

10.26. Tangible fixed assets must be measured initially on the balance sheet at their historical cost. All costs incurred to bring a tangible fixed asset into its intended working condition should be included in the measurement of cost. Charities may adopt an accounting policy of capitalising borrowing costs, including interest, that are directly attributable to the construction of tangible fixed assets, or may write off such borrowing costs as an expense in the SoFA as they are incurred.

### *Accounting for hire purchase and leasing arrangements*

10.27. If leasing a tangible fixed asset, the lease must be classified as a finance lease unless it meets the criteria of an operating lease. The characteristic of a finance lease is that the hire purchase or lease arrangements transfer substantially all the risks and rewards of ownership to the lessee. A finance lease is recorded in the balance sheet of the lessee charity as an asset and a liability is recognised for the obligation to pay future rentals. Charities should refer to section 7 of the FRSSE for more information about the recognition, measurement and note disclosures required for leased assets.

### *Accounting for depreciation*

10.28. A tangible fixed asset, less its residual value (its scrap or realisable value at the end of its economic life), must be depreciated on a systematic basis over its useful economic life. The charity should choose a depreciation method which reflects the use of the asset and the expected timing or pattern of consumption of its economic benefits.

10.29. Some assets may have a high residual value which will remove the need for depreciation to be charged. For example, land is not depreciated because it will not generally wear out and its residual valuation is likely to be at least equal to its cost or valuation.

## *Accounting and reporting by charities*

- 10.30. Where an asset comprises two or more major components which have substantially different useful economic lives, each component must, unless impractical or involving undue cost or effort, be depreciated separately over its useful economic life.
- 10.31. The depreciation charged for the reporting period must be recognised as an expense in the SoFA. The expense is charged or apportioned to the relevant SoFA heading(s) reflecting the asset's use.
- 10.32. Charities that constantly replace their tangible fixed assets as they wear out may opt not to depreciate them provided their value is not material and their quantity, value and composition are not subject to material variation from one year to the next. Instead, such tangible fixed assets may be included at a fixed amount in the balance sheet, with the cost of replacement assets charged or apportioned to the relevant SoFA heading(s) reflecting the asset's use.

### *Accounting for the revaluation of tangible fixed assets*

- 10.33. A charity may choose to adopt an accounting policy of revaluing one or more classes of the tangible fixed assets it holds at its market value (or best estimate thereof). For example, land and buildings may be revalued but not motor vehicles. If a policy of revaluation is adopted, then all assets within that particular class must be revalued. Buildings of a similar nature, function or use held by the charity constitute a class of tangible fixed assets. If one particular class of building is revalued, then all buildings of a similar nature, function or use held by the charity must be revalued.
- 10.34. Charities should ensure that valuations are sufficiently frequent to reflect material changes in market values. For example, land and buildings might be valued on a rolling basis over a five-year period. The value of land and buildings is usually determined from market-based evidence. However, if the trustees believe that a reliable market valuation is not possible, then the 'value in use' to the charity or the depreciated replacement cost of the building should be used. The FRSSE requires valuations of land and building to be undertaken by an experienced valuer although this SORP specifically permits the valuation to be carried out by a trustee or by a member of the charity's staff who has experience and knowledge of the relevant property market.
- 10.35. In the case of other tangible fixed assets such as motor vehicles, there may be an active second-hand market for the asset, or appropriate indices may exist allowing a valuation to be made with reasonable reliability. In such cases, the valuation need not be undertaken by a qualified valuer and may be undertaken by an appropriate person either internal or external to the charity.
- 10.36. If a policy of revaluation is adopted, then revaluations and recognised gains and losses must be presented in the accounts as follows:
- A separate revaluation reserve must be shown within the funds analysis on the balance sheet.
  - Revaluation gains must be recognised as 'Gains on the revaluation of fixed assets' within the SoFA, unless they reverse a charge for impairment that has previously been recognised as a cost within the expenditure headings of the SoFA.

## *Accounting and reporting by charities*

- Any gain on disposal over the carrying amount must be recognised in 'Other' income within the SoFA.
- Revaluation losses must be recognised as an expense in the relevant expenditure heading of the SoFA except to the extent to which they offset any previous revaluation gains, in which case the loss is shown in the 'Gains/(losses) on the revaluation of fixed assets' section of the SoFA.

### *Disclosures*

10.37. The FRSSE requires that the notes to the accounts must:

- set out the depreciation method used and the useful economic lives of assets or the depreciation rate used;
- explain the effect of any change in the method of depreciation and the reason for the change;
- state the amount of finance costs, if any, capitalised in the cost of tangible fixed assets;
- state the amount of contractual commitments to acquire tangible fixed assets; and
- identify the existence and carrying amounts of property, plant and equipment to which the charity has restricted title or that are pledged as security for liabilities.

10.38. In addition, this SORP requires an analysis reconciling the opening and closing carrying amounts of each class of tangible fixed asset held to be provided. An example of such an analysis is given in Table 6.

10.39. If any class of tangible fixed assets has been revalued, charities reporting under the FRSSE must disclose:

- the year in which they were revalued;
- in the case of assets that have been revalued during the reporting period, the names of the persons who valued them or particulars of their qualifications for so doing;
- the bases of the valuation; and
- the historical cost of each class of asset revalued.

**Table 6: Analysis of opening and closing carrying amounts**

	Freehold land and buildings	Leasehold land and buildings	Plant and machinery	Fixtures, fittings and equipment	Total
	£	£	£	£	£
<b>Cost or valuation</b>					
At beginning of the year					
Additions					
Disposals					
Revaluations					
Transfers					
<b>At end of the year</b>					
<b>Depreciation and impairments</b>					
At beginning of the year					
Disposals					
Depreciation					
Impairment					
Transfers					
<b>At end of the year</b>					
Net book value at beginning of the year					
Net book value at end of the year					

### A3: Heritage assets

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

10.41. Heritage assets are a distinct class of tangible fixed asset or intangible fixed asset. Charities holding heritage assets must refer to the SORP module '[Accounting for heritage assets](#)'. This module explains the recognition, measurement and disclosures relevant to heritage assets.

#### **A4: Investments**

10.42. Fixed asset investments are held to generate income or for their investment potential, or both. Investments may include 'social investments' where the purpose in making the investment is wholly or partly to further the charity's aims.

10.43. Fixed asset investments exclude those investments held specifically for sale or those investments which the charity expects to realise within 12 months of the reporting date.

10.44. Investment gains and losses, whether realised or unrealised, are combined and shown in the heading 'Gains/(losses) on investments' in the SoFA.

#### *Investments listed or traded on a recognised stock exchange*

10.45. This SORP requires that fixed asset investments in quoted shares, traded bonds and similar investments must be carried in the balance sheet at their market value at the reporting date.

#### *Investment properties*

10.46. An investment property is an interest in land and/or buildings whose construction and development is completed and is held for its investment potential with rental income being negotiated at an arm's length. A property that is occupied by a charity for its own purposes or let to and occupied by another entity within the same group must not be included within investment properties.

10.47. Land and/or buildings are excluded from investment properties and treated as tangible fixed assets instead if:

- the construction work and development has not been completed; or
- the property is occupied by the charity for its own purposes; or
- the property is let and occupied by another group undertaking; or
- the property is held for sale in the ordinary course of business (in which case the property should be included as a current asset).

10.48. This SORP requires that mixed use property should be separated between investment property and property held for operational use as a tangible fixed asset. However, if the market value of the investment property component cannot be valued reliably without undue cost or effort, current practice requires that the entire property should be accounted for as property within tangible fixed assets.

10.49. The FRSSE requires that investment properties must be included in the balance sheet at their market value. Depreciation is not provided on investment property except where it is held on a lease with an unexpired term of 20 years or less.

### *Unlisted investments*

10.50. The SORP requires that unlisted equity investments should be included in the balance sheet at the best estimate of their market value where practicable. Estimates of value may be based, for example, on the underlying net assets or by reference to earning or dividend record from the investment. Where valuation techniques are considered unreliable or the cost involved in the valuation outweighs the benefits to the users of the accounts, the investment should be included at its cost and assessed at each reporting date for any indication that the asset should be written down. Where the charity holds an interest in subsidiaries, associates and joint venture entities, it should refer to the relevant SORP module(s).

### *Social investments*

10.51. This SORP uses the term 'social investments' to describe programme related and mixed motive investments. Programme related investments are held to further the charitable purposes of the investing charity. Although programme related investments can generate a financial return, the achievement of a financial return is incidental to furthering the charitable purposes of the investing charity.

10.52. 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.

10.53. Charities holding mixed motive or programme related investments must refer to the SORP module '[Accounting for social investments](#)', which explains their recognition, measurement and disclosure.

### *Disclosure of investments and investment properties*

10.54. This SORP requires that notes to the accounts must:

- state the accounting policies for investments, including the basis on which investments are valued;
- provide an analysis of investments by class of investment identifying the amounts held within each class, with those investments held at market value differentiated from those held at historical cost less any write down; and
- provide an analysis reconciling the opening and closing carrying amounts of each class of fixed asset investment held.

10.55. The classes of investments disclosed in the note will vary from charity to charity reflecting the differing nature of the investments held. The analysis required by the SORP must as a minimum identify material amounts held in the following classes of investment:

- cash or cash equivalents;
- listed investments;
- investment properties;
- loans to group undertakings;



- equity investment in group undertakings;
- social investments; and
- other investments.

10.56. The FRSSE also requires that charities holding investment property must disclose:

- the name or particulars of the qualifications of the person who undertook the valuation of investment property;
- the bases used by them; and
- whether the person undertaking the valuation was an employee of the charity.

## **B: Current assets – headings, classification and disclosures**

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10.57. Current assets are the assets of the charity which are not intended for use on a continuing basis in the charity's activities and are usually consumed, realised or expended as part of the charity's activities, within 12 months of its reporting date. Current assets include stocks, debtors, investments held for sale and cash. The sections that follow set out how these categories of assets are measured and disclosed in the accounts. Charities should also refer to Section 8 and Appendix III of the FRSSE.

10.58. Charities that hold donated assets for distribution or resale or have received them in the reporting period must refer to the SORP module '[Donated goods, facilities, and services, including volunteers](#)'.

### **B1: Stocks**

10.59. Stocks are items that will be used by the charity in providing goods and services. Stocks may include goods held for distribution to beneficiaries, or educational literature or brochures for distribution.

10.60. Stocks held for sale as part of a non-charitable trade must be measured at the lower of the cost and net realisable value of the separate items of stock or groups of similar items.

10.61. When goods or services are provided as part of a charitable activity either free or at a subsidised cost, then net realisable value should be based on the service potential provided by the items of stock. For example, if goods are held for free distribution and the item continues to meet the need(s) for which it was purchased, then it should not be written down to a nil realisable value except where the item of stock is damaged or obsolete. Damaged or obsolete stocks should be written down as an expense and charged to the relevant SoFA heading(s) reflecting their intended use.

10.62. When stocks are immaterial to the balance sheet, the FRSSE permits their inclusion in the balance sheet at a fixed amount provided:

- the quantity, value and composition of the stocks does not vary materially;
- the stocks are being constantly replaced;
- the value is not material to assessing the charity's state of affairs; and
- all the costs incurred in the production of stock items in the reporting period are charged to the relevant activity category of the SoFA.

10.63. Charities which have contracts of less than one year's duration may have work in progress at the reporting date. Where the value of work in progress is material, it should be valued at cost less any foreseeable loss that is likely to occur on the contract and shown separately as a subheading within stock.

### *Disclosures*

10.64. This SORP requires that notes to the accounts must disclose:

- the accounting policies adopted in measuring the value of stocks and, if applicable, work in progress and any cost formulae used; and
- the carrying amount of stocks and, if applicable, work in progress analysed between activities.

## **B2: Debtors**

10.65. Debtors include amounts owed to the charity for the provision of goods and services or amounts the charity has paid in advance for the goods and services it will receive. Debtors also include amounts receivable on grant funding to which the charity is entitled.

10.66. Debtors must be measured at their recoverable amounts (the amount the charity anticipates it will receive from a debt or the amount it has paid in advance for goods or services).

### *Disclosures*

10.67. This SORP requires that the notes to the accounts must set out, within the disclosure of accounting policies, the basis on which debtors are measured.

10.68. This SORP also requires that the notes to the accounts must provide an analysis of the amounts, including comparatives for the previous reporting period, of the following items:

- trade debtors;
- amounts owed by group and associated undertakings;
- prepayments and accrued income; and
- other debtors.

10.69. If material to the disclosure of debtors, the amount of debtors recoverable more than a year after the reporting date must be separately disclosed in the notes to the accounts.

### **B3: Current asset investments**

10.70. Current asset investments are investments which a charity holds for resale or pending their sale and cash or cash equivalents with a maturity date of less than one year.

This heading includes cash on deposit and cash equivalents with a maturity of less than one year held for investment purposes rather than to meet short-term cash commitments as they fall due.

10.71. To be classified as a current asset, the charity should not intend to hold the cash or cash equivalents as part of its on-going investment activities for more than one year from the reporting date. However, cash and cash equivalents that are held from time to time as part of a fixed asset investment portfolio should be presented as part of fixed asset investments. Current asset investments must be valued at their market value (i.e. the current value measured at the lower of the cost to replace the asset and its net realisable value if sold).

#### *Disclosures*

10.72. This SORP requires that the notes to the accounts must explain, within the disclosure of accounting policies, the basis on which current asset investments are measured and how the charity has defined any short-term, highly liquid investments as current asset investments.

10.73. This SORP also requires that the notes must provide an analysis of amounts, including comparatives for the previous reporting period, of the following items included within current asset investments:

- cash on deposit;
- investment properties held for sale;
- investment in group undertakings held for sale;
- listed investments; and
- other investments.

### **B4: Cash at bank and in hand**

10.74. Cash at bank and in hand is held to meet short-term cash commitments as they fall due rather than for investment purposes and may include short-term deposits.

## **C: Liabilities (C1 to C3) – headings, classification and disclosures**

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10.75. Liabilities are amounts due to creditors and any provision made as a result of an obligation to transfer economic benefits, usually in the form of a cash payment, to a third party. Liabilities must be measured at their settlement amount. A liability is recognised for the amount that the charity anticipates it will pay to settle the debt or the amount it has received as an advance payment for goods or services it must provide.

10.76. A provision is a liability where the amount and/or timing of its settlement is uncertain. The FRSSE requires a provision to be recognised only when:

- there is a present obligation at the reporting date as a result of a past event;

## *Accounting and reporting by charities*

- it is probable that a transfer of economic benefit, usually in the form of cash, will be required in settlement; and
- the amount of the settlement can be estimated reliably.

10.77. Provisions for liabilities must be measured at the best estimate of their settlement amount. If the settlement amount provided takes account of risk then the discount rate used may be based on the market rate on relevant UK government bonds. The unwinding of the discount is treated as a finance cost, which is an item of charitable expenditure if it relates to a charitable activity.

10.78. Provisions recognised in the balance sheet must be reviewed at the reporting date and adjusted to reflect the current best estimate of the settlement amount.

### *Disclosures*

10.79. In the balance sheet, the SORP requires that creditors and provisions must be analysed between:

- (C1) creditors: amounts falling due within one year;
- (C2) creditors: amounts falling due after one year; and
- (C3): provisions for liabilities.

10.80. This SORP requires that the notes to the accounts must explain, within the disclosure of accounting policies, the basis on which creditors and provisions for liabilities and charges are recognised and measured.

10.81. This SORP also requires that in the notes, creditors falling due within one year and after one year must be analysed between:

- accruals for grants payable;
- bank loans and overdrafts;
- trade creditors;
- amounts owed to group and associated undertakings;
- payments received on account for contracts or performance-related grants;
- accruals and deferred income;
- taxation and social security; and
- other creditors.

10.82. The FRSSE also requires the disclosures, where applicable, of:

- the amount of the provision at the beginning and end of the reporting period;
- any amounts transferred to or from the provision during the reporting period;
- the source and application of the amounts transferred; and
- particulars of each material provision included in the balance sheet.

### *Contingent liabilities and contingent assets*

10.83. A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because:

- a transfer of economic benefit to settle the possible obligation is not probable; or
- the amount of the obligation cannot be estimated reliably.

10.84. A contingent asset is a possible asset that arises from a past event but is not recognised in the balance sheet as its existence can only be confirmed by future events which are not within the charity's control.

### *Disclosures*

10.85. Contingent liabilities are disclosed unless the possibility of their existence is remote. Contingent assets are disclosed when their existence is probable.

10.86. The FRSSE requires that charities must provide details of:

- the nature of each contingent item;
- where practicable, an estimate of its financial effect;
- the legal nature of the contingency;
- any charge on any assets of the charity and where practicable the amount secured; and
- the aggregate amount of any contracts for capital expenditure (including under finance leases) or other financial commitments not provided for in the balance sheet.

### **C4: Defined benefit pension scheme asset or liability**

10.87. Charities that participate in a defined benefit pension scheme must refer to the SORP module '**Retirement benefits**' for the recognition, measurement and disclosure of defined benefit pension scheme assets and liabilities.

## **D: Funds of the charity (D1 to D4) – classification and disclosures**

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10.88. The assets and liabilities administered by a charity are referred to as its funds.

10.89. Charities must refer to the SORP module '**Fund accounting**', which sets out the required disclosures for the separate funds a charity may hold. A charity may choose to disclose the amount identified in its reserves policy statement as its reserve fund under a sub-heading of its unrestricted funds provided that this amount is positive.

10.90. A revaluation reserve arises on the revaluation of an asset subsequent to its initial recognition. While a revaluation reserve will often form part of the unrestricted funds of the charity, any part of the reserve derived from the revaluation of assets held within a restricted fund must be shown as part of restricted funds.

10.91. The SORP permits charities participating in a defined benefit pension scheme to show the equivalent value of the pension asset or liability as a separate pension reserve. The pension reserve will often form part of the unrestricted funds of the charity. The circumstances when part of a pension reserve may be allocated to a restricted fund are set out in the SORP module '**Retirement benefits**'.

## 11. Accounting for financial assets and financial liabilities

### Introduction

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- 11.1. All charities are likely to have financial assets and financial liabilities. The FRSSE use the term 'financial instruments' to include both financial assets and financial liabilities. Charities reporting under the FRSSE should refer to section 12 of the FRSSE when accounting for financial instruments.
- 11.2. Financial assets include cash, shares held in other entities and contractual rights to receive cash or other financial assets from other entities, for example trade debtors or loans made by the charity.
- 11.3. A financial liability is a contractual obligation to transfer cash or another financial asset to another entity, for example trade creditors, a loan received by a charity or a provision made in relation to a grant commitment.
- 11.4. Concessionary loans made by charities to further their charitable aims are financial instruments.
- 11.5. An asset or liability arising from a non-exchange transaction such as a gift or a grant is not a financial instrument because it is non-contractual in nature. For certain non-exchange transactions where settlement is delayed and the effect of the time value of money is material, the transaction is recognised at the present value of the likely settlement amount.
- 11.6. This module deals with how financial assets and financial liabilities are accounted for except for those detailed below which are covered by other SORP modules:
  - investments in subsidiaries, associates and joint ventures;
  - leases; and
  - defined benefit pension schemes.
- 11.7. Charities that hold derivative products and other more complex financial instruments should have regard to their own existing accounting policies for these transactions. If a charity has no existing policy, in developing a new policy it should have regard to sections 11 and 12 of FRS 102. More complex arrangements that charities may enter into include advance fee schemes and contracts or options to buy or sell foreign currency.
- 11.8. This module sets out:
  - **accounting for financial instruments;**
  - **accounting for concessionary loans made or received; and**
  - **disclosures to be made in the notes to the accounts.**

## Accounting for financial instruments

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- 11.9. Charities preparing accounts using the FRSSE normally measure a financial asset or financial liability on its first recognition at the amount receivable or payable. However, borrowings must be stated in the balance sheet at fair value of the loan received. The carrying amount of the borrowing is then increased by the finance cost for the reporting period and reduced by payments made in respect of the borrowings. The finance costs must be allocated to periods over the term of the borrowing at a constant rate and charged to the activities disclosed in the SoFA that the borrowing funded.
- 11.10. Where borrowings involve an arrangement fee that is a significant additional cost of finance compared with the interest payable over the life of the loan, the arrangement fee must be treated as a finance cost and allocated to periods over the term of the borrowing at a constant rate. Where any arrangement fee is not significant, the fee must be charged as an expense to the relevant heading(s) of the SoFA immediately it is incurred.
- 11.11. Depending on their nature, financial instruments are carried in the balance sheet at the value of the consideration payable or receivable, market value or fair value of the instrument. For example:
- Current assets and current liabilities arising from contractual rights or obligations (for example trade debtors or trade liabilities) must be carried in the balance sheet at the cash amount or other consideration expected to be received or paid in their settlement.
  - Borrowings, for example, a bank loan, must be measured at the fair value of the loan (see paragraph 11.9).
  - This SORP requires that investments in listed shares which can be publicly traded must be measured at their market value.
  - Investments in shares which cannot be publicly traded must be measured at cost less any provision for their diminution in value if a reliable estimate of market value cannot be established by the trustees, for example by using a valuation technique.

