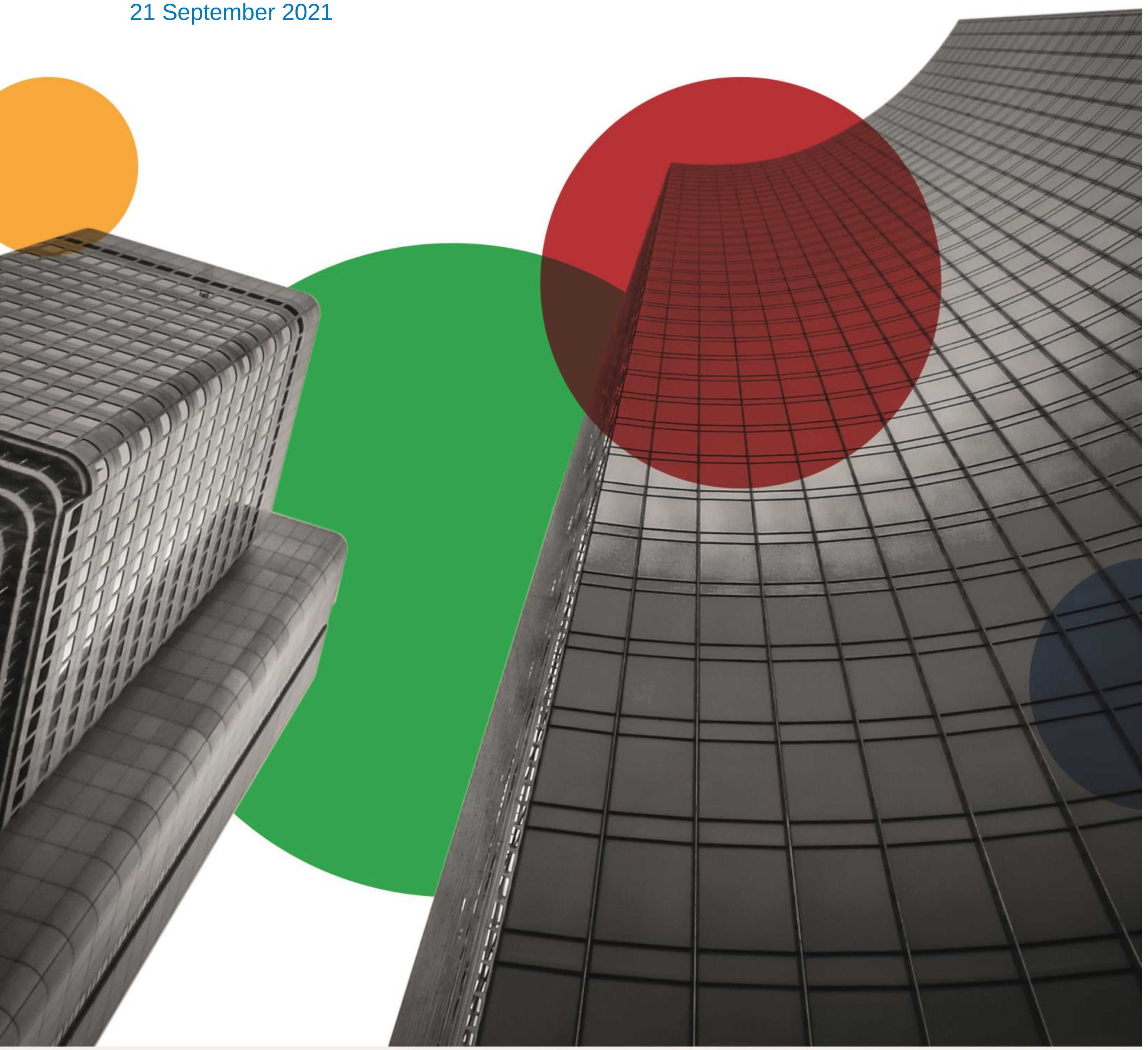
Part 2: Specific NPO financial reporting issues

Response from ICAS to the IFR4NPOs Initiative

21 September 2021



Introduction

ICAS is a professional body for more than 22,000 world class businesspeople who work in the UK and in more than 100 countries around the world. Our members have all achieved the internationally recognised and respected CA qualification (Chartered Accountant). We are an educator, examiner, regulator, and thought leader.

