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Dear Michelle,

British Red Cross' response to revised proposals for the future of financial reporting (FREDs 46, 47 & 48)

We welcome the opportunity to comment on the revised proposals for the future of financial reporting (FREDs 46, 47 & 48). We are broadly supportive of the latest proposals but we still have a few significant concerns about the impact of these proposals on financial reporting in the charity sector.

We are pleased that the ASB has taken into account previous feedback and have updated the proposals accordingly. In particular, we are glad that the valuation of donated stock and accounting for volunteer time, which were areas of concern to us, have now been addressed and the impracticalities of accounting for them have been recognised.

We have structured this letter to address the issues that cause us concern, rather than addressing the individual consultation questions.

Performance conditions

Under the current rules, charities generally recognise grants and donations for restricted purposes with repayment clauses as income on receipt. The proposals appear to require charities to recognise such donations as deferred, until they have been used as specified. The probability of repayment of such grants and donations is generally very small and we believe the accounting treatment should reflect probability of repayment, rather than the strict legal form of whether the donor agreement contains a repayment clause or not.



Protective emblems used by
the International Red Cross
and Red Crescent Movement

The British Red Cross Society
Incorporated by Royal Charter 1908
Registered charity numbers:
England and Wales: 220949
Scotland: SC037738

Patron: Her Majesty The Queen

It is unclear in the proposals if grants and donations that have been deferred can be recognised during the period as performance conditions are met (e.g. matched with expenditure) or not at all until after the performance conditions are fully met (e.g. all the money is spent).

Definition of restrictions

“Restriction” is already an established and widely-used term in the charity sector and this is well understood by charities and donors. We are concerned that the definition included in the proposal will likely cause confusion. For example, the proposal’s definition of restriction specifically excludes resources with a repayment clause, whereas existing practice includes such resources with a repayment clause, which have to be spent on specific purposes, as restricted.

Where a grant or donation is received with a restriction but without repayment conditions attached, then trust law would often require that repayment is made if the money was not spent in line with the restriction. As a result, there is currently confusion whether such income should be recognised as restricted income or should be considered to have performance conditions attached to it and therefore not recognised until spent.

Liability for repayment of income

The standard requires that a liability be recognised when repayment becomes probable due to a failure to meet performance conditions. It would appear that the only effect of this would be to reallocate an existing liability, as the income should have been deferred until the performance conditions were met. We recommend that the wording be amended to provide clarification.

Funding commitments

When funding commitments are made, it appears unlikely that liabilities will be recognised in most cases. If there is a condition requiring repayment for non-compliance, then no liability is created when the commitment is made. Given that the probability of repayment is often very low, it is arguable that a liability should be created.

Where funding is given in advance of performance conditions being met, it appears that the expenditure would have to be treated as an asset, like a prepayment. However, the funder has little or no control over that money other than the performance condition and likely no expectation of the money being repaid or any other economic benefit. It is questionable how this would meet the definition of an asset.

Legacies

We would appreciate clearer guidance on when it is possible to recognise legacy income. We believe that the certainty and reliability criteria can often be satisfied before the finalisation of the probate process. Currently, we review our legacies on a case by case basis and accrue where we consider there to be sufficient evidence. The decision to accrue can be based on interim accounts or other information about the case.



Related party transactions

Under the current charity SORP, there is an exemption not to disclose donations received from related parties. There is no such exemption in the proposals. Provided the donation is unrestricted or part of a general appeal, it will not change the operations of a charity but the disclosure requirement may prevent such donations being made in the first place.

Please call me on 0845 054 7311 if you would like to discuss any of our responses.

Yours faithfully,

Ewan Aitchison
Financial accountant