## Accounting for concessionary loans made or received

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- 11.12. Concessionary loans are those loans made or received by a charity to further its purposes and any interest charged is below the prevailing market rates. See the SORP module '[Accounting for social investments](#)' for the accounting treatment of concessionary loans.

## Disclosures to be made in the notes to the accounts

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- 11.13. All charities must provide the detailed disclosure of assets and liabilities required by the SORP module '[Balance sheet](#)'.
- 11.14. This SORP requires that charities must disclose the accounting policy adopted for each material class of financial instruments, including financial assets and liabilities.
- 11.15. If the charity makes or receives a concessionary loan, reference must also be made to the SORP module '[Accounting for social investments](#)'.

## 12. Write-down of assets to their recoverable amounts

### Introduction

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- 12.1. The FRSSE requires that fixed assets and goodwill must be carried in the balance sheet at no more than the recoverable amount. The recoverable amount of an asset is the higher of the amounts that can be obtained from selling the asset (i.e. net realisable value) or continuing to use the asset in the business (i.e. value in use). If the carrying amount (net book amount) of a fixed asset or goodwill is considered not to be recoverable in full at the balance sheet date, the carrying value of the asset must be written down to the estimated recoverable amount.
- 12.2. Charities reporting under the FRSSE when assessing whether there is any indication that an asset should be written down should refer to paragraphs 6.44 to 6.48 of the FRSSE.
- 12.3. This module must be applied by all charities using the FRSSE and applies to capitalised goodwill and all fixed assets (i.e. tangible fixed assets, intangible assets and investments) except:
- investment properties;
  - programme related or mixed motive investments which must be referred to the SORP module 'Accounting for social investments'; and
  - financial instruments (other than investments in subsidiaries, associates and joint ventures).
- 12.4. This module sets out:
- assessing if a write-down is required;
  - indications that the recoverable amount should be estimated;
  - estimating the recoverable amount;
  - accounting for write-downs and reversals; and
  - disclosures to be made in the notes to the accounts.

### Assessing if a write-down is required

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- 12.5. At each reporting date an assessment must be carried out of whether there is any indication that an asset should be written down (i.e. whether its carrying amount is more than its recoverable amount). If there is no indication that an asset should be written down, it is not necessary to estimate the recoverable amount.



## Indications that the recoverable amount should be estimated

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- 12.6. When assessing whether there is any indication that an asset should be written down, charities must refer to the FRSSE (paragraphs 6.45A to 6.45C) which lists a number of factors which might be considered. These factors include:
- a significant decline in an asset's market value;
  - significant changes in technology or markets, or in the economic or legal environment, which have an adverse effect on the charity's activities;
  - an asset becoming idle, or plans being made for its disposal earlier than expected;
  - evidence of an asset's obsolescence or physical damage; and
  - evidence of worse than expected results or cash flow from the use of an asset.
- 12.7. The demand or need for the services provided by a charity using an asset may fluctuate over time and a temporary reduction in demand is not necessarily an indication that an estimate of the recoverable amount is required. Similarly, an asset's service potential may not always be fully utilised and surplus capacity at certain periods will not always indicate that an estimate of the recoverable amount is needed. For example, it may be necessary to have the spare capacity to respond to urgent need or have the capacity to provide services at all times in the face of fluctuating need. In such circumstances, the surplus capacity is part of the required service potential of the asset and should not be taken as an indication that the asset recoverable amount should be estimated.
- 12.8. However, where demand for services significantly decreases or ceases, this would be an indication that the recoverable amounts of the assets used to provide those services must be estimated. Similarly, major social, demographic or environmental changes may have an impact on the number, nature or needs of a charity's beneficiaries and may therefore also provide an indicator of the need to estimate the recoverable amount.

## Estimating the recoverable amount

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- 12.9. When, following an assessment, there is any indication that an asset should be written down, the recoverable amount of that asset must be estimated. The recoverable amount of an asset is the higher of the amounts that can be obtained from selling the asset (i.e. net realisable value) or continuing to use the asset within the charity (value in use). However, the assets of a charity may be subject to restrictions as to their use or disposal and assets may also be held to deliver services to beneficiaries rather than to generate a cash flow.
- 12.10. A restriction may be imposed by the donor or created by the terms of an appeal used to fund the purchase of an asset. While a restriction will affect how the charity uses an asset, it is unlikely that a restriction imposed by charity law on the use of an asset would be passed on to a purchaser of that asset. Therefore, a restriction on use of an asset imposed by charity law would not normally reduce the amount obtainable on the sale of that asset.

## *Accounting and reporting by charities*

- 12.11. Occasionally, the terms of a gift will require the on-going use of a specified asset by the charity which would prevent its sale. In such instances, there may be costs involved in removing the restriction before the asset can be sold. The additional cost of removing a restriction should be reflected in the estimate of the asset's net realisable value.
- 12.12. The method used to determine the 'value in use' of an asset held by a charity will depend on whether the asset is primarily held to generate cash as a commercial return or for its service potential to the charity's beneficiaries.
- 12.13. An asset is held to generate a commercial return when it is used to generate a positive cash flow and earn a return that reflects the risks involved in holding the asset. When an asset is held to generate cash flows, its value in use will be the present value of the future cash flows expected to be derived from the asset including any cash flow resulting from its ultimate disposal.
- 12.14. The calculation of an asset's present value involves estimating the amount of the net cash flow that will be generated from the asset's use and then applying a discount rate to establish the present value of those future cash flows. Charities using the FRSSE may use the market rate for relevant UK government bonds if the anticipated cash flow has been adjusted for uncertainty as to the asset's ability to generate cash in the future.
- 12.15. However, charities often hold assets primarily to provide services to their beneficiaries rather than for generating cash flows. A charity may provide its services freely or at below commercial rates. Where an asset is primarily held for its service potential to beneficiaries, it would be inappropriate to measure value in use by reference to its cash flow. In such circumstances, it is more appropriate to regard value in use as the present value of the asset's service potential rather than the present value of its cash flow.
- 12.16. The method used to value an asset's service potential should be reliable, relevant to the asset and capable of measurement. This SORP considers that depreciated replacement cost is one method that may be used to provide a measure of an asset's service potential. The replacement cost of an asset is the most economical cost that would be incurred in replacing the asset's service potential. This cost is then depreciated to reflect the remaining economic life of the asset in its used condition.
- 12.17. Value in use measured on the basis of an asset's service potential will have particular relevance for specialist assets used by a charity. The net realisable value of a specialist asset may not reflect the cost that a charity avoids by using that asset in providing services. For example, the net realisable value of a specialist building may be less than its recent construction cost. However, provided the building continues to meet its intended service potential then its value in use would be better reflected by its replacement cost (its construction cost) rather than the amount for which it could be sold in the market.

## Accounting for write-downs and reversals

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- 12.18. If, and only if, the recoverable amount of an asset is less than its carrying amount, a charity must reduce the carrying amount of the asset to its recoverable amount. This write-down (and any reversals) to the recoverable amount must be charged (or credited) to the relevant heading(s) to which the asset's use is charged in the statement of financial activities (SoFA). However, where tangible fixed assets or investments are carried at revalued amounts, any write-down that reverse previous revaluation gains must instead be recognised within the other recognised gains and losses section of the SoFA provided that the carrying amount of the revalued asset remains greater than its depreciated historical cost.
- 12.19. If there is an indication that an asset should be written down, this may also indicate the need to review the asset's remaining useful life, the depreciation method or its residual value and to adjust these as necessary even if no loss is recognised for writing down the asset.
- 12.20. On occasions, the recoverable amount of a tangible fixed asset may subsequently increase as a result of a change in economic conditions or in the expected use of the asset. In these circumstances, the carrying amount of the asset must be written back to the lower of the recoverable amount or the amount at which the asset would have been recorded had the original write-down not been made. This reversal must be recognised under the appropriate expenditure heading(s) in the SoFA as a reduction in expenditure.
- 12.21. If the recoverable amount of an intangible asset or capitalised goodwill subsequently increases, the write-down must only be reversed if an external event caused the original write-down and subsequent external events clearly and demonstrably reverse the effects of that event in a way that was not foreseen when the original write-down was calculated.

## Disclosures to be made in the notes to the accounts

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- 12.22 This SORP requires that the amount of any write-down (and any reversals) of fixed assets or goodwill during the period must be disclosed in a note to the accounts.

## 13. Post balance sheet events

### Introduction

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- 13.1. This module sets out the accounting treatment of events occurring after the balance sheet date and applies to all charities. The accounting requirements of the FRSSE for post balance sheet events are set out in section 14 of that standard.
- 13.2. Once the accounts have been prepared, there is often a period of time before the trustees formally approve them. When preparing the accounts, charities make estimates or judgements based on the information available at the time, so they are required to assess the effect of events occurring between the end of the reporting period and the approval of the accounts to see whether adjustments to amounts or disclosures are necessary.
- 13.3. Events occurring after the end of the reporting period fall into two categories: adjusting events and non-adjusting events.

### Adjusting events occurring after the end of the balance sheet date

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- 13.4. Adjusting events are those events occurring after the balance sheet date but before the accounts are authorised for issue which provide evidence of conditions existing at the balance sheet date which affect items in the balance sheet. Charities must review and amend the amounts recognised in the accounts and any related disclosures in the notes to the accounts to reflect adjusting events.
- 13.5. Examples of events occurring after the balance sheet date that require adjustment include:
- settlement of a court case that confirms that the charity had a liability at the end of the reporting period and not a contingent liability;
  - notification that the payment of a legacy from an estate is no longer probable as a result of the will being contested;
  - the determination of the amount of a Gift Aid payment to a parent charity by a subsidiary undertaking, when the subsidiary had a present legal (for example, a deed) or constructive obligation to make the payment at the balance sheet date;
  - information allowing a more reliable estimate of an amount designated (however, designation of funds for a new purpose after the reporting date is not an adjusting event);
  - identification of a fraud, misstatement or error which has a material effect on an item in the accounts;
  - new information concerning an impairment of an asset, for example doubts over the authenticity of a heritage asset or a bad debt; or
  - new information that indicates that the charity may not be a going concern.

13.6. If there is uncertainty about the charity being a going concern, this must be disclosed (see the SORP module '[Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors](#)'). If the charity is no longer a going concern, the accounts must be restated on an appropriate basis.

### [Non-adjusting events occurring after the end of the reporting period](#)

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13.7. Non-adjusting events are those events occurring after the balance sheet date but before the accounts are authorised for issue which relate to conditions that arose after the end of the reporting period. The disclosure of non-adjusting events provides useful and relevant information about the charity to users of the accounts. Examples of non-adjusting events that may occur after the reporting date that should be disclosed include:

- a decision that the charity is going to merge with another charity;
- the opening of a new branch in a new locality or a material expansion of the range or scale of activities undertaken;
- the purchase of a new building to expand a charity's capacity to further its purposes;
- the announcement or implementation of a major restructuring;
- the announcement of a new fundraising appeal or the degree of success achieved by a fundraising appeal;
- a material loss of assets or diminution in the value (impairment) of assets subsequent to the reporting date, for example due to fire or flood;
- a material decline in the market value of investments;
- the commencement of major litigation; or
- the entering into significant commitments or the identification of material contingent liabilities or the giving of material guarantees.

### [Disclosure in the accounts for non-adjusting events after the end of the reporting period](#)

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13.8. The FRSSE requires that for each material category of non-adjusting event, the notes to the accounts must provide details of the nature of the event and an estimate of its financial effect or a statement that such an estimate cannot be made.

## 14. Cash flow statement

### Introduction

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- 14.1. Charities preparing their accounts under the FRSSE and this SORP are encouraged, but not required, to prepare a cash flow statement. If a charity chooses to prepare a cash flow statement, it should refer to the guidance set out in Section D: Voluntary Disclosures and Appendix III of the FRSSE.
- 14.2. The cash flow statement provides information about the ways in which a charity uses the cash generated by its activities and about changes in cash held by a charity. It also provides information that is helpful in assessing a charity's liquidity and underlying solvency. 'Liquidity' refers to the ability to meet its immediate and short-term obligations as they fall due. 'Solvency' refers to the ability of a charity to meet its longer-term obligations as they fall due.
- 14.3. The statement identifies a charity's cash flows and the net increase or decrease in cash in the financial year. For charities using the FRSSE, cash is normally regarded as cash 'at bank and in hand' less overdrafts repayable on demand which should be reconciled to the balance sheet amounts.
- 14.4. This module sets out:
- structure of the cash flow statement;
  - methods of compiling the cash flow statement; and
  - template for a cash flow statement.

### Structure of the cash flow statement

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- 14.5. The format of the cash flow statement when prepared under the FRSSE should identify cash generated from a charity's activities, cash from other sources and the application of cash and reconcile the net increase or decrease in cash to the balance sheet amounts at the end of the financial year.
- 14.6. An example of how a cash flow statement may be presented is provided in Table 7, which may be adapted as necessary for the reporting purposes of the charity. For example, a columnar presentation may be adopted to distinguish between cash flows relating to restricted funds and cash flows relating to unrestricted funds. When a charity is preparing consolidated accounts, a cash flow statement must, if prepared, be on a consolidated basis.

### Methods of compiling the cash flow statement

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- 14.7. The FRSSE encourages, but does not require, the use of the indirect method when presenting cash flow information. The indirect method is the method most commonly used and is the method illustrated in Table 7.

14.8. The indirect method involves identifying the cash flows from operating activities which is normally the net income/(expenditure) shown in the statement of financial activities (SoFA) which is adjusted for:

- non-cash movements in the SoFA; and
- any deferrals or accruals arising from cash receipts or payments.

### Template for a cash flow statement

14.9. A template for a cash flow statement using the indirect method is given in Table 7. Charities using this format must provide a reconciliation to show how the net movement in funds presented in the SoFA has been adjusted to arrive at the cash flows from operating activities presented in the cash flow statement. An example of how this reconciliation may be set out is given in Table 8. A reconciliation of cash should also be provided and an example is given in Table 9.

14.10. The template for the cash flow statement set out in Table 7 must be adapted as necessary for any additional items that apply. An example would be cash flows arising from the payment of taxes. Similarly, any headings that do not apply must be omitted.

**Table 7: Cash flow statement**

	Total funds	Prior year funds	Note
	£	£	
<b>Cash generated from operating activities:</b>			
<b>Net cash provided by (used in) operating activities</b>	X	(X)	Table 8
<b>Cash flows from other sources:</b>			
Dividends, interest and rents from investments	X	X	
Proceeds from the sale of property, plant and equipment	X	X	
Cash inflows from new borrowing	X	-	
Proceeds from sale of investments	X	-	
Receipt of endowment	X	-	
	X	X	
<b>Application of cash:</b>			
Purchase of property, plant and equipment	(X)	(X)	
Purchase of investments	(X)	(X)	
Repayments of borrowing	(X)	(X)	
	(X)	(X)	
<b>Net increase/(decrease) in cash:</b>	X	(X)	
Cash at bank and in hand less overdrafts at the beginning of the year	X	X	Table 9
<b>Cash at bank and in hand less overdrafts at end year</b>	X	X	Table 9

**Table 8: Reconciliation of net income/(expenditure) to net cash flow from operating activities**

	Current Year	Prior Year
	£	£
<b>Net income/ (expenditure) (as per the statement of financial activities)</b>	<b>X</b>	<b>(X)</b>
<b>Adjustments for:</b>		
Depreciation charges	X	X
Dividends, interest and rents from investments	(X)	(X)
Loss/(profit) on the sale of fixed assets	X	(X)
(Increase)/decrease in stocks	(X)	X
(Increase)/decrease in debtors	(X)	X
Increase/(decrease) in creditors	X	(X)
<b>Net cash provided by (used in) operating activities</b>	<b>X</b>	<b>(X)</b>

**Table 9: Analysis of cash at bank and in hand less overdrafts**

	Current Year	Prior Year
	£	£
Cash at bank and in hand	X	X
Overdrafts included in bank loans and overdrafts falling due within one year	(X)	(X)
	<b>X</b>	<b>X</b>



## Selection 1: Special transactions relating to charity operations

### 15. Charities established under company law

#### Introduction

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- 15.1. Charities registered as companies under company law (charitable companies) must comply with the reporting requirements of company law. Charitable companies reporting under UK company law should refer to the FRSSE which identifies company specific presentational and disclosures requirements in bold print. However, charitable companies must adapt the presentation and headings used in the FRSSE for the special nature of the company and its activities. Charities established as public guarantee companies in the Republic of Ireland are not permitted to follow the FRSSE.
- 15.2. In jurisdictions where adherence to this SORP is not a legal requirement, there is a strong presumption that charitable companies will comply with this SORP in order for their accounts to give a true and fair view as required by company law.
- 15.3. Charitable companies using this SORP must adapt their statement of financial activities (SoFA) to meet the requirements of company law or prepare a separate summary income and expenditure account.
- 15.4. This module, which applies to all charitable companies using the FRSSE, explains how the following requirements of company law must be met by companies when applying this SORP:
  - preparation of the directors' report;
  - requirement for an income and expenditure account;
  - preparation of a combined SoFA and income and expenditure account;
  - summary income and expenditure account;
  - additional considerations that apply when consolidated (group) accounts are prepared under company law;
  - disclosure of equity on the balance sheet; and
  - disclosure of revaluation reserves (UK only).

#### Preparation of the directors' report

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- 15.5. Company law in the UK requires certain information to be provided in the directors' report in addition to the information that this SORP requires to be included in the trustees' annual report.
- 15.6. A combined directors' report and trustees' annual report can be prepared provided it includes all the information required by the SORP module '**Trustees' annual report**' and applicable charity law. Charitable companies should ensure that the combined annual report makes it clear that it also contains a directors' report as required by company law.

## The requirement for an income and expenditure account

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- 15.7. Company law sets out the form and content requirements for the accounts. These detailed requirements are set out in the Companies Act 2006 and in Regulations made under that Act. Charities established as companies in the UK must refer to the FRSSE and Regulations to ensure the disclosure requirements of company law are met.
- 15.8. Not-for-profit companies reporting in the UK under the Companies Act 2006 must prepare an income and expenditure account as part of their accounts. The SoFA can often be adapted to include an income and expenditure account and therefore the presentation of a separate income and expenditure account may not be required.

## Preparation of a combined statement of financial activities and income and expenditure account

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- 15.9. To ensure that the SoFA meets the requirements of company law for an income and expenditure account, a combined statement must:
- identify, within the statement's heading, that an income and expenditure account is included;
  - include a line identifying the amount of any tax on activities; and
  - identify, as a prominent sub-total in the statement, the charity's net income/ expenditure for the reporting period.
- 15.10. If a combined statement is not presented, then the charitable company must produce a separate summary income and expenditure account as part of its accounts.

## Summary income and expenditure account

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- 15.11. The amounts presented in a summary income and expenditure account must be derived from the corresponding figures in the SoFA but exclude any endowment funds. The reporting of income and expenditure need not distinguish between unrestricted and restricted income funds.
- 15.12. In the UK, a company must adapt the headings and sub-headings used in the income and expenditure account to reflect the special nature of its activities. The example given in Table 10 is illustrative.

**Table 10: Minimum requirements for a summary income and expenditure account**  
**Summary income and expenditure account for (named) company year ending**  
**(day/month/year)**

	Note	All income funds (current year)	All income funds (previous year)
		£	£
Income*			
Realised gains/(losses) on investments		x	x
Interest and investment income**		x	x
<b>Gross income in the reporting period</b>		X	X
Expenditure*			
Interest payable**		x	x
Depreciation and charges for impairment of fixed assets**		x	x
<b>Total expenditure in the reporting period</b>		(X)	(X)
Net income (expenditure) before tax for the reporting period		X	X
Tax payable		(X)	(X)
<b>Net income (expenditure) for the financial year</b>		X	X

\* Income and expenditure may be analysed in further detail using the analysis headings of the SoFA.

\*\* Items marked may either be shown as separate line items as above or included within other line items and disclosed separately in a note to the accounts.

### Additional considerations that apply when consolidated (group) accounts are prepared under company law

15.13. A charity in the UK that is the parent company of small group may voluntarily prepare consolidated accounts (also known as group accounts) under section 398 of the Companies Act 2006. However, consolidated accounts are required by charity law in England and Wales and Scotland when the aggregate income of the group after any consolidation adjustments exceeds £500,000 in the financial year.