Almost two thirds of our working membership work in business; many leading some of the UK's and the world's great companies. The others work in accountancy practices ranging from the Big Four in the City to the small practitioner in rural areas of the country.

We currently have over 4,000 students striving to become the next generation of CAs under the tutelage of our expert staff and members. We regulate our members and their firms. We represent our members on a wide range of issues in accountancy, finance and business and seek to influence policy in the UK and globally, always acting in the public interest.

ICAS was created by Royal Charter in 1854.

General comments

The ICAS Charities Panel welcomes the opportunity to comment on the second consultation conducted by the International Financial Reporting for Not-for-Profit Organisations (IFR4NPOs) Initiative which considers specific financial reporting issues likely to fall within formal Guidance for Not-for-Profit Organisations (NPOs).

In our response to the first consultation we expressed our support for using the International Financial Reporting Standard for Small and Medium-sized Entities (the IFRS for SMEs) as the basis of the Guidance to be developed as part of the Initiative. Our view on this is further reflected in our responses to the consultation questions.

We have not responded to all the issues covered by the second consultation and while we agree that all the topics covered are important, we selected the following issues we believe to be of the highest priority:

- The reporting entity and control.
- Non-exchange revenue.
- Accounting for outgoing resources (expenses and liabilities).
- Inventory held for use or distribution.
- Presentation of financial statements (including fund accounting).

In our response to the first consultation we highlighted the importance of considering the guidance needs of smaller or less complex entities where the availability of concessions may encourage adoption of the final NPO Guidance.

We believe that disclosure concessions for smaller or less complex entities would likely form the bulk of any concessions given, followed by presentation, with recognition and measurement concessions being rarer. In this response our focus has been largely on recognition and measurement requirements and we have not identified any specific concessions for smaller or less complex entities. However, we would urge that potential concessions are identified at an early stage and that the topic of tiering is addressed in the exposure draft which will follow in due course.

Included in the Annex are details of the information requested from all participants and we set out our responses to the consultation questions on our five selected topics below.

Responses to specific matters for comment

Section 1, issue 1: the reporting entity and control
1.a. Do you agree with the description of issue 1: reporting entity and control (including branches)? If not, why not?

1.b. Do you agree that the list of alternative treatments that should be considered for issue 1 is exhaustive? If not, please describe your additional proposed alternatives, and explain why these should be considered?

1.c. Do you agree with the advantages and disadvantages articulated for each alternative accounting treatment for issue 1? If you do not agree, please set out the changes you propose, and why these should be made?

1.d. Please identify the alternative view that you favour for issue 1, and the reasons for your view?

Response to specific matter for comment 1
In our response to Part 1 of the consultation we stated that we support an approach to NPO Guidance which is based on the IFRS for SMEs. Therefore, we support an approach in relation to the issue of the reporting entity and control which is based on the IFRS for SMEs. We recognise that additional material within the Guidance will need to be provided so that parent NPOs can determine the entities they control and address the financial reporting implications accordingly.

We highlighted in our response to Part 1 that more guidance is required on defining the 'reporting entity'. This is necessary first step for accounts preparers prior to being able to identify entities controlled by the reporting entity.

The Conceptual Framework for Financial Reporting issued by the International Accounting Standards Board provides commentary on the reporting entity and its boundary. Given that the NPO Guidance will not be underpinned by its own conceptual framework and the complex structure of some NPOs, it will be necessary to provide guidance on the reporting entity and its boundary, in addition to providing a definition of control.

Branches, by their nature, certainly in the UK, are not considered to be reporting entities in their own right. Therefore, we believe that guidance regarding branches will need to be included within the scope of material on the reporting entity and its boundary, separate from the definition of control of other entities.

We have a preference for alternative 1 which is preparing NPO-specific guidance on the nature of reporting entities and the use of the principles-based approach of substance over form to define control.

Section 2, issue 3: non-exchange revenue
3.a. Do you agree with the description of issue 3: non-exchange revenue? If not, why not?

3.b. Do you agree that the list of alternative treatments that should be considered for issue 3 is exhaustive? If not, please describe your additional proposed practical alternative, and explain why they should be considered.

3.c. Do you agree with the advantages and disadvantages articulated for each alternative accounting treatment for issue 3? If you do not agree, please set out the changes you propose, and why these should be made.

3.d. Please identify the alternative treatment that you favour for issue 3, and the reasons for your view.

3.e. If you consider an alternative other than alternative 4 for issue 3, do you consider that the exceptions to the recognition and measurement of gifts in-kind and services in-kind should be available under your preferred option?

3.f. Are there any practical consideration, for example, impacts on tax or audit threshold, or questions that arise from implementing your preferred option for issue 3?

Response to specific matter for comment 3
We support alternative 1 as the basis for developing guidance for NPOs on the recognition of revenue from non-exchange transactions. This approach will mean that the recognition and measurement principles and the requirements on accounting for government grants in the IFRS for SMEs will form the basis of guidance on this important topic.

ICAS is involved in the UK's Charities SORP development process and as part of our participation in this process we have considered the following matters which fall within the scope of issue 3:

- Grant income from government and other sources.
- Donations in kind (Donated goods for resale, donated goods for onward distribution to beneficiaries, donated goods for own use, donated property plant and equipment, and donated services and facilities).
- Income from other non-exchange transactions (for example, pledges and membership fees).

Guidance for NPOs will need to be capable of applying to all of the above and it will be necessary to provide additional guidance beyond the material in the IFRS for SMEs.

We note that the recognition of legacy/ bequest income and endowments are outside the scope of topic 3 and may be addressed in a later phase of the project.

Grants
Section 24 of the IFRS for SMEs requires entities to recognise government grants using a method known in the UK as 'the performance model' and UK charities are required to apply this method of accounting to all grants, including non-government grants. This approach to accounting also means that there is currently no requirement to distinguish between revenue and capital grants, as income is recognised in the statement of financial performance when the recognition criteria are met.

There is not universal support for this method of accounting in the UK as it can lead to charities recognising income which they have not yet received and where related activity will not take place until a future reporting period. This can give the impression that an entity's financial health is stronger than it actually is, with the reverse being true in future accounting periods where there is related expenditure but no related income. Non-performance related conditions are implicit in the IFRS for SMEs (paragraph 24.4a)) but it will likely be necessary for this matter to be dealt with explicitly in the NPO Guidance, including time-related conditions linked to multi-year grants.

Another concern expressed in the UK about this method of accounting is the treatment of capital grants. Like the recognition of revenue grants without conditions attached, a capital grant is normally recognised in full in the statement of financial performance on receipt. This can create volatility in an entity's financial statements which may also appear to give a false impression of its financial health. However, we are aware that this method of accounting for capital grants is likely to be supported by grant funders. This means that robust presentation and disclosure requirements about capital grants are needed to ensure that users of NPO financial statements understand the impact of capital grants on the NPO's finances.

The IFRS for SMEs is silent on the treatment of non-government grants. As a standard designed for profit orientated entities, grants from other sources have not been considered. This may be due to the fact that these would lack economic substance in the commercial world. However, it is difficult to see an argument that government and non-government grants should be accounted for differently by an NPO.

Key points
Our key points on grants are as follows:

- We believe that it will be necessary to deal explicitly with non-performance related conditions in the NPO Guidance, including time-related conditions. This will ameliorate the risk of grant income being overstated and an NPO flipflopping in and out of audit.
- Grants for the purchase of property, plant and equipment i.e. capital grants should be distinguished from revenue grants for presentation and disclosure purposes. This will improve user understanding of the financial statements. This point is also relevant to issue 7 on financial statement presentation.
- Accounting guidance for government and non-government grants should be the same to ensure consistency and comparability.