15.14. Charitable companies which prepare consolidated accounts must prepare a summary consolidated income and expenditure account for the charity and its subsidiaries (the group) if the consolidated SoFA cannot be adapted to meet the requirements for an income and expenditure account.

## Disclosure of equity on the balance sheet

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- 15.15. Charitable companies are usually established as companies limited by guarantee. However, in rare cases, charitable companies may have issued share capital provided those shares have no right to receive a dividend or other distribution attached to them. Charitable companies that have issued share capital must modify the 'Funds of the charity' heading of the balance sheet to disclose called up share capital. Charitable companies with share capital must provide details of their share capital as set out in section 12.9 of the FRSSE.

## Disclosure of revaluation reserves (UK only)

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- 15.16. Regulations made under the UK Companies Act 2006 require a revaluation reserve to be set up when assets are revalued upwards. A revaluation reserve represents the difference between the cost or valuation of an asset when first recognised, less any depreciation and its subsequent revalued amount.
- 15.17. Although the separate reporting of a revaluation reserve has less significance for charities, as unlike commercial entities they do not distribute profits, the amount of any revaluation reserve must still be disclosed by charitable companies.
- 15.18. To comply with the regulations made under the Companies Act 2006, charitable companies must disclose any revaluation reserves on the face of the balance sheet. These reserves will form part of the funds in which the revalued assets are held. This can be presented by showing these reserves as a separate component of the relevant class of fund.

## 16. Presentation and disclosure of grant-making activities

### Introduction

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- 16.1. This module sets out the SORP's requirements for the disclosure of grant-making activities that apply to all charities where grant-making is a material component of their charitable activities. The disclosure of grant-making activities is not addressed by the FRSSE. Charities adopting this SORP are required to make the disclosures set out in this module for their grant-making activities.
- 16.2. For the purposes of this module, a grant is a voluntary payment made by a charity to further the purposes of the grant-making charity to either a person or an institution. Grant payments may be made to fund the general purposes of, or for a specific purpose of, the recipient, for example funding a particular activity or service.
- 16.3. A grant payment may be unconditional, or subject to conditions which must be met before the recipient is entitled to the payment. Refer to the SORP module '[Recognition of expenditure](#)', for the basis on which any liability for grant commitments and obligations are recognised in a charity's accounts.
- 16.4. This module sets out for all charities:
- [how charities must present grant-making activities in their accounts](#);
  - [how to present grant-making and support costs](#);
  - [accounting for activities partly undertaken through grant-making](#);
  - [the treatment of grants to individuals](#);
  - [the disclosure of grant-making activities in the notes to the accounts](#);
  - [the exemptions to disclosure](#);
  - [information required in cases of serious prejudice](#); and
  - [the statutory exemption applicable in England and Wales](#).

### How charities must present grant-making activities in their accounts

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- 16.5. Grants made by a charity must be included under the heading of 'expenditure on charitable activities' in the statement of financial activities (SoFA).
- 16.6. The information provided in the notes to the accounts should help the user to understand how grants made by a charity relate to its purposes and the policies adopted by the trustees in pursuing them.
- 16.7. The SORP module '[Trustees' annual report](#)' provides further details of the narrative reporting of the grant-making activities and policies that must be provided in the trustees' annual report.

16.8. The notes to the accounts should provide the user of the accounts with an understanding of the activities or projects that are being funded and whether the financial support is provided directly to individuals or to assist an institution to undertake activities or projects. In the case of institutional grants, information as to the recipient(s) of the funding must be provided so that the user can appreciate the type and range of institutions supported. This information must be disclosed in the notes for the accounts or the trustees' annual report unless the charity is eligible to (and chooses to) take advantage of certain exemptions to disclosure, or the charity has elected to provide this information via a link to the charity's webpage.

### How to present grant-making and support costs

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16.9. When reporting on the cost of grant-making activities, charities preparing their SoFA on an activity basis must include related support costs. Support costs related to grant-making activities will include:

- costs incurred as part of the grant application and decision making processes prior to the award of a grant;
- monitoring costs incurred following the award of a grant; and
- support costs incurred relating to grant-making activities (refer to the SORP module '[Allocating costs by activity in the statement of financial activities](#)' for guidance on the allocation of support costs to activities).

### Accounting for activities partly undertaken through grant-making

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16.10. Charities may carry out their activities through a combination of direct service provision and grants to third party institutions. In such cases, the total cost of the activity is the combined expenditure incurred directly by the charity and the funding provided to third party individuals or institutions through its grant-making activities.

### The treatment of grants to individuals

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16.11. A grant to an individual is one that is made for the direct benefit of the individual who receives it, for example to relieve financial hardship or as an educational bursary. Charities are not required to name the recipients of individual grants (except where the recipient is a related party).

16.12. All other grants should be regarded as institutional. For example, a grant which is made to an individual to carry out a research project should be regarded as a grant to the institution to which the individual is connected rather than as a grant to the individual undertaking the research.

## The disclosure of grant-making activities in the notes to the accounts

16.13. This SORP requires that the notes to the accounts must provide the following details which reconcile with the total of grants payable:

- the total amount of grants paid analysed between grants to individuals and grants to institutions;
- an analysis of the total amount of grants paid by nature or type of activity or project being supported; and
- the amount of support costs allocated to grant-making activities.

16.14. This analysis of grants should provide the user of the accounts with an understanding of the nature of the activities or projects being funded by the grant-maker.

16.15. For example, in the case of activity funded exclusively through grant-making, this analysis may be set out as shown in Table 11.

**Table 11: Analysis of grants**

Analysis	Grants to institutions	Grants to individuals	Support cost	Total
	£	£	£	£
Activity or Project 1				
Activity or Project 2				
Activity or Project 3				
<b>Total</b>				

16.16. The analysis should relate to the grant-making charity's purposes. In the case of a general grant-maker, its grants may be analysed under project or activity headings such as social welfare, medical research, the performing arts, welfare of people in financial need, or help to people seeking to further their education. Alternatively, the analysis may be based on projects or programmes undertaken or by type of activity or geographical location of the project being funded.

16.17. Charities that make grants to institutions must also disclose details of a sufficient number of these institutional grants so that the user of the accounts can develop an understanding of the range of institutions the charity has supported. This disclosure must include all grants made to each institution when these are material in the context of the charity's total charitable expenditure. This information must be provided in the notes to the accounts, or by providing details of the charity's webpage URL at which this information can be accessed, or this information may be set out within the trustees' annual report.

## Accounting and reporting by charities

16.18. This analysis, whether provided as a note to the accounts or made available on the charity's website or included within the trustees' annual report, must provide:

- the name of the institution(s) in receipt of material grants;
- the total value of grants made to each institution in receipt of material grants in the reporting period; and
- a reconciliation of the amount of material institutional grants disclosed to the total amount of institutional grants made in the reporting period.

16.19. Charities that provide a number of different grants to a single institution to undertake different activities or projects must disclose the total value of the grants to that institution. For example, a charity may have made grants to different officers or departments of a particular university for different projects. Such grants must be treated as made to the same institution.

16.20. When activities are carried out through a combination of direct service or programme activity and grant funding of third parties, the notes to the accounts must differentiate between activities undertaken directly by the charity and grant funded activities. The disclosures required may be presented in a format such as that shown in Table 12.

**Table 12: Analysis of charitable activities**

Activity or programme	Activities undertaken directly	Grant funding of activities	Support costs	Total
	£	£	£	£
Activity 1				
Activity 2				
Activity 3				
<b>Total</b>				

## Exemptions to disclosure

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16.21. Information provided in relation to grant-making need not be disclosed where:

- grants are made to individuals – in which case details of the recipient are not required (except those grants made to related parties);
- the grant-making activities in total are not material in the context of a charity's overall charitable activities – in which case no disclosures are required;
- total grants to a particular institution are not material in the context of institutional grants – in which case the name of the recipient institution need not be disclosed; or
- disclosure could result in serious prejudice to the grant-maker and/or the recipient institution or individual working for the recipient institution.

16.22. In exceptional cases, it is possible that the disclosure of the details of one or more of those grants could seriously prejudice the furtherance of the purposes either of the recipient institution or of the charity itself. Situations where serious prejudice is clearly indicated include those where disclosure could result in serious personal injury.



## Information required in cases of serious prejudice

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16.23. This SORP requires that where the circumstances amount to serious prejudice, a charity may withhold details of the recipient of any institutional grant but must, in such circumstances, state as part of its disclosure of material grants made to institutions:

- the total number, value and general purpose of those grants where these details have not been disclosed; and
- that an exemption applies to disclosure on the grounds of serious prejudice.

16.24. It is very unlikely that all the material institutional grants of a charity would fall within this exemption.

## The statutory exemption applicable in England and Wales

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16.25. Charity law provides an exemption to charitable trusts registered in England and Wales from providing the names of grant recipients and the amounts of such grants during the lifetime of the settlor who donated the funds from which the grants are paid or during the lifetime of any spouse or civil partner of the settlor. A charitable trust that opts to use this disclosure exemption is required by this SORP to state that this exemption has been taken in the notes to the accounts. This disclosure exemption does not apply to charities registered in Scotland, Northern Ireland or the Republic of Ireland.

## 17. Retirement benefits

### Introduction

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- 17.1. This module applies to all charities using the FRSSE that have defined benefit or defined contribution pension schemes that provide benefits to their staff after they have left the employment of the charity. The accounting requirements and disclosures in the notes to the accounts for pension or other retirement benefits arrangements depend on whether the scheme is classified as a defined contribution scheme or defined benefit scheme.
- 17.2. Charities reporting under the FRSSE should refer to section 10 and Appendix II of the FRSSE for more information.
- 17.3. This module sets out:
- accounting for defined contribution schemes;
  - accounting for defined benefit schemes;
  - fund accounting for defined benefit schemes;
  - fund accounting and the treatment of a defined benefit scheme surplus or deficit;
  - accounting for multi-employer defined benefit schemes;
  - disclosures in the accounts relating to schemes accounted for as defined contribution schemes; and
  - disclosures in the accounts relating to defined benefit schemes.

### Accounting for defined contribution schemes

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- 17.4. Defined contribution schemes are pension or other retirement schemes into which the employer pays regular fixed contributions as an amount or as a percentage of pay. The employer will have no legal or constructive obligation to pay further contributions if the scheme does not have sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.
- 17.5. The cost of the scheme charged to the SoFA is equal to the contributions payable in the reporting period. Any liability and expenses should be allocated to unrestricted funds and restricted funds on the same basis as other employee-related costs unless the terms of a restriction prohibit the allocation of such costs to a restricted fund.

### Accounting for defined benefit schemes

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- 17.6. A defined benefit scheme is a pension or other retirement benefit scheme whose rules define the benefit independently of the contributions payable, and the benefits are not directly related to the investments of the scheme. A feature of defined benefit schemes is that the employer has offered a guarantee to fund the amount or level of pension or benefit ultimately payable and is therefore liable to make additional contributions to provide that guaranteed level of benefit.

- 17.7. Charities reporting under the FRSSE must refer to Appendix II of the FRSSE for the methodology to be followed in calculating the scheme's assets and liabilities and how the components of the change in the defined benefit asset or liability are charged to the statement of financial activities (SoFA).

### Fund accounting for defined benefit schemes

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- 17.8. The component costs of the defined benefit scheme must be allocated between the expenditure categories in the SoFA on a fair and reasonable basis. The allocations are made on the basis of the charity's own computations. The basis of the allocations should be consistent from year to year. One approach is to allocate the components of the defined benefit scheme based on the staff costs of employees within the scheme, although other approaches (for example, allocation based on pension contributions payable) may also produce an equitable allocation.
- 17.9. In cases where a restricted fund may be of a short-term nature or staff may be frequently transferred between activities funded from restricted funds, there may be uncertainty as to the fund which will ultimately recover any surplus or meet future contributions resulting from any deficit. In these circumstances, only an appropriate portion of the current service cost component of the pension cost relating to the staff engaged in activities funded from restricted funds should be charged to the restricted funds.
- 17.10. Past service costs and gains and losses on curtailments and settlements should be charged to restricted funds only when a charity can demonstrate that the costs relate to staff presently engaged in the activities funded by the restricted funds.

### Fund accounting and the treatment of a defined benefit scheme surplus or deficit

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- 17.11. A surplus in a defined benefit scheme is the excess of the value of the assets in the scheme over the present value of the scheme's liabilities. A deficit in a defined benefit scheme is the shortfall in the value of the assets in the scheme below the present value of the scheme's liabilities.
- 17.12. A surplus in a defined benefit scheme is the excess of the value of the assets in the scheme over the present value of the scheme's liabilities. A charity, as employer, must recognise an asset to the extent that it is able to recover a surplus either through reduced contributions in the future or through refunds from the scheme.
- 17.13. A deficit in a defined benefit scheme is the shortfall in the value of the assets in the scheme below the present value of the scheme's liabilities. A charity, as employer, must recognise a liability to the extent it reflects its legal or constructive obligation.
- 17.14. Charities must recognise the actuarial gain or loss arising in the reporting period in the 'other recognised gains and losses' heading in the SoFA under a separate sub-heading, 'actuarial gains or losses on defined benefit pension schemes'.

- 17.15. Where a surplus or deficit in a defined benefit scheme gives rise to an asset or liability, the asset or liability must be shown on the balance sheet within the unrestricted funds of the charity, except where staff are specifically engaged on a long-term project funded from restricted funds and it is demonstrable that all or part of the asset or liability is properly attributable to those restricted funds.
- 17.16. It may be necessary for the charity to liaise with the provider of a particular restricted fund in order to establish the basis on which any pension asset or liability is allocated to that fund and the pension costs that may be properly charged to it. Charities allocating a pension asset or a liability to a restricted fund should review the basis of the allocation annually to assess whether the benefit or obligation continues to accrue to that fund.
- 17.17. Where staff changes or the cessation of a particular project indicate that the economic benefits or obligations will no longer accrue to a particular restricted fund, then the asset or liability should be allocated to the unrestricted funds by means of a transfer in the SoFA.

### Accounting for multi-employer defined benefit schemes

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- 17.18. This SORP requires that charities participating in a multi-employer defined benefit pension scheme and that do not have an existing accounting policy for the scheme that conforms with accepted practice should refer to paragraphs 28.11, 28.11A and 28.40A of FRS 102 to establish current practice. Charities, in order to conform with accepted practice, must account for a multi-employer scheme as a defined benefit scheme unless insufficient information is available so to do. In such circumstances, charities participating in a multi-employer defined benefit scheme must account for contributions to the scheme as if they were made to a defined contribution scheme.
- 17.19. Where a charity accounts for a multi-employer defined benefit scheme as though it were a defined contribution scheme, it may retain its existing accounting policy when accounting for an agreement to make contributions to fund a deficit in the scheme provided that policy reflects accepted practice. Again, if the charity does not have an existing accounting policy for such agreements it should refer to paragraph 28.11A of FRS 102 when developing its accounting policy. When an expense is recognised for the contributions payable, it should be allocated, where practicable, to the activities in the SoFA to which the past service cost relates and disclosed separately if it is material (refer to the SORP module '[Statement of financial activities](#)').

### Disclosures in the accounts relating to schemes accounted for as defined contribution schemes

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- 17.20. The FRSSE requires that a charity must make the following disclosures in respect of a defined contribution scheme:
- the nature of the scheme (i.e. defined contributions);
  - the costs for the period; and
  - any outstanding or prepaid contributions at the balance sheet date.

## Disclosures in the accounts relating to defined benefit schemes

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17.21. The FRSSE requires that a charity must make the following disclosures in respect of a defined benefit scheme:

- the nature of the scheme (i.e. defined benefit);
- the date of the most recent full actuarial valuation on which the amounts in the accounts are based and if the actuary is an employee or officer of the reporting charity, or of the group of which it is a member, this fact should also be disclosed;
- the contribution made in respect of the reporting period and any agreed contribution rates for future years; and
- for closed schemes and those in which the age profile of the active membership is rising significantly, the fact that under the projected unit method the current service cost will increase as the members of the scheme approach retirement.

17.22. The FRSSE (Appendix II) also requires the fair value of the scheme assets, the present value of the scheme liabilities based on the accounting assumptions and the resulting surplus or deficit must be disclosed in a note to the accounts. Where the asset or liability in the balance sheet differs from the surplus or deficit in the scheme, an explanation of the difference should be given. An analysis of the movements during the period in the surplus or deficit in the scheme should be given.

17.23. If a charity treats a defined benefit multi-employer scheme as a defined contribution scheme because sufficient information is not available to use defined benefit accounting, a charity reporting under this SORP must also ensure there is adequate disclosure of financial implications of the scheme to the charity. In particular, this SORP requires that a charity must disclose:

- the fact that it is a defined benefit plan and the reason why it is being accounted for as a defined contribution plan, along with any available information about the scheme's surplus or deficit and the implications, if any, for the charity; and
- how any liability recognised in the accounts arising from an agreement with a multi-employer scheme to fund a deficit has been determined.

## Selection 2: Accounting for special types of assets held

### 18. Accounting for heritage assets

#### Introduction

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- 18.1. The FRSSE does not contain any requirements for heritage assets. A charity applying the FRSSE that holds heritage assets may continue to use its existing accounting policies for such assets provided those policies reflect accepted practice and relevant disclosures are made. This module reflects current practice which charities adopting this SORP must follow if they do not have an existing policy for heritage assets or whose existing policy does not reflect accepted practice. All charities holding heritage assets that are material in the context of their accounts are encouraged to adopt current practice as set out in this module.
- 18.2. Charities adopting current practice should also refer to section 34 of FRS 102.
- 18.3. This module sets out the accounting treatment of heritage assets which must be followed when charities adopt current accounting practice for heritage assets:
- definition of a heritage asset;
  - recognition and measurement of heritage assets on the balance sheet;
  - how to measure heritage assets that have been purchased;
  - how to measure heritage assets that have been donated;
  - depreciation and impairment of heritage assets;
  - accounting treatment for heritage assets recognised on the balance sheet;
  - disclosures required for all charities holding heritage assets;
  - disclosure of heritage assets recognised on the balance sheet;
  - disclosure of heritage assets not recognised on the balance sheet; and
  - disclosure of a five-year summary of transactions.

#### Definition of a heritage asset

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- 18.4. 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.
- 18.5. An asset may have the attributes of a heritage asset, for example it may 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.

## *Accounting and reporting by charities*

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

- A historic building used by an educational establishment for teaching would not be accounted for as a heritage asset because it is held to provide a facility for teaching rather than the building itself contributing to knowledge and culture.
- In the case of a museum or gallery, it is the collections held and not the buildings or display cases that house them that will be treated as heritage assets unless the structures themselves also have the attributes of a heritage asset and are held principally for their contribution to knowledge and culture.
- Works of art or historic buildings principally held for investment purposes are categorised as investments, as they are held for investment gain or for income generation rather than for their contribution to knowledge and culture.

18.7. Similarly, a requirement to hold and maintain an asset, for example as an endowment, does not mean that asset is held for its contribution to knowledge and culture. For example:

- An inalienable building or painting, which must be retained indefinitely by a charity due to the terms of a gift, is not a heritage asset unless it meets the definition of a heritage asset.

18.8. However, a heritage asset used incidentally for operational purposes unconnected with the promotion of knowledge and culture may still fall within the definition of a heritage asset. For example:

- A historic building incidentally used for service or administrative activities by a charity but principally held and maintained for its contribution to knowledge and culture is accounted for as a heritage asset.

18.9. Although a heritage asset is normally tangible, it is possible for it to be intangible.

For example:

- A library of digital recordings or film rights can be a heritage asset if it is held for its contribution to knowledge and culture.

18.10. Heritage assets may include abbeys, monasteries, cathedrals and historic churches and monuments where a contribution to knowledge and culture is ancillary to faith or other purposes.

18.11. Similarly, the artefacts contained within, or associated with, such assets may also be heritage assets. For example, associated artefacts could include religious artefacts contained within a cathedral or historic church.

- 18.12. 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.