Donations in kind
We can see that going back to Section 2 of the IFRS for SMEs on concepts and pervasive principles could give rise to donations in kind being recognised in NPO financial statements.

However, this is an area which has caused practical challenges for UK charities. These challenges fall largely around the reliable measurement of donations in kind, the practicalities of measurement and the cost benefit of measurement.

We have the following points to make:

- Donated goods for resale. Inventories are normally recognised at the lower of cost or net realisable value (i.e. estimated selling price less costs to complete or sell). In the case of donated goods, cost is 'nil'. Their only value to an NPO is at the point of sale – such goods would not be replaced if they were lost and are not normally insurable. There are also practical problems in measuring these at fair value. However, recognising income at the point of sale should be straightforward.
- Donated goods for onward distribution. Similar to the above but we recognise that for some charities, such as Non-governmental Organisations (NGOs), donated goods for onward distribution could be significant and it is perhaps preferable to recognise these at fair value, where 'fair value' is the cost to the donor. This will only be feasible where the cost to the donor is known.
- Donated goods for own use. These would be donated goods which are not capitalised and we would favour these being dealt with through disclosure rather than recognition, where these are material.
- Donated property, plant and equipment. There could be significant measurement challenges around the recognition of such assets. However, it should, in most instances, be possible to establish a fair value for land and buildings (other than heritage assets which are outside the scope of issue 3).
- Donated services and facilities. We do not believe that it is appropriate for NPOs to recognise donated services and facilities. In the UK, charities are required to value these at 'value to the charity' as cost or fair value are not believed to be suitable measures. It is likely that an NPO would not purchase services and facilities equivalent to those which have been donated on the grounds of affordability so establishing a reliable value is very problematic.

Key points
Our key points on donations in kind are as follows:

- Our starting premise is that donations in kind should not be recognised on the grounds that these have no cost and that it is not normally practical to value these reliably and, where it is practical, the cost of doing so is likely to outweigh any corresponding benefits.
- A disbenefit, could be to push an NPO into an audit due to having to recognise income related to donations in kind.
- Robust disclosures should be required about any 'material' donations in kind not recognised in the financial statements. This applies to volunteer time. We accept that assessing what is material is a challenge especially for items which do not have a monetary value placed on them.
- Income from goods donated for resale should be recognised at the point of sale.

- Consideration should be given to recognising donated goods for onward distribution at fair value at the point of receipt where the cost to the donor is known. 'Cost to the donor' being a proxy for fair value.
- Donated land and buildings should be recognised at fair value. Fair value being 'deemed cost' where the NPO does not adopt a policy of revaluation for land and buildings.

Income from other non-exchange transactions
Recognition and measurement requirements should follow Section 2 of the IFRS for SMEs. We envisage that any income would be measured on the basis of its monetary value.

Care should be taken to ensure that promises are not recognised as income. For example, this issue has arisen in the UK where pledged donations are recognised but quite frequently do not come to fruition and are written back in the next reporting period. We are aware of charities seeking pledges near the end of their reporting period and this indicates that pledges may be being sought to give the impression that the charity's finances are stronger than they are.

Membership fees are an example of a type of income which has both an exchange and a non-exchange element. The following are aspects of transactions which have two elements which need to be considered in developing guidance for NPOs:

- How should such transactions be presented in the statement of financial performance? Should there be a split presentation?
- If so, what criteria should charities use to identify the exchange and non-exchange elements?
- Any tax relief available on the non-exchange element from a country's tax authorities may have a bearing on the presentation of such transactions.
- Materiality should be a factor in the classification of such transactions.

Key points
Key points on income from other non-exchange transactions:

- Care should be taken to ensure that the criteria for the recognition of income and specifically non-exchange income excludes income which is promised but where the NPO has no means to enforce payment by the potential donor.
- Consideration should be given as to how NPOs should report on transactions which have both an exchange and non-exchange element. This point links to issue 7 on financial statement presentation.