### Recognition and measurement of heritage assets on the balance sheet

- 18.13. Heritage assets must be recognised as an asset on a charity's balance sheet separately from other assets where practicable. Heritage assets are reported as a separate class of tangible fixed asset on the balance sheet and should be measured initially at either their cost or valuation if donated.
- 18.14. Heritage assets initially recognised at cost may continue to be carried at historical cost subject to any depreciation or impairment, or charities may choose to adopt a policy of valuation.
- 18.15. 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. Where reliable information on cost or value is not available, charities will need to consider if the cost of obtaining a valuation is justified by the usefulness of the information to the users of the accounts and to the charity for its own stewardship purposes.
- 18.16. Charities may adopt any reliable valuation technique to estimate the fair value of a heritage asset. For example, for some heritage buildings, the use of market value may provide a reasonable approach; in other cases, the use of depreciated replacement cost may be appropriate. However, depreciated replacement cost may not be an appropriate method where a building cannot be replicated using modern building methods or where the value of the original asset lies in its unique historic or heritage qualities. If a valuation method is adopted, it must be applied to all assets within a particular class or to a group of similar assets.

### How to measure heritage assets that have been purchased

- 18.17. When a heritage asset is purchased, its cost of acquisition will be known and therefore the asset must be recognised initially at this amount. Should the acquisition be by way of an exchange of assets, the cost of acquisition is represented by the carrying amount of the asset exchanged and any cash settlement made or payable at the date the charity assumed legal title or control of the acquired asset. A heritage asset that is recognised initially at its cost may be subsequently carried at a valuation where a charity adopts a policy of carrying its heritage assets (or group of heritage assets) at valuation. There is no prescribed minimum period between valuations. However, if the valuation model is adopted, the carrying amount of the asset should be reviewed with sufficient frequency to ensure that the valuations remain current.



## How to measure heritage assets that have been donated

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- 18.18. Heritage assets donated to the charity should be recognised initially at their fair value where practicable. Fair value can often be estimated by reference to recent market transactions in identical assets or in assets that are substantially the same as the asset being measured. Fair value may be determined by the appraisal of market-based evidence by trustees or staff who have relevant skills, knowledge and experience or by a professionally qualified valuer. Where no market-based evidence exists, depreciated replacement cost may be used to estimate the fair value of certain properties held as heritage assets. If a reliable estimate cannot be made of the asset's fair value or the cost of valuation is likely to exceed the benefits provided by the information, the asset is not recognised in the accounts and the relevant note disclosures concerning the nature of asset and its accounting treatment should be provided.
- 18.19. Where a heritage asset has been acquired by way of donation or other form of non-exchange transaction, the initial valuation may be treated as its deemed cost removing the need for subsequent revaluations.

## Depreciation and impairment of heritage assets

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- 18.20. A heritage asset must be depreciated over its useful economic life. However, certain heritage assets may have indefinite lives and are therefore not depreciated. In either case, a heritage asset must be reviewed at the reporting date for impairment. Impairment may be due to physical deterioration, breakage, new evidence giving rise to doubts as to its authenticity, or other factors.

## Accounting treatment for heritage assets recognised on the balance sheet

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- 18.21. This SORP requires that when heritage assets are recognised in the balance sheet, a charity must:
- present heritage assets as a separate class of fixed asset in the balance sheet;
  - include the value placed on any heritage asset gifted to the charity in the 'income from donations' heading in the statement of financial activities (SoFA) and allocate that income to a restricted fund when the use of the asset is restricted;
  - recognise any change in the valuation of a heritage asset as a gain or loss on revaluation of fixed assets in the SoFA;
  - recognise any gain on the disposal of a heritage asset as other income in the SoFA; and
  - recognise any loss on disposal, depreciation or impairment of a heritage asset as a cost of charitable activities in the SoFA.

## Disclosures required for all charities holding heritage assets

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18.22. Charities holding heritage assets using the FRSSE may continue to use their existing accounting policies for the recognition, presentation and disclosure of heritage assets provided the policies reflect accepted practice. This SORP requires that charities retaining their existing accounting policies must disclose, as a minimum, their accounting policies for heritage assets and make sufficient disclosures to give users of the accounts a reasonable understanding for the nature and scale of the assets held and of any material additions and disposals in the reporting period. Charities are encouraged to adopt current practice by making the disclosures set out below in this module.

18.23. Charities adopting current practice should disclose the following for all heritage assets held:

- an indication of the nature and scale of heritage assets held;
- the policy for the acquisition, preservation, management and disposal of heritage assets (including a description of the records maintained by the charity of its collection of heritage assets and information on the extent to which access to the assets is permitted); and
- the accounting policies adopted for heritage assets, including details of the measurement bases used.

18.24. The above notes should be brief but sufficiently informative. Charities providing further information on these matters in the trustees' annual report should include a cross reference to the annual report in the notes.

18.25. The disclosures relating to heritage assets can be aggregated for groups or classes of heritage assets provided that this does not obscure significant information.

## Disclosure of heritage assets recognised on the balance sheet

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18.26. When heritage assets are recognised in the balance sheet, charities adopting current practice should disclose:

- the carrying amount of heritage assets by class or group both at the beginning of the reporting period and at the reporting date, distinguishing between classes or groups of heritage assets recognised at cost and those recognised at valuation at the reporting date; and
- where assets are recognised at valuation, sufficient information to assist in understanding the valuation being recognised (date of valuation, method used, whether carried out by external valuers and, if so, their qualifications, and any significant limitations on the valuation).

18.27. Charities may choose to present a reconciliation of the movements between the opening and closing carrying amount(s) in the balance sheet for heritage assets. This information may be presented in a tabular format (see Table 13).

**Table 13: Analysis of heritage assets**

Basis of capitalisation	At valuation Group A	At cost Group B	Total
	£	£	£
Carrying amount at beginning of the reporting period	X	X	X
Additions	X	X	X
Disposals	(X)	(X)	(X)
Depreciation/impairment	(X)	(X)	(X)
Revaluation	X	-	X
Carrying amount at reporting date	X	X	X

### Disclosure of heritage assets not recognised on the balance sheet

18.28. When heritage assets have not been recognised on the balance sheet, charities adopting current practice should:

- explain the reasons why;
- describe the significance and nature of those assets; and
- disclose information that is helpful in assessing the value of those assets.

18.29. In exceptional circumstances where it is not practicable to obtain a valuation of heritage assets acquired by donation, the reason why it is not practicable should be stated.

### Disclosure of a five-year summary of transactions

18.30. Charities adopting current practice should provide a summary of transactions relating to heritage assets for the reporting period and for each of the previous four reporting periods disclosing:

- the cost of acquisition of heritage assets;
- the value of heritage assets acquired by donation;
- the carrying amount of heritage assets disposed of in the period and the proceeds received; and
- any impairment recognised in the period.

18.31. The summary should show separately those transactions that are included in the balance sheet and those that are not. Charities that have been operating for fewer than five years should provide information for such prior periods as are available. The required information may be presented in a tabular format (see Table 14).

18.32. The disclosures required in the five-year summary need not be given for any reporting period earlier than the period immediately before 1 January 2015 if it is impractical to provide this information; a statement explaining why it is impractical should be provided.

18.33. Charities should note that the accounting disclosures required for heritage assets are similar to those of the withdrawn Financial Reporting Standard 30 'Heritage Assets' which was in effect from 1 April 2010. The information required to provide a summary of heritage asset transactions should therefore be available to those charities whose accounting disclosures previously reflected the requirements of that Standard.

**Table 14: Summary analysis of heritage asset transactions**

	2015	2014	2013	2012	2011
	£	£	£	£	£
Purchases					
Group A					
Group B					
Donations					
Group A					
Group B					
<b>Total additions</b>					
Charge for impairment					
Group A					
Group B					
<b>Total charge for impairment</b>					
Disposals					
Group A: carrying amount					
Group B: carrying amount					
<b>Total disposals</b>					
Proceeds from disposals					
Group A: sale proceeds					
Group B: sale proceeds					
<b>Total sale proceeds</b>					

## **19. Accounting for funds received as agent or as custodian trustee**

### **Introduction**

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- 19.1. This module applies to charities that administer the funds of another entity as its agent. Paragraphs 48 to 60 of Appendix III of the FRSSE provide guidance on the presentation of income as principle or as agent. This module also sets out the disclosure of agency arrangements and for charities that act as a custodian trustee required by this SORP.
- 19.2. As agent, a charity will act in line with the instructions of the entity that acts as the principal. For example, a charity may operate in an area of the world where the principal does not and so, by agreement with the principal, the charity administers the principal's funds in accordance with the instructions received. Within the charity sector, agency arrangements are sometimes referred to as conduit funding because the charity, in acting as agent, provides a conduit through which funds are passed in order to fund activities or assist the beneficiaries of the principal.
- 19.3. The agent is usually bound by an agency agreement and distributes the funds it holds as agent to specified third parties in line with the instructions given by the principal. The funds transferred to the agent remain under the control of the principal and the principal remains responsible for the charitable application of those funds. A charity acting as agent should ensure that the terms of the agency agreement and the use of the funds are consistent with its own purposes.
- 19.4. It is important to consider the substance of the arrangement over its legal form so as to distinguish between a charity acting as agent and a charity acting as principal:
- As agent, the trustees of a charity have no discretion about the use to which the funds received are put. The charity acts only in accordance with the instructions or directions of the principal.
  - As principal, the trustees of a charity have discretion (subject to the purposes or terms on which the funds are held) as to how the funds are used.
- 19.5. A restricted donation is not an agency arrangement. A charity accounts for the receipt of a restricted fund as principal because the charity's trustees control how it is subsequently spent. For example, even if the purposes of the gift were narrowly defined by the donor, the trustees of a grant-making charity would still retain discretion as to the selection of grant recipients and the timing of the payment.
- 19.6. Charities may also act as custodian trustee holding the title to property belonging to another charity on its behalf. Property held as custodian does not belong to the custodian trustee and so is not a component of the custodian trustee's assets, income or expenditure in the reporting period.

19.7. This module sets out:

- accounting for funds held as agent;
- distinguishing consortia or similar arrangements involving a 'lead' charity; and
- disclosure of funds received as agent or held as custodian trustee.

### Accounting for funds held as agent

19.8. Funds received by a charity as agent are not recognised as an asset in its accounts because the funds are not within its control. Consequently, the receipt of funds as agent is not recognised as income nor is its distribution recognised as the agent's expenditure.

19.9. However, any fee receivable by a charity for acting as agent is recognised as its income. Similarly, any costs incurred by a charity in the administration of the agency arrangement are recognised as expenditure in its accounts.

### Distinguishing consortia or similar arrangements involving a 'lead' charity

19.10. Charities may also enter into a consortium or similar arrangement whereby two or more charities co-operate to achieve economies in the purchase or supply of goods or services for members of the arrangement or to a third party. The accounting for a consortium's transactions requires an understanding of the substance of any underlying contractual arrangements.

19.11. Consortium arrangements can be set up through:

- a formal joint venture arrangement (refer to the SORP module, 'Branches, linked or connected charities and joint arrangements');
- a joint venture entity (refer to the SORP module 'Accounting for joint ventures');
- a charity acting as principal entering into contractual arrangements and then subcontracting with other parties or charities to deliver components of the contract (refer to the SORP module 'Recognition of income, including legacies, grants and contract income'; or
- a lead charity acting as agent for the consortium's members administering the contractual arrangements on behalf of all the members of the consortium.

19.12. When a lead charity acts as agent for members of a consortium, it may provide administrative support to the consortium arrangement, including invoicing and making payments on behalf of the consortium members. However, each charity participating in the consortium retains its own contractual obligations and rights despite the lead charity being the main point of contact with the customer or being the commissioning body for a service. The lead charity is not acting as agent if it is the principal under the contract and is then subcontracting work to third parties, including other charities, in order to fulfill its contractual obligations.

## Disclosure of funds received as agent or held as custodian trustee

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19.13. This SORP requires that a charity that has acted as agent during the reporting period must disclose in the notes to the accounts:

- an analysis of funds received and paid by the charity as agent;
- details of any balances held as agent at the reporting date;
- details of any balances outstanding between any participating consortium members for which it is administratively responsible; and
- where funds have been held as agent for related parties, the charity must make the required disclosures for related parties required by the SORP module '[Disclosure of trustee and staff remuneration, related party and other transactions](#)'.

19.14. This SORP requires that a charity that has acted as custodian trustee during the reporting period must disclose in the trustees' annual report or as a note to the accounts:

- a description of the assets, classes of assets or categories of assets which they hold in this capacity;
- the name and objects of the charity (or charities) on whose behalf the assets are held and how this activity falls within the custodian charity's objects; and
- details of the arrangements for safe custody and segregation of such assets from the charity's own assets.

## Selection 3: Accounting for investment

### 20. Total return (investments) - (England and Wales only)

#### Introduction

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- 20.1. This module applies to charities established in England and Wales that hold investments as permanent endowment and adopt a total return approach to the investment of those funds. This module reflects the requirements of charity law and regulations in England and Wales where a statutory power exists that enables charities to adopt a total return policy for the investment of permanently endowed funds. The FRSSE does not contain any requirements in relation to charities with permanent endowment funds invested on a total return basis.
- 20.2. Trust law requires the trustees of a permanently endowed fund to be even-handed in the way that they allocate investment returns between current and future beneficiaries. Under standard trust rules, income generated from endowed investments must be spent on the purposes of the fund for current beneficiaries and any capital gains or losses must be allocated to the capital of the endowment held to produce income for the benefit of future beneficiaries.
- 20.3. When a total return approach to investment is adopted, the permanently endowed funds are invested to produce an investment return without regard to whether that return is in the form of income (for example, dividends or interest) or capital appreciation.
- 20.4. The investment return forms a component of the endowment fund known as the 'unapplied total return'. The trustees then periodically determine how much of the 'unapplied total return' is released to income for spending and how much is retained for investment as a component of the endowment. This allocation must be made equitably to balance the need for income to meet current requirements and to hold funds as part of the endowment to produce investment returns for the future.
- 20.5. Under a total return approach to investment, the endowment has two distinct components:
  - the value of the original and any subsequent gifts made to the capital of the endowment (which cannot normally be spent) which is termed the 'value of the trust for investment'; and
  - the 'unapplied total return' which represents the accumulated investment returns from the investment of the endowment less any amounts which have been allocated to income.
- 20.6. A charity must have the relevant investment power to adopt a total return approach to investment. This power may be granted to endowed charities in England and Wales by an order of the Charity Commission made under section 105 of the Charities Act 2011 or exercised by trustees under section 104A of the Charities Act 2011 as amended by the Trust (Capital and Income) Act 2013. Charities exercising the power to invest on a total return basis under section 104A of the Charities Act 2011 must also refer to the Charities (Total Return) Regulations 2013 and the further guidance available from the Charity Commission's website.



20.7. This module sets out:

- the accounting treatment;
- disclosures required in the notes to the accounts where permanent endowment is invested on a total return basis; and
- disclosures required in the trustees' annual report.

## The accounting treatment

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20.8. This SORP requires that the following accounting treatment must be used where a charity adopts a total return approach to the investment of endowment:

- income from the endowment's investments must be recognised as 'investment income' in the endowment column of the statement of financial activities (SoFA);
- investment gains and losses (realised and unrealised gains and losses) must be recognised as 'investment gains and losses' in the endowment column of the SoFA;
- any part of the unapplied total return that is allocated to income funds must be separately identified in the SoFA as an allocation between endowment funds and income funds either within the 'transfer' line or within the 'other income' section of the SoFA; and
- the amount of any unapplied total return fund must be included as a part of the relevant endowment together with the value of the trust for investment on the balance sheet.

20.9. Exceptionally, where investment losses exceed the amount of unapplied total return, the loss must be treated as a reduction in the value of the trust for investment component of the permanent endowment until such time as these losses are reversed.

## Disclosures required in the notes to the accounts where permanent endowment is invested on a total return basis

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20.10. This SORP requires that the notes to the accounts must provide the following information for each endowment fund that is invested on a total return basis:

- the amount of the value of the trust for investment which comprises the gift component of the endowment at the start of the reporting period;
- the amount of any additional gifts to the endowment fund during the reporting period added to the value of the trust for investment;
- the amount of any unapplied total return at the start of the reporting period;
- the amount of the investment return from the investment of the endowment for the reporting period;
- the amount of any allocations of unapplied total return to income funds;
- the amount of any recoupment to make good the value of the trust for investment;
- the amount of any allocation from the trust for investment to the unapplied total return;

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- the amount of any unapplied total return at the end of the reporting period;
- the total amount of the endowment fund at the end of the reporting period; and
- details of the power of investment or the order that permits the charity to adopt a total return approach to investment.

20.11. Table 15 summarises how the disclosures required in the notes to the accounts may be set out.

**Table 15: Example of the disclosure of a total return approach to investment of permanent endowment**

	Trust for Investment	Unapplied Total Return	Total Endowment
	£	£	£
<b>At beginning of the reporting period:</b>			
Gift component of the permanent endowment	X	-	X
Unapplied total return	-	X	X
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>
<b>Movements in the reporting period:</b>			
Gift of endowment funds	X	-	X
Recoupment of trust for investment	X	(X)	-
Allocation from trust for investment	(x)	X	-
Investment return: dividends and interest	-	X	X
Investment return: realised and unrealised gains and (losses)	-	X	X
Less: investment management costs	-	(X)	(X)
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>
Unapplied total return allocated to income in the reporting period	-	(X)	(X)
<b>Net movements in reporting period</b>	<b>X</b>	<b>X</b>	<b>X</b>
<b>At end of the reporting period:</b>			
Gift component of the permanent endowment	X	-	X
Unapplied total return	-	X	X
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>

### Disclosures required in the trustees' annual report

20.12. This SORP requires that a charity that has been granted the power to invest on a total return basis by a Charity Commission order (charities registered in England and Wales), or where the trustees have exercised the power granted under section 104A (2) of the Charities Act 2011, must provide the following additional information in the trustees' annual report:

- the date that the initial value of the trust for investment and the initial value of the unapplied total return was established;

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- the policy used to identify the initial amounts of the trust for investment and any unapplied total return and the date this analysis was performed;
- an explanation of the policies used by the charity's trustees and the factors considered in determining the amount of the unapplied total return allocated to income (termed the trust for application) and any amounts allocated to the trust for investment in the reporting period;
- an explanation of the policies used by the charity trustees and the factors considered in determining the amount, if any, of the trust for investment (permanent endowment) allocated to the unapplied total return or any recoupment made from the unapplied total return into the trust for investment in the reporting period; and
- the name and professional qualifications of any person who has provided advice to the charity's trustees as to the amount that can be allocated to income and/or the trust for investment from the unapplied total return in the reporting period.

## 21. Accounting for social investments

### Types of social investment and income risk sharing arrangements

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- 21.1. This module applies to all charities adopting this SORP that make social investments. It explains when an investment is recognised by a charity as either a programme related investment or as a mixed motive (mixed purpose) investment. The FRSSE 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 when reporting under the FRSSE;
- accounting for a write-down to the recoverable amount;
- 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

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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

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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

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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)

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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

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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

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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 if its receipt is probable. If it is virtually certain that the guarantee will be called upon, the asset and the related income receivable is then recognised.

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

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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

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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, there should be an assessment of whether there is any indication that an asset should be written down.

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 when reporting under the FRSSE

21.26. A programme related investment or mixed motive investment in the form of ordinary or preference shares must be measured at the reporting date at either:

- its cost less any provision for diminution in value; or
- at market value (or best estimate thereof), provided this amount can be measured reliably, for example by reference to a current market price or a recent transaction or by the use of estimation techniques.

21.27. 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:

- measure the loans at the amount received or paid, with the carrying amount adjusted for any repayments and any accrued interest (and adjusted if necessary to the recoverable or settlement amount if the loan or part of the loan is irrecoverable or waived); or
- adopt current accounting practice and carry the investment at its amortised cost using the effective interest method (for more information on the use of the effective interest method, users of the FRSSE may find it helpful to refer to section 11 of FRS 102).

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

21.29. 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.

21.30. Programme related investments or mixed motive investments that are measured at cost or amortised cost must be assessed for any indication that an asset should be written down at the end of the reporting period.

21.31. If there is evidence that the carrying value of the investment may not be recoverable, for example a default on repayments due or evidence of significant financial difficulty in the entity in which the investment has been made, then a provision for the loss must be recognised in the statement of financial activities (SoFA) in the same way as for other investments or financial assets.



## Accounting for a write-down to the recoverable amount

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- 21.32. A loss arising on the write-down of a programme related investment to its recoverable amount should be recognised as a cost within 'expenditure on charitable activities' in the SoFA.
- 21.33. In the case of a mixed motive investment, the loss arising from the provision should be recognised within the 'gains/(losses) on investments' line in the SoFA.
- 21.34. Any reversal of a previous write-down must be credited to the heading in the SoFA that was initially charged with the loss. The reversal of the charge must not result in an asset's carrying amount exceeding its carrying amount prior to its initial write-down.

## Accounting for gains on disposal

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- 21.35. Any gain on the disposal of a programme related investment is recognised as 'other income' in the SoFA after offsetting any prior write-down of the investment.
- 21.36. 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 write-down of the investment.