Section 3, issue 4: accounting for grant expenses
4.a. Do you agree with the description of issue 4: grant expenses? If not, why not?

4.b. Do you agree that the list of alternative treatments that should be considered for issue 4 is exhaustive? If not, please describe your additional proposed alternatives, and explain why they should be considered.

4.c. Do you agree with the advantages and disadvantages articulated for each alternative accounting treatment for issue 4? If you do not agree, please set out the changes you propose, and why these should be made.

4.d. Please identify the alternative treatment that you favour for issue 4, and the reasons for your view.

Response to specific matter for comment 4
We support alternative 1 for accounting for grant expenses, guidance based on the concepts and pervasive principles of the IFRS for SMEs, including additional guidance on recognition, measurement and disclosure.

We believe that the following requirements on liabilities and expenses in the IFRS for SMEs illustrate that it will provide a sound principles-based approach for the recognition of grant related liabilities and expenses:

"**Financial position**

Liabilities

2.20. An essential characteristic of a liability is that the entity has a present obligation to act or perform in a particular way. The obligation may be either a legal obligation or a constructive obligation. A legal obligation is legally enforceable as a consequence of a binding contract or statutory requirement. A constructive obligation is an obligation that derives from an entity's actions when:

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

2.21. The settlement of a present obligation usually involves the payment of cash, the transfer of other assets, the provision of services, the replacement of that obligation with another obligation or the conversion of the obligation to equity. An obligation may also be extinguished by other means, such as a creditor waiving or forfeiting its rights.

Recognition in financial statements

Liabilities

2.39. An entity shall recognise a liability in the statement of financial position when:

a) the entity has an obligation at the end of the reporting period as a result of a past event;
b) it is probable that the entity will be required to transfer resources embodying economic benefits in settlement; and
c) the settlement amount can be measured reliably.

2.40. A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 2.39. An entity shall not recognise a contingent liability as a liability, except for contingent liabilities of an acquiree in a business combination.

Expenses

2.42. The recognition of expenses results directly from the recognition and measurement of assets and liabilities. An entity shall recognise expenses in the statement of comprehensive income (or in the income statement, if presented) when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably."

Alternative 2, which would draw on IPSASB's proposals on transfer expenses with performance obligations (ED 72), may introduce additional complexity. While more prescription may create consistency of practice, clear principles-based guidance with scope for professional judgement may give NPOs in different jurisdictions the ability to apply the guidance to a broader range of circumstances, including any not currently envisaged.

Paragraph 2.21 of the IFRS for SMEs on the settlement of an obligation will need to be adapted to the treatment of grant expenses.

It is important that guidance on accounting for outgoing resources deals with the following circumstances:

- Funding with no conditions attached.
- Funding with performance related conditions attached.
- Funding with non-performance related conditions attached.

The analysis of alternative 1 (on page 122) does not specifically mention non-performance related conditions, and it is really vital that these are dealt with in the NPO Guidance. For the treatment of multi-year grants, this is especially important.

It is likely that there will be conditions within funding agreements which do not prevent the recognition by the donor (the grantor) of grant expenses. While it will not be possible for the NPO Guidance to provide absolute clarity about whether or not a non-performance related condition is sufficient to prevent recognition, every effort should be made to set out guidance on this matter. This will reduce the risk that donors will place onerous non-performance related conditions on grant recipients merely to avoid recognition and which are not necessary for their own purposes.

Donor imposed time-related conditions are likely to be a feature of multi-year grant awards. While we believe that clearly specified time-related conditions would normally prevent a grant recipient from recognising grant income relating to future reporting periods, we do not believe that the existence of a time-related condition alone is sufficient to prevent the donor from recognising a related grant expense and liability. This means that for multi-year grants where the only conditions are time-related, the accounting treatment by the donor cannot be the mirror image of a recipient NPO which is also following the NPO Guidance.

Key points
Our key points on grant expenses are therefore as follows:

- The NPO Guidance should take a principles-based approach to guidance on the recognition of grant expenses and related liabilities.
- Guidance on non-performance related conditions should be prominent to help donors assess if a non-performance related condition is meaningful i.e. prevents recognition of an expense and liability until the condition is fulfilled. If more than one non-performance related condition is imposed, all conditions would need to be fulfilled prior to recognition.
- Time-related conditions should not prevent the recognition of a multi-year grant by the donor.

Section 4, issue 6: inventory held for use or distribution
6.a. Do you agree with the description of issue 6: inventory held for use or onward distribution? If not, why not?

6.b. Do you agree that the list of alternative treatments that should be considered for issue 6 is exhaustive? If not, please describe your additional proposed alternatives, and explain why these should be considered?

6.c. Do you agree with the advantages and disadvantages articulated for each alternative accounting treatment for issue 6? If you do not agree, please set out the changes you propose, and why these should be made?

6.d. Please identify the alternative view that you favour for issue 6, and the reasons for your view?

Response to specific matter for comment 6
We support alternative 1 for the treatment of inventory held for use or distribution with additional guidance.

We comment on specific aspects of accounting for inventories held for use or distribution in our comments on issue 3: non-exchange revenue.

In summary, we believe the following approaches are appropriate for the following donated items we refer to in our comments on issue 3:

- Donated goods for resale. Income from donated goods held for resale should be recognised at the point of sale. Donations should be recorded at cost at the point of receipt which is 'nil'.

- Donated goods for onward distribution. Consideration should be given to requiring goods for onward distribution to be recognised initially at 'fair value' where their fair value is cost to the donor. If 'cost to the donor' is not known, then recognition should not be required, primarily on the grounds of measurement uncertainty. We recognise that where goods are measured at fair value, it will be necessary to recognise any impairment losses at the reporting date.
- Donated goods for own use. Donated goods for own use should not be recognised.

We also support the proposal included in alternatives 2 and 3 to permit work in progress of services to be provided at no or nominal cost to be expensed as incurred. We recognise that an accounting policy choice is being given and that could lead to a lack of comparability. However, on the grounds that work in progress may be difficult to value in these circumstances, we believe that this is a necessary concession.

We believe that there are significant practical challenges in reliably measuring donated goods/ inventories, including work in progress provided at no or nominal cost to the recipient and that the cost of measuring such items could be likely to outweigh the benefits.

We appreciate that recognising such assets in the balance sheet would give NPOs a means to demonstrate their stewardship of those assets. However, as referenced in the consultation paper at paragraph 2.6 (on page 140), NPOs may not have an inventory control system in place or even basic inventory records. The prospect of having to fair value donated inventories under the NPO Guidance if they improve their recording keeping, systems and internal controls may deter rather than encourage NPOs to make improvements.

Our preferred approach to donated goods/ inventories would reduce the need to assess materiality in relation to their recognition. However, materiality will need to be applied in relation to the disclosure of goods donated for resale, donated goods for onward distribution and donated goods for own use. Disclosure requirements could be a proportionate means of encouraging improvements in record keeping.

Key points
Our key points on inventories are therefore as follows:

- Guidance on purchased inventories and the cost of own produced inventories should follow the requirements of the IFRS for SMEs.
- Where inventories are donated, recognition should only be required or permitted in specific limited circumstances.
- Disclosures should be developed where donated inventories are material to the NPO. Disclosure requirements could encourage improvements in record keeping.
- NPOs should have an accounting policy choice as to whether to recognise or expense work in progress for services provide for nil or nominal cost.

Section 5, issue 7: presentation of financial statements (including fund accounting)
7.a. Do you agree with the description of issue 7: financial statement presentation? If not, why not?

7.b. Do you agree that the list of alternative treatments that should be considered for issue 7 is exhaustive? If not, please describe your additional proposed alternatives, and explain why these should be considered?

7.c. Do you agree with the advantages and disadvantages articulated for each alternative accounting treatment for issue 7? If you do not agree, please set out the changes you propose, and why these should be made?

7.d. Please identify the alternative view that you favour for issue 7, and the reasons for your view? In your response please consider the presentation of unrestricted reserves allocated for internal purposes.