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

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- 21.37. 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

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- 21.38. 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.
- 21.39. 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.

## *Accounting and reporting by charities*

21.40. The applicable disclosures set out in the SORP module '[Accounting for financial assets and financial liabilities](#)' must also be made.

21.41. The SORP also requires that charities making or receiving concessionary loans 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.

## 22. Accounting for charities pooling funds for investment

### Introduction

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22.1. The FRSSE does not address how charities account for pooled investment funds. This module sets out the accounting requirements, reflecting charity law, for:

- common investment funds and common deposit funds;
- restricted participation common investment funds (England and Wales only);
- accounting for pooling schemes and arrangements with common trustees; and
- disclosures for pooling schemes and arrangements with common trustees.

### Common investment funds and common deposit funds

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22.2. Common investment funds (CIFs) and common deposit funds (CDFs) are charities which accept contributions or deposits from any charity and invest these contributions or deposits to earn a return for the investing charities.

22.3. The fund managers and any corporate trustees of CIFs and CDFs are usually regulated by the financial markets' regulator in the jurisdiction(s) in which they are established.

22.4. CIFs and CDFs must not adopt the charities SORP. Instead, as collective investment schemes, CIFs and CDFs must follow the Investment Management Association Statement of Recommended Practice in conjunction with any charity-specific reporting requirements set out in the regulations applying in the jurisdiction in which they are established.

### Restricted participation common investment funds (England and Wales only)

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22.5. Certain CIFs restrict participation in the fund to particular charities that are connected in some way, for example by having similar purposes but without necessarily sharing a common body of trustees. Restricted participation CIFs should adopt the Investment Management Association Statement of Recommended Practice in order to provide appropriate accountability to their charity investors to whom they owe a fiduciary duty.

22.6. In England and Wales, the applicable Charities (Accounts and Reports) Regulations place particular reporting requirements on CIFs, including restricted participation CIFs, which are based on the Investment Management Association Statement of Recommended Practice.

## Accounting for pooling schemes and arrangements with common trustees

- 22.7. Charities with the same body of trustees may pool their investments to form a single investment fund, resulting in greater efficiency in the management of the investment. A pooling scheme or arrangement with common trustees may include linked charities or special trusts (England and Wales) or connected charities (Scotland). Separate charity accounts are not generally published for the pooling scheme or arrangement. Instead, the pooling scheme or arrangement must be presented as a restricted fund of the reporting charity responsible for operating the pooling scheme or arrangement.
- 22.8. The assets of the pooling scheme or arrangement are the investments held. Its liabilities are the share of these investments due to those charities or funds which have invested through the pooling scheme or arrangement. The income and costs of managing investments will accrue to the charities or funds investing in the pool. Much of this information will already be presented in the reporting charity's accounts but charities may choose to summarise this information as a note to the accounts, as set out in Table 16.

**Table 16: Analysis of fund movements for a pooling scheme**

	Fund/ Charity A	Fund/ Charity B	Fund/ Charity C	Fund/ Charity D	Fund/ Charity E	Total
	£	£	£	£	£	£
Net assets brought forward						
Additions to investment pool						
Investment income						
Investment management expenses						
Realised investment gains/(losses)						
Unrealised investment gains/(losses)						
Less distributions (for charitable expenditure)						
<b>Net assets carried forward</b>						

- 22.9. A pooling scheme or arrangement that is registered or established as a separate charity must prepare its own accounts in accordance with this SORP and must make the additional disclosures set out in the section below.

## Disclosure for pooling schemes and arrangements with common trustees

22.10. This SORP requires that a charity which is a pooling scheme or arrangement preparing separate accounts must disclose:

- that the accounts presented are for an investment pooling scheme or arrangement;
- the date and authority, if any, for the scheme or arrangement (for example, a scheme registered with a charity regulator);
- the names of the charities participating in the pooling scheme or arrangement;
- an analysis of the investments held within the pooling scheme or arrangement in accordance with the SORP module '[Balance sheet](#)'; and
- an analysis of the investment income, gains and investment management costs in accordance with the SORP module '[Statement of financial activities](#)'.

22.11. The notes to the accounts should also provide:

- an analysis of the proportions of the funds of the pooling scheme or arrangement attributable to each participating charity or fund at the end of the reporting period; and
- an analysis of the of fund movements attributable to each participating charity or fund, reconciling the value of funds brought forward and carried forward.

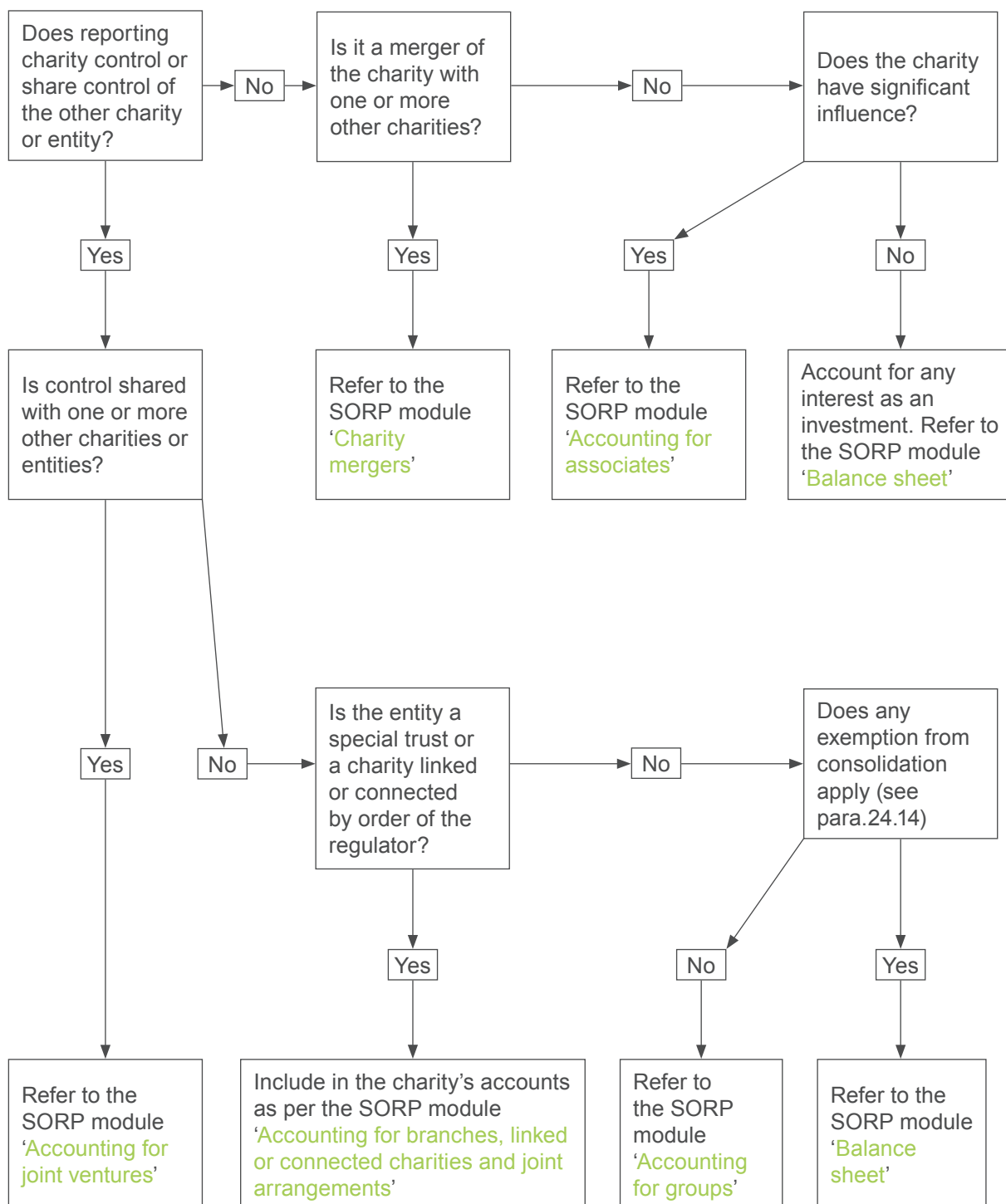
22.12. An example of how the analysis of fund movements for an investment pooling scheme or arrangement may be presented as set out in Table 16.

## Selection 4: Accounting for branches, charity groups and combinations

### 23. Overview of charity combinations

- 23.1. Charities may operate through branches or group structures or share resources, knowledge or service arrangements by working with other charities or non-charity entities to further shared objectives by establishing joint arrangements, activities and operations.
- 23.2. The accounting to be followed for the combination or joint venture depends on the substance of the arrangement and what form it takes, the nature and level of control exercised and whether that control is exercised over the other entity. Depending on the nature of the arrangement, the charity must refer to:
- the SORP module 'Charity mergers';
  - the SORP module 'Accounting for associates';
  - the SORP module 'Balance sheet';
  - the SORP module 'Accounting for joint ventures';
  - the SORP module 'Branches, linked or connected charities and joint arrangements'; or
  - the SORP module 'Accounting for groups and the preparation of consolidated accounts'.
- 23.3. If the reporting charity is itself a subsidiary, it must refer to the SORP module 'Charities as subsidiaries'.
- 23.4. Related party transactions between a parent charity and its subsidiaries, associates and joint ventures must be disclosed. Similarly, in those circumstances where charities have trustees in common, consideration should be given as to whether the circumstances are such that related party disclosures are required. Refer to the SORP module 'Disclosure of trustee and staff remuneration, related party and other transactions'.
- 23.5. Figure 2 provides a guide to which module to refer to when deciding on the accounting for a charity combination.

Figure 2: Guide to accounting for charity combinations



## **24. Accounting for groups and the preparation of consolidated accounts**

- 24.1. All charities using the FRSSE that prepare consolidated accounts, whether as a requirement of charity law or on a voluntary basis under company law, must follow this module.
- 24.2. The FRSSE does not specifically deal with the preparation of consolidated accounts although the FRSSE does set out particular disclosures required by company law that all entities using the FRSSE must have regard to when presenting their accounts. In particular, section 15 of the FRSSE sets out the disclosures relating to subsidiary entities and section 16 sets out disclosure required in consolidated (group) accounts. Section 6 of the FRSSE set out the accounting treatment of purchased goodwill arising from an acquisition.
- 24.3. A charity applying the FRSSE that prepares consolidated accounts may follow its existing accounting policies provided those policies reflect accepted practice and relevant disclosures are made. This module reflects current practice and should be followed by charities using the FRSSE that do not have existing policies for the preparation of consolidated accounts or whose existing policies do not reflect accepted practice. All charities are encouraged to follow current practice as reflected in this module when preparing consolidated accounts. Charities adopting current practice should refer to section 9 of FRS 102 for more information.
- 24.4. Consolidated accounts are prepared by a parent charity and include all of the resources controlled by the parent charity. A parent charity is a charity that has one or more charitable or non-charitable subsidiaries (subsidiary entities).
- 24.5. Where consolidated accounts are prepared, the accounting disclosures required of the charity by other applicable modules are extended to the group accounts (unless otherwise stated).
- 24.6. This module sets out when consolidated accounts must be prepared and the accounting treatment that must be followed when charities adopt current accounting practice for the preparation of consolidated accounts:
- the legal requirements to prepare consolidated accounts;
  - what are consolidated accounts?;
  - how control is identified;
  - the consolidation procedures and accounting for non-controlling interests (minority interests);
  - accounting for charity combinations
  - accounting for the acquisition and disposal of non-charitable subsidiaries; and
  - disclosures required where consolidated accounts are prepared.



## Legal requirements to prepare consolidated accounts

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- 24.7. A parent charity must prepare consolidated accounts to include all of its subsidiary entities where the accounts' preparation is a requirement of:
- company law;
  - charity law in the relevant legal jurisdiction(s); or
  - any other statutory or mandatory framework applicable to the charity.
- 24.8. Details of the thresholds at which the preparation of consolidated accounts is mandatory are set out in Appendix 3, '[Thresholds for the UK and the Republic of Ireland](#)'.

## What are consolidated accounts?

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- 24.9. Consolidated accounts, which are also known as group accounts, combine the activities, assets and liabilities of the reporting charity with those of the subsidiaries it controls. Consolidated accounts include the activities and funds of any subsidiary charity that is controlled by a parent charity as its trustee.
- 24.10. Consolidated accounts present the financial performance and financial position of the accounting group as though it were a single economic entity with a unity of trusteeship.
- 24.11. Consolidated accounts must include any associates or joint venture entities in which the parent charity has an interest. Refer to the separate SORP modules '[Accounting for associates](#)' and '[Accounting for joint ventures](#)' for more information.
- 24.12. The headings used in the accounting statements must state that they present the 'consolidated statement of financial activities' and 'consolidated balance sheet' of the parent charity and its subsidiaries, and the 'consolidated statement of cash flows'.
- 24.13. A subsidiary is not excluded from consolidation because its activities are dissimilar to those of the parent charity or other entities within the consolidation. Nor is a subsidiary excluded from consolidation because it operates in a jurisdiction that imposes restrictions on transferring cash or other assets out of that jurisdiction provided it is able to control and manage those assets within that jurisdiction to further its charitable purposes. If immaterial, subsidiaries, associates or joint ventures are excluded from the consolidated accounts, these are treated as investments and are reported at cost or valuation as appropriate. For more information, refer to the SORP modules '[Balance sheet](#)', '[Accounting for associates](#)' or '[Accounting for joint ventures](#)'.
- 24.14. A subsidiary must be excluded from consolidation where:
- severe long-term restrictions substantially hinder the exercise of the rights of the parent over the assets or management of the subsidiary; a charitable subsidiary must only be excluded when both its charitable objects and its beneficiary class are not concurrent with that of its parent; or
  - the subsidiary is held exclusively with a view to its subsequent resale and the subsidiary has not been previously consolidated by the charity.

## How control is identified

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- 24.15. A parent charity consolidates the subsidiaries it controls. 'Control' is the power to govern the financial and operating policies of an entity in order to obtain benefits from its activities.
- 24.16. Control is made up of two elements: power and benefit. The underlying principle is that the parent charity exercises control to obtain benefit from its interest in the subsidiary. The parent charity is deemed to exercise control over a subsidiary if it has both the power to govern and the ability to benefit.
- 24.17. The power element is presumed to exist when the parent charity owns, directly or indirectly through its subsidiaries, more than half the voting power of an entity. However, control can also exist when the parent charity directly or indirectly controls half or less than half of the voting power of an entity, if it has:
- power over more than half of the voting rights by virtue of agreement with other investors;
  - the power to govern the financial and operating policies of the entity under a statute or an agreement;
  - the power to appoint or remove the majority of the members of the board of directors or equivalent governing body, and control of the entity is by that board or body; or
  - the power to cast the majority of votes at the meetings of the board of directors or equivalent governing body, and control of the entity is by that board or body.
- 24.18. The nature of the control a parent charity exercises differs in its character between non-charitable subsidiaries and controlled charities. Where a charity exercises control as an owner or investor in a non-charitable subsidiary, it does so to benefit from the cash flows and the financial return from that investment.
- 24.19. The parent charity can exercise control through trusteeship, which gives a parent charity the ability to govern the financial and operating policies of the subsidiary charity. The consolidated accounts show the total funds under the trusteeship of the parent charity.
- 24.20. The power element of control of one charity by another can be identified through:
- sole trusteeship;
  - powers to appoint and/or remove a majority of the trustees;
  - the terms of a formal agreement or arrangement; or
  - the provisions of a clause in the governing document or a legislative provision.
- 24.21. Having trustees in common does not in itself demonstrate that the power element is present. Also, simply being the sole or main funder of another charity or entity is insufficient to demonstrate that the power element is present. While the funding of one charity by another indicates a degree of concurrence of purposes, for control to exist the power element must be present.

- 24.22. The benefit element of control is met where the purposes of the parent charity and its subsidiary charity are concurrent. The purposes of the parent charity do not have to be identical to those of its charitable subsidiary, nor do they need to encompass all the purposes of the charitable subsidiary. For concurrence, the purposes of the parent charity have to be similar enough to those of the subsidiary that the activities of the subsidiary can be seen to contribute to the purposes and aims of the parent charity and to benefit the parent charity's beneficiaries.
- 24.23. When considering whether the purposes are concurrent, judgement is required. The charity should consider whether the preparation of consolidated accounts will give a true and fair view of the nature of control it can exercise and its ability to benefit from its interest as the trustee of another charity.
- 24.24. The parent charity might benefit where the services and benefits provided by the subsidiary charity to its own beneficiaries also contribute to the purposes of the parent charity. The funds of the subsidiary charity are restricted to its own purposes and, unless the parent and subsidiary charity have identical purposes, the subsidiary will be a separate component of the group's reported restricted funds. The reporting of a restriction over the use of a subsidiary charity's funds is important for the understanding of the consolidated accounts and of how funds held by charitable subsidiaries may be used. For example, the funds of a subsidiary charity are not normally available to the creditors of the parent charity in the event of the latter's insolvency.

### Consolidation procedures and accounting for non-controlling interests (minority interests)

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- 24.25. When preparing consolidated accounts current practice requires that a parent charity must ensure that:
- the consolidation is undertaken on a line-by-line basis;
  - balances and transactions between the parent and the subsidiary are eliminated;
  - the accounts of the parent and its subsidiaries have, if practicable, the same reporting date; and
  - uniform group accounting policies are adopted for transactions and other events or conditions in similar circumstances.
- 24.26. Transactions between a parent and subsidiary charity are eliminated on consolidation. In the consolidated balance sheet, the charitable funds of the parent charity and the subsidiary charity must not be consolidated on a line-by-line basis; instead, the subsidiary charity's funds should be shown as a component of restricted funds – unless the subsidiary and parent have identical purposes. Where the purposes are identical, the unrestricted funds of the subsidiary are a component of the unrestricted funds of the group.
- 24.27. In some cases, a parent charity may not own the entire equity of a subsidiary. In this case, a non-controlling interest (minority interest) must be recognised. A non-controlling interest exists where a third party has a right to dividends or the distribution of resources, a claim on the net assets of the subsidiary through the holding of equity or significant influence through its voting power.

## Accounting and reporting by charities

24.28. Where a non-controlling interest exists, it is important to consider the substance of the interest as well as legal form. For example, a subsidiary may be established to assist a charity to further its aims with supporters of the charity subscribing to the share capital. If the non-controlling interest enters into an agreement to waive their right to a share of the net assets in the event of the subsidiary being wound up and to receive any dividends, then the parent charity enjoys all the economic benefits of the subsidiary and the non-controlling interest should not be recognised.

24.29. Where a non-controlling interest in a non-charitable subsidiary is recognised, the parent charity must:

- present in its consolidated balance sheet the non-controlling interest in the net assets of the consolidated subsidiaries separately from the parent charity's interest in them;
- present separately the non-controlling interest share of net income (or net expenditure) in the income or expenditure section of the consolidated SoFA; and
- separately present the non-controlling interest's share of any net gain or loss reported within the 'other recognised gains and losses' section of the consolidated SoFA.

24.30. In the case of a non-controlling interest in a subsidiary charity, the measurement of the non-controlling interest should consider the substance of the arrangement and the extent to which, if at all, the non-controlling interest benefits from its interest.

### Accounting for charity combinations

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24.31. Charities may on occasion combine into one reporting entity or operate through a restructured group. To establish whether the combination meets the definition and criteria of a merger, reference must be made to the SORP module 'Charity mergers'. Combinations that are not mergers may also take place between charities whereby assets and liabilities of one charity are transferred into the control of another charity at nil or nominal consideration and are in substance a gift. If the fair value of the assets received exceeds the fair value of the liabilities assumed, a gain is recognised and shown separately within income – normally as a gift (donation). Conversely, if the fair value of liabilities assumed exceed the fair value of the assets acquired then a net loss is recognised and shown separately in charitable expenditure. If the combination is neither in substance a gift nor a merger, it must be accounted for as an acquisition with any negative goodwill written off in the reporting period of acquisition.

### Accounting for the acquisition and disposal of non-charitable subsidiaries

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24.32. The income and expenditure of a subsidiary are included in the consolidated accounts from the date of the acquisition. The income and expenditure of a subsidiary are similarly included in the consolidated accounts until the date on which the parent charity ceases to control the subsidiary.