7.e. The term statement of financial performance is used in the consultation paper to describe the statement that contains an NPO's revenues and expenses. Do you agree with the use of this term? If not, describe your preferred term and explain your reasoning.

Response to specific matter for comment 7
In the UK, the form and content of financial statements (primary statements and notes) for companies and Limited Liability Partnerships is set out in detail by law, in secondary legislation (regulations). For non-specialist charities (depending on the charity law jurisdiction(s) they operate in and their legal form), the form and content of their financial statements is determined to varying degrees by law and through the Charities Statement of Recommended Practice (SORP) which an interpretation of Financial Reporting Standard 102 (applicable in the UK and the Republic of Ireland), which itself is based on the IFRS for SMEs. In practice, the form and content of the financial statements of non-specialist charities across the UK is driven by the Charities SORP, with some additional requirements for charitable companies that arise from company law.

The importance of flexibility
Why is this important? It is therefore likely that the form and content of NPO financial statements, more than any other aspect of financial reporting requirements/ guidance, is determined by a country's laws and regulations.

This means that the NPO Guidance will need to be sufficiently flexible to accommodate country requirements, as being too prescriptive could jeopardise the ability of NPOs to adopt the NPO Guidance or to state that they had adopted it.

Alternative 2
With this in mind (and in response to part of question 7d) we believe that the IFRS for SMEs should form the basis of guidance for NPOs on financial statement presentation. Therefore we support alternative 2.

Fund accounting
As a general point, the inclusion of fund accounting will have implications for comparative information. Under the UK's FRS 102 (which charities applying the Charities SORP must also comply with), comparatives must be provided unless these are specifically highlighted as not being required. Fund accounting has given rise to charities having to provide additional comparative information which has led to financial statements being lengthy and questions being raised about the value of some comparatives, especially as the previous year's financial statements are normally available. Therefore, we recommend that if fund accounting is introduced, that requirements to provide comparatives are clear and proportionate. One area where it may be appropriate to dispense with comparatives is the provision of comparatives for movements in funds, similar to the approach taken, for example, to the presentation of the property, plant and equipment in the notes (see Section 17 of the IFRS for SMEs).

Reserves policy and calculating reserves
Alternative 2 requires the disclosure of policies regarding the management of reserves. The management of reserves is a financial management issue rather than a financial reporting issue and we believe that where an NPO has a reserves policy that it should be set out in the NPO's narrative report. It is not the place of guidance on financial reporting to require NPOs to have a reserves policy, even though it is highly desirable that they have one.

Some NPOs may not have reserves. It is important that guidance on disclosing a reserves policy is worded so that it is understood that there is a difference between having a policy of not holding reserves, not having a policy on holding reserves and not having reserves.

We are supportive of NPOs having to calculate their 'free' reserves, i.e. those reserves available to spend at their own discretion, within the bounds of their founding documents or the applicable law. There are several different approaches available to presenting this calculation, for example:

- A disclosure in the narrative report where the policy on holding reserves and performance against that policy is reported.
- A note to the financial statements.

- A primary financial statement, perhaps combined to include funds as well as reserves.
- Disclosure at the bottom of the statement of financial position.
- Presentation as part of the statement of financial position.

Perhaps the approach which would fit best with limiting undue specialisation would be to include a note to the financial statements. Care will need to be taken to ensure that the note is sufficiently prominent. If NPOs are required to document their policy on holding reserves, if they have one, and their performance against that policy in their narrative report, then the calculated reserves figure will also be included in that narrative report: this may provide a suitable level of prominence. In addition, any funds set aside by management for a specific purpose should be disclosed and explained in the narrative report rather than the financial statements. (This point specifically addresses part of question 7d).

We recommend that a definition of 'free' reserves is included in the NPO Guidance and that guidance is provided on how to calculate these. The consultation paper refers to unrestricted reserves. This could be a conflation between unrestricted funds and 'free' reserves as there will likely be reconciling items to take into consideration when calculating 'free' reserves from unrestricted funds, for example, property, plant and equipment not held in a restricted fund. There is a general point to be made here about the use of terms and the importance of defining these in a glossary.