- 24.33. Where the parent charity purchases a non-charitable subsidiary and the consideration paid exceeds the value of the net assets acquired, goodwill arises on acquisition and is disclosed in the consolidated balance sheet. 'Goodwill' is an intangible fixed asset arising on the acquisition of a subsidiary purchased by the reporting charity. Capitalised goodwill must be depreciated over its useful economic life and if a reliable estimate cannot be made then its economic life is presumed not to exceed five years. The FRSSE requires that goodwill must be depreciated and its economic life reviewed at each balance-sheet date.
- 24.34. However, in the case of a combination which is in substance a gift to the parent charity (where the consideration paid is nil or a nominal amount and is less than the net assets acquired) the parent charity has made a gain. The parent charity should recognise that gain as 'other income' in the consolidated SoFA, rather than treat it as negative goodwill on consolidation. In all other cases, where a parent charity acquires a subsidiary for consideration that is less than the value of the assets acquired, negative goodwill arises on the acquisition. Negative goodwill is disclosed separately on the consolidated balance sheet and released to income as the acquired non-monetary assets are depreciated or recovered through sale. Any negative goodwill in excess of the fair values of the non-monetary assets acquired is recognised as income in the periods expected to benefit.
- 24.35. On the disposal of a controlling interest in a subsidiary, the reporting charity recognises a gain or loss on disposal in the appropriate line of the consolidated SoFA. If the reporting charity retains an equity interest in the former subsidiary, it must determine whether the retained interest represents an investment, an associate or a joint venture entity and account for it accordingly.

### Disclosures required where consolidated accounts are prepared

- 24.36. This SORP requires that the following disclosures must be made in the group's accounting policies note when consolidated accounts are prepared:
- a statement that the accounts are consolidated;
  - the basis for concluding that control exists when the parent charity does not own, directly or indirectly through subsidiaries, more than half of the voting power;
  - any difference in the reporting date of the accounts of the reporting charity parent and its subsidiaries in the preparation of the consolidated accounts;
  - the nature and extent of any significant restrictions on the ability of subsidiaries to transfer funds to the parent charity in the form of cash dividends or to repay loans;
  - the value of any non-controlling interest as a separate item, after the 'Funds of the charity' heading, on the balance sheet; and
  - the name of any subsidiary excluded from consolidation, and the reason for its exclusion.

## *Accounting and reporting by charities*

24.37. This SORP requires that consolidated accounts must disclose, in relation to each material subsidiary:

- its name(s), company number and, where applicable, its charity registration number;
- particulars including the percentage of the parent charity's equity shareholding or other means of control;
- the aggregate amount of its assets, liabilities and funds at the end of the reporting period; and
- a summary of its turnover (or gross income) and expenditure and its profit or loss (or surplus or deficit) for the reporting period;

24.38. If a charity has a large number of subsidiary undertakings, the SORP allows a charity to limit the information to those subsidiary undertakings the results or financial position of which have a material effect on the amounts shown in the consolidated accounts.

24.39. Where the reporting charity acquires a material subsidiary in the reporting period, this SORP requires that it must also disclose:

- the date of acquisition;
- the cost of acquisition and how it was settled, for example by cash or debt instrument; and
- the amounts recognised for each class of assets, liabilities and contingent liabilities at acquisition.

## 25. Branches, linked or connected charities and joint arrangements

### Introduction

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- 25.1. All charities that operate through branches must apply this module. This module also applies to charities when accounting for:
- special trusts and any other non-corporate entities which are administered by, or on behalf of, the reporting charity and whose funds are held for specific purposes which are within the general purposes of the reporting charity;
  - charities linked by the Charity Commission (England and Wales);
  - charities that are connected (Scotland); and
  - joint venture arrangements involving shared assets or shared operations that do not involve a separate joint venture entity being established.
- 25.2. The FRSSE does not deal with accounting for branches, special trusts, linked or connected charities, and shared operations or assets. This module reflects the requirements of charity law and current accounting practice which charities adopting this SORP must follow.
- 25.3. This module sets out:
- what is meant by the term 'branch'?
  - accounting for branches;
  - when to apply branch accounting to other arrangements;
  - branch accounting for special trusts (England and Wales) and similar arrangements;
  - branch accounting for linked charities (England and Wales);
  - branch accounting for connected charities (Scotland); and
  - accounting for joint arrangements involving other charities.

### What is meant by the term 'branch'?

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- 25.4. The term 'branch' is used in this SORP to describe a charity's administrative arrangements whereby its internal operating structure is arranged according to function, location or other factor designed to facilitate its administration.
- 25.5. Branches may include supporters' groups, members' groups, and offices in different countries, communities or parishes that are part of a charity. Branches are commonly used to organise fundraising, to represent the charity in a locality or to carry out the charity's work in a locality.
- 25.6. The indicators of a branch include the following:
- It uses the name of the reporting charity in its title.
  - It raises funds exclusively for the reporting charity and/or its local activities.

## Accounting and reporting by charities

- It uses the reporting charity's registration number on its letterheads, publicity and website.
- It uses the reporting charity's registration number to receive tax relief on its activities.
- It represents itself to the public as the reporting charity's local representative or its representative for a particular purpose.
- It receives support from the reporting charity through advice, publicity materials, fundraising, etc.

25.7. Excluded from the SORP definition of branches are:

- charities that are incorporated and have a legal personality separate from their directors/trustees and members, for example, charities incorporated under the Companies Act, Industrial and Provident Societies, Charitable Incorporated Organisation or companies established by statute or Royal Charter;
- groups of people who gather together to raise funds for a charity or a number of different charities; and
- special interest groups that are affiliated to a particular charity but do not themselves undertake charitable or fundraising activities for the charity.

25.8. All the funds held by the branch will be the legal property of the reporting charity or under the direct control and management of the trustees of the reporting charity. This is the case whether or not a branch has a separate bank account.

### Accounting for branches

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25.9. A branch is an internal structure adopted by a charity to undertake its activities. All transactions undertaken through a branch must be accounted for gross in the reporting charity's own accounts. Similarly, the reporting charity's balance sheet must include all assets and liabilities of the branch when in aggregate these amounts are material. For example, the branch may hold funds at the reporting date that have been raised but not yet remitted to the head office of the reporting charity. When material, these funds must be included in the accounts of the reporting charity.

25.10. Funds raised by a branch for the general purposes of the charity will be accounted for by the reporting charity as unrestricted funds. Funds raised by a branch for specific purposes are accounted for as restricted funds of the charity.

25.11. Any branch accounts form part of the results reported in the accounts of the reporting charity. Individual memorandum branch accounts may be prepared covering only each branch in order to provide information for the benefit of local supporters and beneficiaries.

### When to apply branch accounting to other arrangements

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25.12. Branch accounting should also be adopted for those other arrangements that are not subsidiaries, associates or joint venture entities. Branch accounting should be adopted for:



## Accounting and reporting by charities

- special trusts (in England and Wales) and similar arrangements;
- charities linked by the Charity Commission (England and Wales);
- charities that are connected (Scotland); and
- joint venture arrangements that do not involve a joint venture entity being established.

### Branch accounting for special trusts (England and Wales) and similar arrangements

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- 25.13. If a separate legal entity, which is not an incorporated charity, is administered by, or on behalf of, the reporting charity and its funds are held for specific purposes which are within the general purposes of the reporting charity, that entity may form part of the reporting charity for accounting purposes.
- 25.14. In England and Wales such arrangements will usually fall within the definition of a special trust set out in section 287 of the Charities Act 2011: 'property which is held and administered by or on behalf of a charity for any special purposes of the charity, and is so held and administered on separate trusts relating only to that property'.
- 25.15. A special trust may be a separate endowment fund, a restricted fund, for example a prize fund, or a specific piece of land or an item of property. A special trust can be a separate non-company charity, but where this is the case it is usually listed as a component of the register entry for the reporting charity itself.
- 25.16. A special trust is not a separate reporting entity in charity law for the purposes of preparing and filing of a trustees' annual report and accounts. Instead, it is accounted for as a restricted fund in the accounts of the charity that is acting as trustee of the special trust.
- 25.17. A special trust is accounted for in a similar manner to a branch, but the accounts should separately identify the special trust(s) as a component of restricted funds.

### Branch accounting for linked charities (England and Wales)

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- 25.18. In England and Wales, the Charity Commission can link two or more charities using a direction made under section 12 of the Charities Act 2011. The effect is to link two or more charities for registration and accounting purposes, with the aim of simplifying the reporting arrangements. Linking can apply where the charities either have trustees in common or the charities have common purposes and are interdependent.
- 25.19. Branch accounting should be adopted for all linked charities that are not companies established under company law. If one or more of the linked charities is a company, company law requires that each prepares its own entity accounts. Consolidated accounts must be prepared by the parent charity if the combined income of the reporting charity and linked subsidiary-company charities exceeds the applicable threshold (see Appendix 3, 'Thresholds for the UK and the Republic of Ireland') or they have been linked for reporting purposes in which case the linked charitable company is treated as a subsidiary. Refer to the SORP module 'Accounting for groups and the preparation of consolidated accounts'.

## Accounting and reporting by charities

25.20. Accounts prepared for linked charities on a 'branch' basis combine (or aggregate) the funds held by each linked charity. However, the funds of each linked charity must be separately identifiable as they are not merged together. Each charity retains its own charitable purpose. The separate charities are reported in a manner that is similar to the presentation of restricted funds (refer to the SORP module 'Fund accounting' for the disclosures required for restricted funds).

25.21. Linked charities should be presented in the combined accounts by:

- including a separate column or columns in the statement of financial activities (SoFA) and the balance sheet for each linked charity; or
- providing an analysis in the notes to the accounts differentiating the activities and funds held by each linked charity, including any restricted funds.

### Branch accounting for connected charities (Scotland)

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25.22. In Scotland, two or more charities can be connected under Regulation 7 of the Charities Accounts (Scotland) Regulations 2006 (as amended). Connected charities are those charities that have common or related charitable purposes or those that have common control or unity of administration. The connected charities may prepare a single set of accounts.

25.23. Where connected charities prepare a single set of accounts, they must include all of the information for each charity that would be required if each charity produced individual accounts. This may be achieved, for example, by including a separate column or columns in the SoFA and balance sheet.

### Accounting for joint arrangements involving other charities

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25.24. Joint arrangements can take many forms, and charities must consider the substance of the arrangement. Charities should make reference to any agreements to identify the charity's share of the income and expenditure, and assets and liabilities relating to the joint arrangement.

25.25. A joint venture is a specific form of joint arrangement. A joint venture is established by contractual agreement whereby two or more parties (the venturers) undertake an economic activity that is subject to joint control. Joint control is the contractually agreed sharing of control over an economic activity. It exists only where the strategic financial and operating decisions relating to the activity require the unanimous consent of all of the parties sharing control.

25.26. Where the joint venture is one of jointly controlled operations or jointly controlled assets, this SORP requires each venturer includes in its accounts its own charity's share of the income and expenditure and assets and liabilities relating to the joint venture activity. Where appropriate, the joint venture should be reported as a separate activity in the SoFA and notes to the accounts. However, if a joint venture entity is established, refer to the SORP module 'Accounting for joint ventures' for the accounting treatment to follow.

## 26. Charities as subsidiaries

### Introduction

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- 26.1. On occasion, a company or other incorporated body may act as a charity's corporate trustee, or a charity's trustees may be appointed by another entity. In these circumstances, the charity can be viewed for accounting purposes as a subsidiary because it is being 'controlled' by another entity through the trusteeship arrangements. This module applies to charities that are treated as a subsidiary in the accounts of another entity.
- 26.2. A subsidiary is an entity that is controlled by a parent entity. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Although a charity is controlled and managed by its trustees, it can be a subsidiary for accounting purposes when the criteria for control are met.
- 26.3. Section 15 of the FRSSE sets out particular disclosures required by company law that charities using the FRSSE must have regard to when presenting their accounts. This SORP requires all charities make relevant disclosures as set out in the FRSSE for a parent entity and in addition provide information about how control over the charity is exercised and of transactions with the parent entity.

### Disclosures required by the SORP

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- 26.4. A charity adopting the FRSSE that is a subsidiary must disclose in a note to its own accounts:
- the name of its parent entity;
  - the country of incorporation of its parent entity, if it is outside the UK (or the Republic of Ireland);
  - if unincorporated, the address of its parent's place of business; and
  - the address from which the public can obtain the consolidated accounts that include the subsidiary charity's accounts.
- 26.5. In addition, charities adopting this SORP must also disclose:
- if the parent is a charity, its charity registration number and, if applicable, its company registration number in the jurisdiction of its registration;
  - the parent's principal purposes and activities; and
  - how control can be exercised by the parent, for example, through corporate trusteeship or through a power to appoint or remove the majority of trustees.
- 26.6. Where for accounting purposes the parent entity is itself a subsidiary of another entity, this SORP requires that the notes to the accounts must disclose the same information about the subsidiary charity's ultimate parent entity.
- 26.7. The accounts must also make the applicable disclosures set out in the SORP module '[Disclosure of trustee and staff remuneration, related party and other transactions](#)'.

## 27. Charity mergers

### Introduction

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- 27.1. This module applies to charities that have combined and meet the criteria for merger accounting. A charity merger involves two or more charities coming together in partnership for the mutual sharing of risks and benefits, usually through the creation of a new charity. No party obtains control over any other, or is otherwise seen to be dominant.
- 27.2. The FRSSE does not specifically deal with merger accounting and therefore this module reflects current accounting practice which charities adopting this SORP must follow when accounting for mergers. Charities that combine by way of a merger should also have regard to paragraphs PBE34.80 to PBE34.86 of the specialised activities section in FRS 102.
- 27.3. A merger often involves the formation of a new charity to further the purposes of the combining charities and to control the activities, assets and liabilities of the combining charities. The module sets out:
- criteria for merger accounting;
  - accounting for mergers;
  - accounting for charity reconstructions as mergers; and
  - disclosures relating to mergers.

### Criteria for merger accounting

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- 27.4. A charity combination must be accounted for as a merger if all of the following criteria are met:
- No party to the combination is portrayed as either acquirer or acquiree, either by its governing body or management or by that of another party to the combination.
  - All parties to the combination, as represented by the members of the governing body, participate in establishing the management structure of the combined charity and in selecting the management personnel. Such decisions are made on the basis of a consensus between the parties to the combination, rather than purely by exercising voting rights.
  - There is no significant change to the class of beneficiaries of the combining entities or the purpose of the benefits provided as a result of the combination.
- 27.5. When charities merge, their purposes must be concurrent and the purposes of the new reporting entity must encompass those of the combining charities. While a merger may result in some changes to how activities are carried out, and/or some minor changes to purposes, a significant change in purposes or the beneficiary class would rule out accounting for the combination using merging accounting.

## Accounting and reporting by charities

- 27.6. No significant change to classes of beneficiaries or the purpose of the benefits provided is construed as meaning that there has been no major change. A limited widening of beneficiary class or purposes does not in itself preclude the use of merger accounting.
- 27.7. If the combination does not meet all of the above criteria, then it must be treated as an acquisition (see the SORP module '[Accounting for groups and the preparation of consolidated accounts](#)').

### Accounting for mergers

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- 27.8. Merger accounting involves aggregating the assets, liabilities and funds of the combining charities and presenting them as though they had always been part of the same reporting charity. Although the merger may have taken place part way through a reporting period, the accounts must be drawn up to include the results of the combining charities for the whole of the reporting period in which the merger occurred.
- 27.9. Any funds of the combining charities that are restricted to the particular purposes of the new charity must continue to be presented as 'restricted' in the accounts of the merged charity. The unrestricted funds of the constituent charities to the merger will be aggregated provided that their purposes are identical to the new charity. Refer to the SORP module '[Fund accounting](#)' for more information on the classification of funds.
- 27.10. The accounts must present comparative amounts on the same basis to show the aggregated results for the combining charities for the previous reporting period. The comparative amounts should be identified as being 'combined' figures.
- 27.11. The carrying amount of assets and liabilities of the combining charities are not restated to fair value, although adjustments must be made to ensure uniformity of accounting policies.

### Accounting for charity reconstructions as mergers

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- 27.12. In some cases, a charity may change its legal form but its purposes and beneficiary class remain unchanged. The most common examples are the decision by trustees of an unincorporated trust to establish a charitable company or charitable incorporated organisation to take forward the charity's work and the conversion of a charitable company to a charitable incorporated organisation.
- 27.13. These reconstructions should be treated as mergers and not acquisitions, provided that:
- the use of the merger accounting method is not prohibited by company law or other relevant legislation;
  - the beneficiary class is not significantly changed;
  - the purposes for which funds are held are not significantly changed;
  - the persons who constitute the trustee body are not significantly changed; and
  - no non-controlling interest in the net assets of the charity is altered by the transfer.

## Disclosures relating to mergers

27.14. This SORP requires, in the reporting period in which the merger takes place, that the accounts for the merged charities must disclose:

- the names and descriptions of the combining charities;
- the date of the merger;
- an analysis of the principal components of the current reporting period's statement of financial activities (SoFA), to indicate:
  - the amounts relating to the merged charity for the period after the date of the merger; and
  - the amounts relating to each party to the merger up to the date of the merger;
- an analysis of the principal components of the previous period's SoFA accounts between each party to the merger;
- the aggregate carrying amount of the net assets of each party to the merger, differentiating between restricted and unrestricted funds at the date of the merger; and
- the nature and amount of any significant adjustments they have made in order to align accounting policies, and an explanation of any further adjustments to net assets as a result of the merger (for example any restatement of unrestricted funds).

27.15. This SORP also requires that the accounts of a charity created by a merger must disclose in reporting periods subsequent to the merger:

- the names and descriptions of the combining charities; and
- the date of the merger.

27.16. Tables 17 to 19 illustrate how these disclosures may be shown. On a merger taking place, the unrestricted funds of the participating charities may become restricted in whole or in part due to their objects being narrower than those of the merged charity. In such cases, Table 19 should be adapted accordingly.

**Table 17: Analysis of principal SoFA components for the current reporting period**

	Charity A (pre-merger)	Charity B (pre-merger)	Charity (post- merger)	Combined total
	£	£	£	£
Total income				
Total expenditure				
Net income/(expenditure)				
Other gains/(losses)				
<b>Net movement in funds</b>				

**Table 18: Analysis of principal SoFA components for the previous reporting period**

	Charity A	Charity B	Combined total
	£	£	£
Total income			
Total expenditure			
Net income/(expenditure)			
Other gains/(losses)			
Net movement in funds			
Total funds brought forward			
<b>Total funds carried forward</b>			

**Table 19: Analysis of net assets at the date of merger**

	Charity A	Charity B	Combined total
	£	£	£
Net assets			
Represented by:			
Unrestricted funds			
Restricted income funds			
Endowment funds			
<b>Total funds</b>			

## 28. Accounting for associates

### Introduction

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- 28.1. This module applies to charities with an interest in an associate entity. If a charity has a long-term participating interest in another entity and exercises significant influence over its operating and financial policies, then that entity is likely to be an associate.
- 28.2. The FRSSE does not specifically deal with accounting for associates although section 16 of the FRSSE sets out certain disclosure requirements of company law relating to the presentation of interests in associates to which charities should have regard.
- 28.3. A charity applying the FRSSE may continue to use its existing accounting policies for associates provided those policies reflect accepted accounting practice and relevant disclosures are made. This module reflects current accounting practice which charities adopting this SORP should follow if they do not have an existing accounting policy for associates or whose existing policies do not reflect accepted practice. All charities are encouraged to adopt current practice when accounting for associates.
- 28.4. This module sets out the accounting treatment that must be followed when charities adopt current accounting practice for associates:
- [how to identify an associate](#);
  - [accounting for an interest in an associate](#);
  - [presentation of associates in the accounts](#); and
  - [disclosures of interests in associates](#).

### How to identify an associate

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- 28.5. An associate is an entity over which the investing charity has significant influence, but it is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the associate but is not control or joint control over those policies.
- 28.6. A charity is presumed to have an interest in an associate if, as the investing charity, it holds directly or indirectly 20 per cent or more of the voting power of the associate – unless it can be clearly demonstrated that significant influence does not exist.
- 28.7. Where the charity has an interest in an entity but holds, directly or indirectly, less than 20 per cent of the voting power of that entity, it is presumed that no significant influence exists, unless such influence can be clearly demonstrated.
- 28.8. An investing charity exercises significant influence over an associate if it actively influences the associate's policy decisions so as to benefit. For example, when the associate is a commercial investment, the investing charity might exercise influence over the associate's dividend and reinvestment policies. When the associate is another charity or a programme related investment, the investing charity might exercise influence over the associate to ensure that its activities or objectives contribute to its own.



## Accounting and reporting by charities

- 28.9. Charities may nominate a trustee or trustees or make them available to other charities in order to provide those charities with expertise or to give them access to particular skills. Some funders and grant-making charities combine financial assistance with the provision of advice, or they may be invited by the recipient of the funding to provide or nominate a trustee or trustees with particular skills. Where the recipient charity operates with a small trustee body, this might qualify as creating an associate.
- 28.10. An associate is created if the nomination or appointment power is used in conjunction with a formal or informal agreement to exercise significant influence through direct involvement in setting the funding recipient charity's financial and operating policies. However, the power to make a trustee appointment that is simply used to provide advice or expertise to the recipient charity, while allowing the recipient charity to adopt its own policies and strategies, does not create an associate relationship.