Regarding the consultation question on the use of the term 'statement of financial performance', we support the use of this term in the NPO Guidance. As NPOs are unlikely to have the choice, under the Guidance, between providing a statement of comprehensive income or an income statement, it makes sense to depart from the IFRS for SMEs' use of terminology in this instance. However, we recommend that the NPO guidance gives NPOs the flexibility to use different terms to describe their primary statements so that any local requirements can be complied with. (This point specifically addresses question 7e).

Other financial statement presentation matters
Earlier in our response we have raised the following two matters relevant to the presentation of financial statements:

- Capital grants should be distinguished from revenue grants for presentation and disclosure purposes.
- Consideration should be given as to how NPOs should report on transactions which have both an exchange and non-exchange element.

Key points
Our key point on financial statement presentation are therefore as follows:

- The NPO Guidance on financial statement presentation will need to be flexible so that country specific requirements can be met while still enabling NPOs to say that they have prepared their financial statements in accordance with the Guidance. This includes being able to use a different name for the 'statement of financial performance'.
- We are familiar with fund accounting in the UK and without clear proposals on a viable alternative approach, we support this approach for the NPO Guidance.
- The reporting of reserves policies and performance against reserves policies should be dealt with in NPO narrative reports as these are not financial reporting matters. This includes the reporting of any element of 'free' reserves set aside by management for a specific purpose.
- NPO's should be required to demonstrate, by way of a note to the financial statements, how they have calculated their 'free' reserves. The NPO Guidance should define 'free' reserves in its glossary of terms.

Annex

Information requested from all participants

Name: Christine Scott, Head of Charities and Pensions at ICAS, the Institute of Chartered Accountants of Scotland.

Email address: cscott@icas.com.

Description of the activities of the organisation responding to the consultation:
ICAS is a professional accountancy body based in the UK. Responding to this consultation on behalf of ICAS is the ICAS Charities Panel. Further information about ICAS is included in the 'Background' section of our response.

Jurisdiction(s) to which the feedback relates:
Our feedback primarily relates to our experience of NPO accounting in the UK, mainly charities. Financial reporting requirements for NPOs preparing their financial statements using an accruals-based framework is set at UK level. However, there are sub-UK level differences in respect of legal requirements for NPOs which have a bearing on their financial reporting obligations.

In our response, we have also thought about how accruals-based standards could be applied in jurisdictions where there is currently no NPO financial reporting framework.

Accounting basis of NPO financial reports in the jurisdiction in which you mainly work:
Both modified cash and accruals-based, depending on entity size and other criteria, such as company law.

Financial Reporting Standards used by NPOs in the jurisdiction in which you mainly work:
Accruals-based requirements for UK NPOs are based on the IFRS for SMEs, adopted and tailored as appropriate by FRS 102: the Financial Reporting Standard applicable in the UK and Republic of Ireland. Further specialist requirements apply over and above FRS 102 and the Public Benefit Entity requirements which are included within its scope.

Receipts and payments financial statements requirements for charities are charity jurisdiction specific but all require charities to disclose assets and liabilities.

There are three statements of recommended practice (SORPs) which apply to the financial statements of NPOs in the UK, where the body is required to prepare financial statements using an accruals-based framework, covering:

- Housing bodies.
- Higher and further educational institutions.
- Charities (which are not housing bodies or educational institutions).

SORPs are described as recommended practice but to a large extent compliance with a sector specific SORP is required by law and, where it is not required by law, compliance is considered necessary for financial statements to give a true and fair view.

ICAS is currently involved in the Charities SORP development process: a new process for revising the Charities SORP, which is running alongside the UK Financial Reporting Council's periodic review of FRS 102.

Please indicate whether you wish to receive further information about this project and consent to being contacted at the email address provided:
Agreed. The ICAS Charities Panel also agrees that its response to this consultation can be made public.

Contact us

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