### Accounting for an interest in an associate

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- 28.11. The accounting treatment of an associate depends on whether or not the investing charity prepares consolidated accounts. In its individual accounts, a charity must include the interest in its associate at its cost less any amounts written off or the charity may choose to value the investment on an appropriate basis. This SORP only permits a valuation approach if the fair value of the charity's interest can be measured reliably. Any gain or loss on revaluation of the investment is recognised within the 'other recognised gains/losses' section of the SoFA unless a loss takes the carrying value of the investment below its historical cost or the gain reverses a loss previously charged through income and expenditure. In these latter cases the gain or loss is recognised in the income and expenditure section of the SoFA.
- 28.12. However, when consolidated accounts are prepared, accepted and current practice requires that the charity must use the equity method of accounting to measure its interest in the associate.
- 28.13. The equity method of accounting requires the associate to be initially recognised at its cost (the transaction price paid), including any cost incurred making the investment (transaction costs). In the consolidated accounts, the initial cost equates to the fair value of net assets acquired, plus any goodwill. The carrying amount of an investment in an associate is subsequently adjusted through the income and expenditure sections of the SoFA to reflect the investing charity's share of the associate's results. The carrying amount thereby reflects the investor's share of the post-acquisition change in the net assets of the associate.
- 28.14. If the interest in the associate is achieved through the power to appoint trustees to a charity, the interest should be initially recognised at the fair value of the investing charity's share of the associate's net assets on appointment of the trustees. If no consideration is involved, the interest in the associate established through trusteeship is accounted for as though it were a gift, and recognised as a gain under the 'Income from donations and legacies' heading in the statement of financial activities (SoFA).

28.15. The investing charity's share of the associate's net assets is determined by its ownership interest in the associate. If the associate is a charity, then reference should be made to any formal agreement to identify a basis for measuring the interest or share in the associate. The rebuttable presumption, in the absence of any information to the contrary, is that the interest in the associate is measured by reference to the proportion of the voting rights held by the parent based on voting rights attaching to that interest as set out in the associate charity's governing document.

### Presentation of associates in the accounts

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28.16. This SORP requires that an investment in an associate must be classified as a fixed asset investment and separately identified either on the investing charity's balance sheet or in its notes to the accounts analysing the classes of fixed asset investments it holds.

28.17. If the associate is a charity, the investment should be presented within restricted funds, as the purposes of the associate are likely to be distinct from those of the investing charity. The investment should be shown as a programme related investment.

28.18. When consolidated accounts are prepared, the investing charity's share of the associate's results should be presented as a separate line in the consolidated SoFA, under either 'Income', if a gain, or 'Expenditure', if a loss.

### Disclosures of interests in associates

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28.19. This SORP requires that charities with an investment in an associate must disclose:

- the accounting policy adopted for investments in associates;
- the name of the associate(s);
- the carrying amount of investments in associates; and
- for each material associate that is a charity, an analysis of the investing charity's share of the income and expenditure of the associate, analysed across the main areas of the associate's activities.

## 29. Accounting for joint ventures

### Introduction

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- 29.1. Charities may collaborate with other charities or entities in a number of ways. This module applies to charities that collaborate with other charities or entities through various types of joint venture activity and sets out the accounting treatment for joint venture entities.
- 29.2. A joint venture entity is a jointly controlled entity in which each party (venturer) has an interest. The other venturers may be charities, social enterprises or for-profit companies or other entities.
- 29.3. A unique feature of a joint venture entity is a contractual agreement between the parties that share control of the entity.
- 29.4. The contractual agreement between the venturers establishes joint control over the economic activity of the entity. Joint control exists only where the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control.
- 29.5. The FRSSE does not deal specifically with accounting for interests in joint ventures. A charity applying the FRSSE that has an interest in a joint venture may continue to use its existing accounting policies for that interest provided those policies reflect accepted practice and relevant disclosures are made. This module reflects current practice which charities adopting this SORP must follow if they do not have an existing policy for interests in joint ventures or whose existing policies do not reflect accepted practice. All charities are encouraged to follow current practice when accounting for joint ventures.
- 29.6. This module sets out the accounting treatment that must be followed when charities adopt current accounting practice for the preparation of consolidated accounts:
- the different forms of joint venture activity;
  - method for the identification of respective interests in joint venture charities;
  - accounting for joint venture charities;
  - accounting for joint ventures involving non-charitable entities;
  - presentation of joint ventures involving non-charitable entities in the consolidated accounts; and
  - disclosures relating to joint ventures.

### The different forms of joint venture activity

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- 29.7. There are three forms of joint venture activity:
- jointly controlled operations where each venturer uses its own assets, incurs its own expenses and liabilities, raises its own finance and shares the income from the joint venture in a way that is agreed with the other venturers;

## Accounting and reporting by charities

- jointly controlled assets acquired for the joint venture with the assets, liabilities, income, expenses and income of the joint venture shared between the venturers; or
- jointly controlled entities where a separate legal entity, for example a company, is established in which each venturer has an interest with a contractual agreement in place and joint control exercised.

29.8. This module deals with joint venture activities that are carried out through a separate jointly controlled entity.

29.9. Where charities undertake joint venture activities through jointly controlled operations or through using jointly controlled assets, each charity's gross share of the incoming resources and resources expended and the assets and liabilities should be included in the participating charities' own accounts in accordance with the SORP module 'Branches, linked or connected charities and joint arrangements'.

### Method for the identification of respective interests in joint venture charities

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29.10. Each venturer exercises its right to shared control through an agreement with the other parties to the joint venture. On occasion, the joint venture entity will be established to undertake an activity that furthers the charitable purposes of the investing charities, for example to carry out a joint project. When the joint venture entity is itself a charity, control may be exercised through the appointment of trustees rather than through an equity share. In the absence of equity, judgement is required in order to identify the respective interests of each charity in the joint venture entity.

29.11. In order to identify the respective interests of each venturer, reference should be made to the evidence provided by:

- the joint venture agreement or contract;
- the governing document or any legislative provision, including the provisions that apply upon winding up or ceasing the joint venture;
- the respective voting power of the venturers;
- the pattern of distribution of benefits from the joint venture charity between the venturers; and
- the value of the funding provided by each venturer in support of the activities undertaken by the joint venture; or
- in the absence of any evidence to the contrary, the net assets and results should be attributed equally between the venturers.

### Accounting for joint venture charities

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29.12. An interest in a joint venture charity is normally treated as a restricted fund in the accounts of the reporting charity.

## Accounting and reporting by charities

- 29.13. In a charity's own entity accounts, a joint venture charity should be included in its accounts as a programme related investment at cost less any amounts written off, or the charity may choose to value the investment on an appropriate basis. This SORP only permits a valuation approach if the fair value of the charity's interest can be measured reliably. Any gain or loss on revaluation of the investment is recognised within the 'other recognised gains/losses' section of the SoFA unless a loss takes the carrying value of the investment below its historical cost or the gain reverses a loss previously charged through income and expenditure. In these latter cases the gain or loss is recognised in the income and expenditure section of the SoFA.
- 29.14. If consolidated accounts are prepared, current practice requires that the equity method of accounting must be used. The venturer's share of the net income or net expenditure in a joint venture charity is recognised as a separate line in the statement of financial activities (SoFA), under either 'Income', if a gain, or 'Expenditure', if a loss. On the balance sheet, the net carrying amount should be shown under 'Programme related investments' where the interest is held primarily to further the purposes of the investing charity, and is normally treated as a component of restricted funds.

### Accounting for joint ventures involving non-charitable entities

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- 29.15. Charities may also enter into a joint venture as a commercial activity to raise funds. The accounting treatment of a non-charitable joint venture entity depends on whether the investing charity prepares consolidated accounts or entity accounts.
- 29.16. In a charity's own entity accounts, a joint venture entity must be included in its accounts at cost less any amounts written off or, the charity may choose to value the investment on an appropriate basis. This SORP only permits a valuation approach if the fair value of the charity's interest can be measured reliably.
- 29.17. When consolidated accounts are prepared, current practice requires that the charity must use the equity method of accounting in its consolidated accounts to measure its interest in the joint venture.

### Presentation of joint ventures involving non-charitable entities in consolidated accounts

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- 29.18. The equity method requires the interest in a joint venture to be initially recognised at its cost. The initial cost recognised therefore equates to the value of net assets acquired, plus any goodwill. The carrying amount is then adjusted for the post-acquisition change in the investor's share of net assets in the joint venture entity.
- 29.19. The equity method requires the net share of profit or loss to be shown as a separate line in the consolidated SoFA either as a gain under 'Income' or as a loss under 'Expenditure'. The share of net assets in the joint venture is shown as a separate line in 'Fixed assets' on the balance sheet as a sub-class of investments, with any distributions or dividends received reflected in a reduction to the carrying amount of the joint venture.

## Disclosures relating to joint ventures

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29.20. This SORP requires that charities with an investment in a joint venture entity must disclose:

- the accounting policy adopted for investments in joint ventures;
- the name of each joint venture entity;
- the carrying amount of investments in joint venture entities;
- the investing charity's share or interest in each material joint venture entity;
- the aggregate amount of its commitments relating to each joint venture, including its share of capital commitments;
- for each material joint venture, the investing charity's share of the income and expenditure and other of the joint venture charity analysed across the main areas of the joint venture charity's activities; and
- for each material joint venture charity, the investing charity's share of the assets and liabilities and funds of the joint venture charity at the reporting date.

## Appendices

### Appendix 1: Glossary of terms

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**Accepted (accounting) practice** is the accounting policies and estimation techniques specified in relevant Financial Reporting Standards issued by the Financial Reporting Council (Accounting Standards Board) and in the Charities SORP extant at the date that the most recent accounts for a reporting period commencing before 1 January 2015 were approved.

**Accounts** is a term used in the SORP to refer to the statement of financial activities (SoFA), income and expenditure account (where produced or required by company law), balance sheet, cash flow statement (where provided) and notes to the accounts.

**Accruals accounts** record the income and expenditure of the charity and the increase or reduction in its assets and liabilities. All income and charges relating to the financial year to which the accounts relate must be taken into account without regard to the date of payment or receipt. Accruals accounts are compiled on a 'true and fair' basis in accordance with accounting standards and the SORP.

**Activity classification** of costs is the method of identifying the total cost of an activity, including both direct and indirect costs. An activity is a project, programme of work or activity that furthers one or more of a charity's legal purposes, or an activity undertaken to raise funds for the charity.

The SORP identifies three high-level activities for charities preparing accruals accounts: expenditure on raising funds, expenditure on charitable activities and other expenditure.

**Asset** is a resource controlled by the charity as a result of past events and from which future economic benefits are expected to enable the charity to further its charitable aims.

**Audit** when referred to in the SORP is the statutory requirement under charity law for an audit of the charity or the group where the charity's or group's gross income and/or assets exceed the relevant threshold. The audit threshold is set by charity law on the basis of the income received in the reporting period and the total assets held at the end of the year.

**Balance sheet** (also known as a statement of financial position) is a statement of the assets, liabilities and funds of the charity (the funds of the charity may also be known as the residual interest) at the end of the reporting period (accounting period).

**Branch** - Refer to the SORP module '[Branches, linked or connected charities and joint arrangements](#)'.

**Capital** is the charity law term used by the SORP for resources received by the charity which the trustees are either legally required to invest or retain and use for the charity's purposes. Capital is the term applied to permanent endowment where the trustees have no power to convert it into income and apply or spend it; the term also applies to expendable endowment where the trustees do have this power.

## *Accounting and reporting by charities*

**Charitable companies (company charities)** are those charities established under company law for exclusively charitable purposes. The reference to company law is the law as it applies in England and Wales, Scotland, Northern Ireland and the Republic of Ireland. A feature of charitable companies is that of dual registration with the regulator for companies and the charity regulator. Both company law and charity law apply to the annual reporting requirements of a charitable company.

**Charity** is any institution established for purposes which are exclusively charitable in the law applying in England and Wales, Scotland, Northern Ireland or the Republic of Ireland. A charity includes all those activities, administrative branches and funds falling within the scope of a single governing instrument or for which the trustees are otherwise legally liable to account. The reference to a single governing instrument includes a situation where instruments are supplemental to the main instrument apply.

**Charity trustees** are the people who, under the governing document, are responsible for the general control and management and administration of the reporting charity. Charity trustees are those defined in section 177 of the Charities Act 2011, section 106 of the Charities and Trustee Investment (Scotland) Act 2005, section 180 of the Charities Act (Northern Ireland) 2008 or Part 1 of the Charities Act 2009 (Republic of Ireland). In the charity's governing document, trustees may be called trustees, committee members, governors or directors, or they may be referred to by some other title. In the case of a company charity it is the directors who are the charity trustees.

**Combined financial statements (aggregated accounts)** are accounts prepared by the reporting charity which aggregate the assets and liabilities and income and expenses of one or more connected charities with those of the reporting entity itself. Combined accounts provide a 'true and fair' view of all of the charities controlled and administered by the trustees of the reporting charity.

**Common deposit funds (CDFs)** are collective investment schemes that are authorised to accept deposits and are for charity investors only. They are investment vehicles that pool deposits and provide diversification to reduce risk, and are tax efficient, cost effective and administratively simple. They are deemed by law to be charities themselves, and enjoy the same tax status as other charities.

**Common investment funds (CIFs)** are collective investment schemes that are similar to authorised unit trusts and are for charity investors only. They are investment vehicles that provide diversification to reduce risk, and are tax efficient, cost effective and administratively simple. They are deemed by law to be charities themselves, and enjoy the same tax status as other charities.

**Consideration** is the term for the resources used to settle a transaction or the making of a payment in cash or kind.

**Consolidated accounts** is an accounting term for the accounts (financial statements) of a parent and its subsidiaries presented as those of a single economic entity.



## *Accounting and reporting by charities*

**Constructive obligations** is an accounting term for obligations that derive from actions where:

- through an established pattern of past practice, published policies or a sufficiently specific current statement, the reporting charity has indicated to other parties that it will accept certain responsibilities; and
- as a result, the charity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

**Contingent asset** is an accounting term for a possible asset that arises from past events. Its existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control.

**Contingent liability** is an accounting term for either:

- a possible obligation that arises from past events where its existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control; or
- a present obligation that arises from past events but is not recognised in the accounts – either because it is not probable that a transfer of economic benefits will be required to settle the obligation, or because the amount of the obligation cannot be measured with sufficient reliability.

**Contract income** is income received by a charity for the purpose of providing the goods or services under the terms of a legal contract. It is important that trustees establish from the outset whether the receipt of income is subject to a legally binding contract for the supply of goods or services.

Indicators of a contract for the supply of services are:

- the payer, rather than the recipient charity, has taken the lead in identifying the services to be provided; and/or
- the arrangement provides for damages to be paid in the case of a breach of its terms, rather than, for example, for total or partial refund of the payment made.

If there is no contract, the rights and obligations of the parties will depend primarily on the law of trusts and conditional gifts, rather than on the law of contract; such arrangements are termed 'performance-related grants' by the SORP. A contractual payment to the charity will normally be unrestricted income of the charity.

**Control** (of an entity) is the power to govern the financial and operating policies of an entity in order to obtain benefits from its activities. For example, a charity may exercise control over a subsidiary in order to raise funds for the charity through trading activities or as a vehicle to carry out certain of the charity's aims.

**Current (accounting) practice** are accounting policies set out in relevant Financial Reporting Standards, including the FRSSE, in effect for reporting periods starting on or after 1 January 2015. Current practice includes the accounting policies and estimation techniques specified by this SORP.

**Custodian trustees** have no power to make management decisions and can only act on the lawful instructions of the charity trustees regarding the property they hold on behalf of the charity. The term custodian trustee includes any non-executive trustee in whose name property belonging to the charity is held.

**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. A trustee who is a de facto trustee of a company charity may alternatively be known as a de facto director.

**Deferred income** consists of resources received by a charity that do not meet the criteria for recognition as income in the statement of financial activities (SoFA) because entitlement to the income does not exist at the balance sheet date. Deferred income is not recognised in the SoFA until the charity is entitled to the income. Instead, deferred income is disclosed as a liability in the balance sheet.

**Defined benefit pension scheme** (sometimes known as a final salary pension scheme) is a pension or other retirement benefit scheme other than a defined contribution scheme. Usually, the scheme rules define the benefits independently of the contributions payable, and the benefits paid are not directly related to the investments of the scheme.

**Defined contribution pension scheme** is a retirement benefit plan under which an entity pays fixed contributions into a separate entity (a fund), and has no legal or constructive obligations to pay further contributions if the fund does not have sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

**Designated fund** is a portion of the unrestricted funds of the reporting charity that has been set aside for a particular purpose by the trustees. For example, the value of functional fixed assets used to further the charity's aims may be identified as a separate designated fund. Designated funds continue to count as part of the unrestricted funds of the charity, but the trustees may choose to exclude designated funds from the calculation of the charity's reserves.

**Donated services and facilities** include gifts of facilities or services including any contribution from volunteers. Donated services and facilities can also be referred to as intangible income.

**Donations** comprise gifts that will not provide any economic return to the donor other than the knowledge that someone will benefit from the donation. Income from donations includes gifts that must be spent on some particular area of work (i.e. restricted income funds) or given to be held as endowment funds. Donations will normally include gifts in kind and donated services.

Donations, for accounting presentation purposes, exclude any gifts such as performance-related grants where entitlement is dependent on the performance of a particular level of service or units of output being delivered.

**Economic benefits** refers to the value derived from an asset in terms of cash flows generated, its cash flow generating capacity, or the service potential created, or costs saved or avoided by having control over the asset.

## *Accounting and reporting by charities*

**Emoluments** include all salary and bonus payments made to staff during the reporting period by the charity including the value of any taxable benefits.

**Endowment funds** are resources received by the charity that represent capital. A feature of endowment funds is that charity law requires the trustees to invest it or to retain and use it for the charity's purposes. The term endowment applies to permanent endowment, where the trustees have no power to convert it into income and apply it, and to expendable endowment where the trustees do have this power.

**Existing (accounting)** policies are those accounting policies and accounting disclosures adopted by the charity for the preparation of its accounts for the reporting period immediately prior to the first reporting period beginning on or after 1 January 2015. It will include the accounting policies followed by the charity in adopting the previous Charities SORP (SORP 2005) and those policies that were developed with regard to the accounting standards approved by the Financial Reporting Council (Accounting Standards Board) that were current at that time.

**Ex gratia payments** are payments made at the discretion of trustees and not as a result of a contract or other legal obligation.

Ex gratia payments are of two distinct types:

- those which, in furtherance of the charity's charitable aims, are ex gratia payments by a charity in relation to its charitable activities (for example extra payments to retiring employees); and
- those which are not in furtherance of the charity's charitable aims and are ex gratia payments that the trustees believe are expedient to make as a result of a compelling moral obligation.

**Fair value** is the amount at which an asset or liability could be exchanged in an arm's length transaction between informed and willing parties, other than in a forced or liquidation sale. For traded securities in which there is an established market, the fair value is the value of the security quoted in the London Stock Exchange's Daily Official List or equivalent. For other assets where there is no market price on a traded market, it is the trustees' or valuer's best estimate of fair value. In these circumstances, fair value measurement aims to estimate an exchange price for the asset or liability being measured in the absence of an actual transaction for that asset or liability.

**Financial instrument** is a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

**Fundraising costs** consist of three categories:

- costs of generating donations;
- fundraising trading costs, which are the costs of trading to raise funds and include the cost of goods sold and any other costs associated with a trading operation; and
- investment management costs.

**Funds** is a legal term for the money and other assets held on trust. A fund may be unrestricted and available to apply or spend on any of the purposes of the charity or it may be restricted to a specified purpose or purposes.

Restricted funds may be either endowment or restricted income funds, depending on the nature of the restriction. Where the fund is not endowment and is held on trust for spending on specific purposes, it is known as a restricted income fund. Each fund is a pool of resources that is held and maintained separately from other pools because of the circumstances in which the resources were originally received, or the restrictions on that fund which determine the way those resources are subsequently to be treated. Refer to the SORP module 'Fund accounting' for the legal position as regards the various funds of a charity.

**General volunteer** is a term used in the SORP for a person who is giving unremunerated assistance to the charity of any kind other than assistance which is related to their trade or profession.

**Governance costs** are the costs associated with the governance arrangements of the charity. These costs will normally include internal and external audit, legal advice for trustees and costs associated with constitutional and statutory requirements, for example the cost of trustee meetings and preparing statutory accounts.

Included within governance costs are any costs associated with the strategic as opposed to day-to-day management of the charity's activities. These costs will include any emoluments for trusteeship, the cost of charity employees involved in meetings with trustees and the cost of any administrative support provided to the trustees.

**Governing document** is a legal term and means any document that sets out the charity's purposes for the public benefit and how it is to operate. It may be a trust deed, constitution, memorandum and articles of association, scheme of the Commission, Royal Charter, conveyance or will.

**Government** includes government and inter-governmental agencies and similar bodies whether local, national or international.

**Grant income** is any voluntary income received by the charity (or other transfer of property) from a person or institution. The income or transfer may be for the general purposes of the charity, or for a specific purpose. It may be unconditional or be subject to conditions which, if not satisfied by the recipient charity, may lead to the grant property acquired with the aid of the grant or part of it being reclaimed by the grant-maker.

Entitlement to grant income may be subject to performance conditions, in which case it is classified as a performance-related grant and is recognised as the performance conditions are met.

**Grant payments** are any voluntary payments (or other transfer of property) in favour of a person or institution made by a charity in furtherance of its charitable aims. The payment or transfer may be for the general purposes of the recipient, or for some specific purpose such as the supply of a particular service. It may be unconditional, or be subject to conditions which, if not satisfied by the recipient, may lead to the grant, or property acquired with the aid of the grant or part of it being reclaimed by the charity.

A charity may make a performance-related grant, in which case it recognises its liability, as the goods or services specified in the grant terms are provided by the recipient.

## *Accounting and reporting by charities*

**Gross income** is a term defined in charity law and is used to determine the thresholds governing the requirements for accounts' scrutiny, the preparation of accruals accounts by non-company charities, submission of reports and accounts and any annual return to the charity regulator.

The definition of gross income may vary by jurisdiction. In relation to consolidated accounts, gross income is the gross income of the group after any adjustments arising from consolidation (e.g. intra-group sales).

**Group accounts** is an alternative term for consolidated accounts.

**Heritage assets** are tangible and intangible assets with historic, artistic, scientific, technological, geophysical or environmental qualities that are held and maintained principally for their contribution to knowledge and culture.

**Impact reporting** is the term used in this SORP to describe the difference a charity's work has made to the circumstances of its beneficiaries and, if practicable, any wider benefits to society as a whole.

**Inalienable asset** is an asset held by a charity which it must retain indefinitely. Inalienable assets have all of the following characteristics:

- The asset is retained indefinitely for a charity's own use and benefit to further its charitable aims.
- The charity is effectively prohibited from disposing of the asset without external consent.
- The asset, by its nature, will belong to a charity's restricted funds and, depending on the trusts attached to the asset, may be part of the permanent endowment.

Disposal without external consent could be prohibited by the charity's governing document, the donor's imposed conditions or in some other way. Normally, the asset will belong to the charity's 'permanent endowment', where it is held on trusts that contemplate its retention and continuing use but not its disposal.

However, in the case of a gift in kind of a 'wasting asset', such as a building, a long lease or a non-durable artefact, the terms of trust may not have provided for its maintenance in perpetuity or its replacement. In that case, the asset will be expended to the extent of the aggregate amount of its depreciation, properly provided for in the annual accounts (i.e. based on its currently anticipated useful life).

**Intangible assets** are non-financial fixed assets that do not have physical substance but are identifiable and are controlled by the entity through custody or legal rights.

**Investment management costs** include the costs of:

- portfolio management;
- obtaining investment advice;
- administration of the investments; and
- rent collection, property repairs and maintenance charges relating to investment properties.

**Investment property** is an interest in land and/or buildings:

- in respect of which construction work and development have been completed; and
- which is held for its investment potential, any rental income being negotiated at arm's length, but excluding:
  - a property that is owned and occupied by a company for its own purposes; and
  - a property let to and occupied by another group company.

**Key management personnel** are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of the charity. This definition includes trustees and those members of staff who are the senior management personnel to whom the trustees have delegated significant authority or responsibility in the day-to-day running of the charity.

**Larger charities** is a term used in the SORP to identify those charities subject to audit under charity law in their jurisdiction(s) of formation, registration or operation which the SORP requires to make additional reporting disclosures. In those jurisdictions where there is no charity law audit requirement, the reference to larger charities is construed as applying to those charities with a gross income exceeding £500,000 (UK) or €500,000 (Republic of Ireland) in the reporting period.

**Legal purposes** is the term used to describe what the charity has been established to do as set out in its governing document.

**Liability** is an accounting term for a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow of economic resources from the entity.

It includes an obligation of an entity to transfer economic benefits that results from a duty or responsibility obligating the entity either legally or practically (a constructive obligation), because it would be financially or otherwise operationally damaging to the entity not to discharge the duty or responsibility.

A moral obligation does not create a liability unless it meets the definition of a liability or the definition of a constructive obligation.

**Material** or **materiality** is an accounting test of what elements of information should be given in a particular set of accounts (financial statements). Omissions or misstatements of items are material if they could individually or collectively influence the economic decisions of users taken on the basis of the accounts.

Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor in identifying whether it is material.

Immaterial information will need to be excluded to avoid clutter that impairs the ability to understand other information provided. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects.

## *Accounting and reporting by charities*

Materiality is identified from a combination of factors, rather than any one in particular. The principal factors normally taken into account are:

- the item's size judged in the context of the accounts as a whole and the other information available to users that would affect their evaluation of the accounts (this includes, for example, considering how the item affects the evaluation of trends and similar considerations; and
- the item's nature in relation to:
  - the transactions or other events giving rise to it;
  - the legality, sensitivity, normality and potential consequences of the event or transaction;
  - the identity of the parties involved; and
  - the particular headings and disclosures that are affected.

If there are two or more similar items, the materiality of the items in aggregate as well as of the items individually needs to be considered.

The person preparing the accounts is responsible for deciding whether an item is material. This process may result in different materiality considerations being applied, depending on which aspect of the accounts is being considered. For example, there is a requirement for a high degree of accuracy in the case of certain disclosures, for example trustees' remuneration and expenses, which will override normal materiality considerations.

**Measurement** is the process of determining the monetary amounts at which the elements in the accounts are to be recognised and carried.

**Non-company charity** is any charity that has not been established as a company charity under company law. Non-company charities include unincorporated trusts or associations, charitable incorporated organisations and charities established by Royal Charter.

**Onerous contract** is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected under the contract.

**Performance-related grant** is the term used to describe a grant that has the characteristics similar to those of a contract, in that:

- the terms of the grant require the performance of a specified service that furthers the objectives of the grant-maker; and
- entitlement to the grant receivable is conditional on a specified output being provided by the grant recipient.

**Pooling scheme** is a class of Common Investment Fund that provides for the pooling of investments belonging to two or more charities (which may be special trusts) that are administered by the same trustee body as the body managing the pooling scheme. Such schemes are referred to as 'pool charities', and may be established with or without a formal scheme of the Charity Commission (England and Wales) or the courts.

## *Accounting and reporting by charities*

**Programme related investments** are a type of social investment and are made directly in pursuit of the charity's charitable purposes. The primary motivation for making a programme related investment is not for financial gain but to further the objects of the funding charity. Programme related investments can generate some financial return, and the funding may or may not be provided on commercial terms. Such investments could include loans to individual beneficiaries (such as for housing deposits) or to other charities (for example, in relation to regeneration projects).

**Provision** is an accounting term for a liability of uncertain timing or amount.

**Related parties** is a term used by the SORP that combines the requirements of charity law, company law and the Financial Reporting Standard for Smaller Entities (the FRSSE). The term is used to identify those persons or entities that are closely connected to the reporting charity or its trustees.

The following 'natural persons' are classed as related parties:

- A. any charity trustee and custodian trustee of the charity;
- B. a person who is the donor of any land to the charity (whether the gift was made on or after the establishment of the charity); and
- C. any person who is:
  - 1. a child, parent, grandchild, grandparent, brother or sister of any such trustee (A) or donor (B) of land;
  - 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. a person 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, who has control or joint control over the reporting charity; and
  - 6. a person, or a close member of that person's family, who has significant influence over the reporting 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.

A charity is not necessarily related to another charity simply because a particular person happens to be a trustee of both. It will only be 'related' if the relationship means that one charity, in furthering its charitable aims, is under the direction or control of the trustees of another charity.



## *Accounting and reporting by charities*

The following entities, which are not 'natural persons', are classed as related parties of a reporting entity (including a reporting charity) if any of the following conditions apply:

- the entity and the reporting charity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others);
- one entity is an associate or joint venture of the other entity (or an associate or joint venture of a group of which the other entity is a member);
- both entities are joint ventures of the same third entity;
- one entity is a joint venture of a third entity and the other entity is an associate of the third entity;
- the entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity;
- an entity that is controlled or jointly controlled by a person, or two or more persons, identified in A, B or C;
- an entity in which a person, or two or more such persons, identified in A, B or C, taken together, have a substantial interest or significant influence over the entity;

Control is presumed to exist when one or more persons identified in A, B or C, taken alone or together, hold directly or indirectly, more than half the voting power of an entity. However, control can also exist when they, directly or indirectly, control half or less than half of the voting power of an entity, if they have:

- power over more than half of the voting rights by virtue of agreement with other investors;
- the power to govern the financial and operating policies of the entity under a statute or an agreement;
- the power to appoint or remove the majority of the members of the board of directors or equivalent governing body, and control of the entity is by that board or body; or
- the power to cast the majority of votes at the meetings of the board of directors or equivalent governing body, and control of the entity is by that board or body.

An individual has a substantial interest or significant influence in an entity where that person, or two or more persons identified in A, B or C, taken together, have an interest in the equity share capital of that entity of a nominal value of more than one-fifth of that share capital, or is entitled to exercise, or control the exercise of, more than one-fifth of the voting power at any general meeting of that entity.

**Related party transactions** are the transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

**Reporting charity** is the charity preparing and filing the statutory annual report and accounts (financial statements) for itself and one or more connected (Scotland) or linked (England and Wales) charities or subsidiaries that it controls. The accounts of the reporting charity will combine any special trusts or connected or linked charities administered by the reporting charity. The accounts of the reporting charity will be consolidated where they include one or more subsidiaries.

## *Accounting and reporting by charities*

**Reporting date** is the last date of the charity's reporting period (its accounting period or financial year).

**Reporting period** is the accounting period (financial year) for the reporting charity. The reporting period, which is normally 12 months long, is the period of time over which the transactions of the charity are measured and reported in the accounts (financial statements).

**Reserves** - Refer to SORP module '**Trustees' annual report**'.

**Restricted funds** may be either endowment or restricted income funds, depending on the nature of the restriction. Where the fund is not an endowment fund and is held on trust for spending on specific purposes, it is known as a restricted income fund.

The resources (the assets and liabilities) of each restricted fund are held and maintained separately from other funds. This is in recognition of the circumstances in which the resources were originally received, and/or the restrictions on that fund that determine the way those resources are subsequently to be treated.

**Significant activities** are the activities that the trustees consider to be the main or the most important activities undertaken to further the charity's aims and objectives in the reporting period.

**Social investment** is a class of assets that comprises investments undertaken for both a financial return and to (in whole or part) further the investing charity's charitable aims and objectives.

**Social lotteries** are lotteries that are permitted by the law of the jurisdiction(s) in which the charity is fundraising and are not operated for private or commercial gain for a non-charitable purpose. The regulations applying to social lotteries normally have limitations on the amount of money that can be raised through the sale of tickets, and/or have specific requirements for registration or licensing. They may also set limits on the size of the prize or prize fund.

**Special trust** as defined in section 287 of the Charities Act 2011 (charities registered in England and Wales only) is property that 'is held and administered by or on behalf of a charity for any special purposes of the charity, and is so held or administered on separate trusts relating only to that property'. Whether registered or not, a distinguishing feature of special trusts is that they do not file a separate trustees' annual report and accounts. Instead, a reporting charity combines within its annual report and accounts the results of the special trusts it holds or administers as a component of the restricted funds it reports.

**Statement of financial activities (SoFA)**, analogous to a statement of comprehensive income, shows the charity's income, expenditure, gains and losses and transfers between funds during the reporting period (the financial year). The statement reconciles total funds brought forward and total funds carried forward at the end of the financial year.

**Stock** (also known as inventories) is assets which are:

- held for sale in the ordinary course of business;
- in the process of production for sale; or
- in the form of materials or supplies to be consumed in the production process or in the rendering or providing of services.

## *Accounting and reporting by charities*

**Support costs** are costs incurred to facilitate an activity. Unlike direct costs, which result directly from undertaking the activity, support costs do not change directly as a result of the activity undertaken. Support costs include the central or regional office functions, such as governance, general management, payroll administration, budgeting and accounting, information technology, human resources and finance.

**Total return** is an approach to investment management that allows trustees to manage investments without the need to take account of whether the return is income (dividends, interest, etc.) or capital gains (and losses). Refer to the SORP module '[Total return \(investments\)](#)' for more information.

**Trading** is an activity which has the 'badges of trade' that have been established by the courts. These are: profit-seeking motive; existing trade connections (linked or connected trading activity); repetition; method of finance (borrowing); interval between purchase and sale; selling organisation; method of acquisition (purchased for sale); operations pending sale (making it fit for sale); and the nature of the asset.

**Trustees** has the same meaning as charity trustees.

**Unrestricted fund** is a legal term for the unexpended resources held by a charity on trust, comprising money and other assets that can be used for any of the charitable aims of the charity. The use of unrestricted funds is not restricted to any particular charitable purpose of the charity.

## **Appendix 2: The Charity Accounting (SORP) Committee**

### **Membership**

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#### **Chair/Joint Chairs**

Andrew Hind, Chair (2006–10)  
Kirsty Gray, Deputy Chair (2006–09)  
Laura Anderson, Joint Chair (since 2010)  
Sam Younger, Joint Chair (since 2010)

#### **Observer members**

Mei Ashelford (since 2013)  
Caron Bradshaw (since 2011)  
Frances McCandless (since 2010)  
Alan O'Connor (2006–10)  
Joanna Spencer (2010–13)

#### **Members**

Debra Allcock-Tyler  
Tidi Adetokunbo Diyan  
Pesh Framjee  
Peter Gotham  
John Graham  
Chris Harris (2006–10)  
Keith Hickey  
Noel Hyndman  
Raymond Jones  
Tris Lumley  
Claire Newton (2006–07)  
Lynne Robb (2007–13)  
Carol Rudge  
Kate Sayer  
Catriona Scrimgeour  
Paul Spokes

#### **Secretariat**

Nigel Davies, Administrative & Technical Secretary

## **Appendix 3: Thresholds for the UK and the Republic of Ireland**

### **Thresholds for the use of the Financial Reporting Standard for Smaller Entities**

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A.1. Charities, including non-company charities that would qualify as a small company or small group, had they been incorporated in company law, may apply the FRSSE. Charities must refer to paragraphs 8 to 10 of the FRSSE to ensure they do not fall into the categories of entities excluded from applying the FRSSE, for example companies adopting the fair value rules of schedule D of Schedule 1 of Regulation 2008/409 to the Companies Act 2006 or charities that are engaged in certain regulated financial services activities. The thresholds defining small in the UK are set by the Companies Act 2006, section 382(3). A charity qualifies as small where any two of the following three criteria are met in both the current and preceding financial years:

- i) annual turnover (gross income for charities) not more than £6.5m;
- ii) balance sheet total not more than £3.26m; and
- iii) average number of employees not more than 50.

A group qualifies as small where any two of the following three criteria are met in both the current and preceding financial years:

- i) annual turnover (gross income for charities) not more than £6.5m (or £7.8m gross – before consolidation adjustments);
- ii) balance sheet total not more than £3.2m (or £3.9 m gross – before consolidation adjustments); and
- iii) average aggregate number of employees not more than 50.

Note: Charities produce an income and expenditure account and it is a condition of this SORP that charities adopting the FRSSE apply a 'gross income' threshold in place of the 'turnover' threshold applicable to for-profit companies that prepare a profit and loss account.

- A.2. For financial periods that are shorter or longer than 12 months, the 'turnover' and 'gross income' thresholds should be adjusted in proportion to the length of the financial period.
- A.3. The size parameters are subject to periodic amendment. The latest change in the UK was made in April 2008 by the Companies Act 2006 (Amendment) (Accounts and Reports) Regulations 2008, and applied to accounting (reporting) periods beginning on or after 6 April 2008.
- A.4. In the Republic of Ireland charitable companies are classed as public companies and cannot apply the FRSSE. However, non-company charities that meet the criteria set for small companies under the Companies Acts 1963-2009 may use the FRSSE provided two of the following three conditions are met:
- i) annual turnover (gross income for charities) not exceeding €8.8m;

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- ii) balance sheet total not exceeding €4.4m; and
  - iii) average number of employees not exceeding 50.
- A.5. The size parameters are subject to periodic amendment. The latest change in the Republic of Ireland was made by Statutory Instrument No. 304 of European Union (Accounts) Regulations 2012 which amended the amounts provided in Section 8 Companies (Amendment) Act 1986 and applies to accounting (reporting) periods ending on or after 3 August 2012.

### Threshold for the preparation of accruals accounts

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- A.6. Company charities, irrespective of size, must prepare accruals accounts that give a true and fair view. However, certain jurisdictions permit the trustees of smaller non-company charities to prepare their accounts on a receipts and payments basis, instead of preparing accounts on an accruals basis to give a true and fair view.
- A.7. In England and Wales, the threshold at which accruals accounts must be produced by non-company charities is a gross income of more than £250,000.
- A.8. In Scotland, the threshold at which accruals accounts must be produced by non-company charities is a gross income of £250,000 or more.
- A.9. In Northern Ireland, when section 64 of the Charities Act (Northern Ireland) 2008 is implemented, the threshold at which accruals accounts must be produced by non-company charities is a gross income of £100,000 or more. Currently, there are no form and content requirements for charity accounts in charity law; however, company charities must prepare accruals accounts giving a true and fair view.
- A.10. In the Republic of Ireland, the Charities Act 2009 has yet to be implemented. Prior to its implementation, there are no form and content requirements for charity accounts in charity law; however, company charities must prepare accruals accounts giving a true and fair view.

### Threshold for statutory audit

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- A.11. In England and Wales, an audit is required if either the charity's gross income exceeds £500,000 or its gross assets exceed £3.26m and gross income exceeds £250,000.
- A.12. In Scotland, an audit is required if either the charity's gross income is £500,000 or more or its gross assets exceed £3.26m and the charity has prepared accruals accounts.
- A.13. In Northern Ireland, once section 65 of the Charities Act (Northern Ireland) 2008 is implemented, the income threshold for audit will be gross income of £500,000. Currently, there is no charity law framework in effect for the audit of non-company charities. The audit of company charities is conducted under UK company law and the Companies (Northern Ireland) Order 1986.

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A.14. In the Republic of Ireland, section 50 of the Charities Act 2009, which provides for the minister to set an audit threshold of €500,000 (or less), has yet to be implemented. Consequently, there is no audit or reporting framework for non-company charities in charity law. Company charities must have an audit unless the company qualifies for an audit exemption. Since the threshold criteria for audit exemption set by the Companies (Amendment) Act 1986 did not apply to 'a company not trading for the acquisition of gain by the members', those company charities classed as public companies must be audited.

### **Threshold for the preparation of group accounts**

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- A.15. In England and Wales, any parent charity where the aggregate gross income of the group, the parent charity and its subsidiaries, exceeds £500,000 after consolidation adjustments must prepare group accounts. These group accounts are prepared in accordance with the Charities Act 2011 and applicable regulations. However, where a company charity is required by section 399 of the Companies Act 2006 to prepare group accounts, its group accounts are prepared under the Companies Act 2006.
- A.16. In Scotland, any parent charity where the aggregate gross income of the group, the parent charity and its subsidiaries, is £500,000 or more after consolidation adjustments must prepare group accounts. These group accounts are prepared in accordance with the Charities and Trustee Investment (Scotland) Act 2005 and applicable regulations. However, where a company charity is required by section 399 of the Companies Act 2006 to prepare group accounts, its group accounts are prepared under the Companies Act 2006.
- A.17. In Northern Ireland, schedule 6 to the Charities Act (Northern Ireland) 2008 has yet to be implemented, and the applicable regulations setting the income threshold for group accounts have not been made. Any parent company charity that does not fulfil the requirement for a small group under the Companies Act 2006 must prepare group accounts in accordance with company law requirements. It is best practice for a parent non-company charity to prepare group accounts where the combined income of the group would exceed the small group threshold.