



## Accounts Monitoring Review

# Do charity annual reports and accounts meet the reader's needs?

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### Summary

The purpose of the trustees' annual report and accounts is to tell the reader what the charity is set up to do, what it achieved and how it spent its money. Three quarters of a sample of 107 sets of charity accounts filed with us provided basic information on charitable activities. They showed how the trustees had used the charity's money and included either an audit or independent examination report. A quarter of charities failed to provide this basic information and fell well short of the standard the public has every right to expect. The main reasons why these sets of accounts failed to meet our basic standard were that either the annual report did not explain the charity's activities to achieve its objectives or that the accounts did not balance or were incomplete.

### About our accounts monitoring reports

Charities' accounts are publicly available on **GOV.UK**. Each year, we monitor a sample to check compliance with the Charities Statement of Recommended Practice (SORP) and to identify issues of regulatory concern. We are publishing a series of reports on our findings, which will help trustees to manage the risks that their charity faces, improve reporting standards and enhance the accountability of charities to their donors, beneficiaries and the public.

### Why are we reviewing charities' accounts?

All registered charities with an annual income over £25,000 are required to file the following documents with us within 10 months of their financial year end:

- their trustees' annual report (annual report)
- the report of an independent scrutiny of their accounts
- their accounts

We are reviewing charities' sets of accounts because they are the prime means by which the trustees are publicly accountable to donors, beneficiaries and the wider public for the charity's activities and how they have used the charity's money. Good reporting is important to public trust and confidence in both the reporting charity and the wider charity sector.

## How do we assess whether accounts meet the needs of readers?

The focus of our assessment was on whether each set of accounts met the basic requirements of the users of those accounts rather than on strict technical compliance with the SORP and other reporting requirements. We based our view of the user's requirements on the Populus survey of public trust and confidence (June 2016). Populus found that 'ensuring that a reasonable proportion of donations make it to the end cause' and 'make a positive difference to the cause they work for' remain the most important factors driving public trust and confidence in charities. Populus also concluded that the public 'show a clear preference for charities that satisfy their needs for transparency and impact'.

This led us to focus on the following criteria:

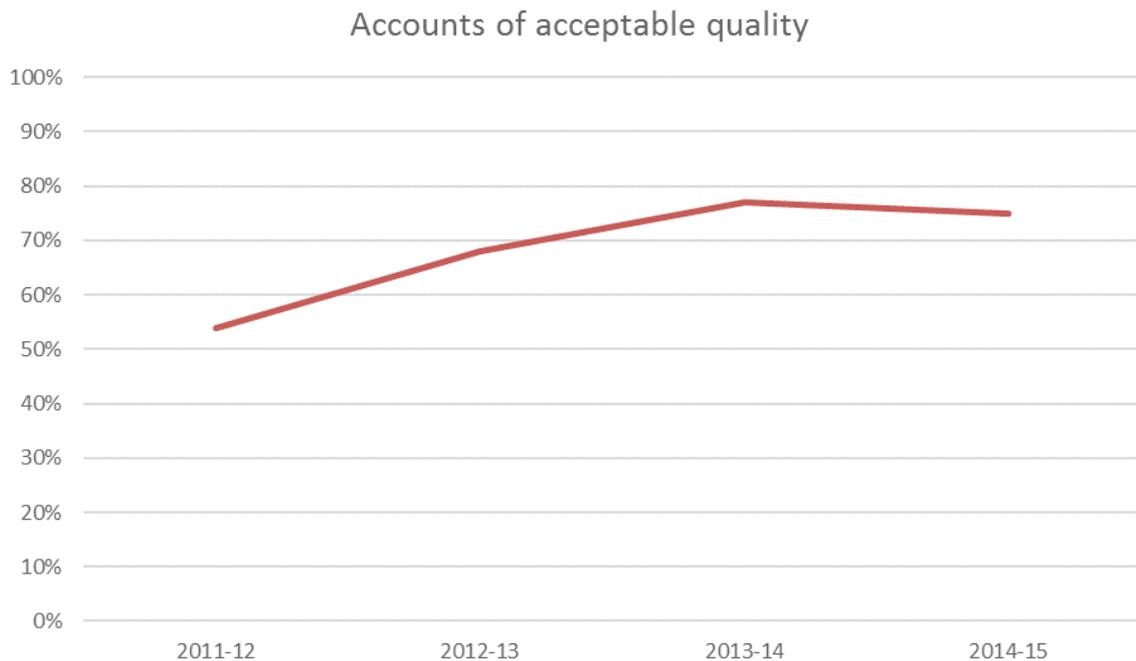
- have the trustees filed all of the required documents that make up a set of accounts (the annual report, independent scrutiny report and the accounts) and are they transparent and internally consistent in what is reported?
- does the annual report explain what activities the charity had carried out during the year to achieve its purposes?
- have the accounts been subject to the required level of independent scrutiny depending on the charity's income and gross assets, either an audit or an independent examination?
- have the accounts been prepared on the correct basis depending on the charity's income and type, either receipts and payments or accruals accounts (also known as SORP accounts)?
- do the accounts contain both a statement of financial activities (SOFA) that analyses the charity's expenditure and a balance sheet and are they consistent with each other (or the equivalent if receipts and payments accounts were prepared)?

A full explanation of our methodology is provided in the appendix.

## How we carried out the review

In September 2016, we selected a random sample of 107 charity sets of accounts from the register of charities, covering accounting years ending during the 12 months to 31 March 2015. As with all samples, there is margin of error. Charities with an income less than £25,000 are not required to file their accounts with us and so are not included in this review.

## What did we find?



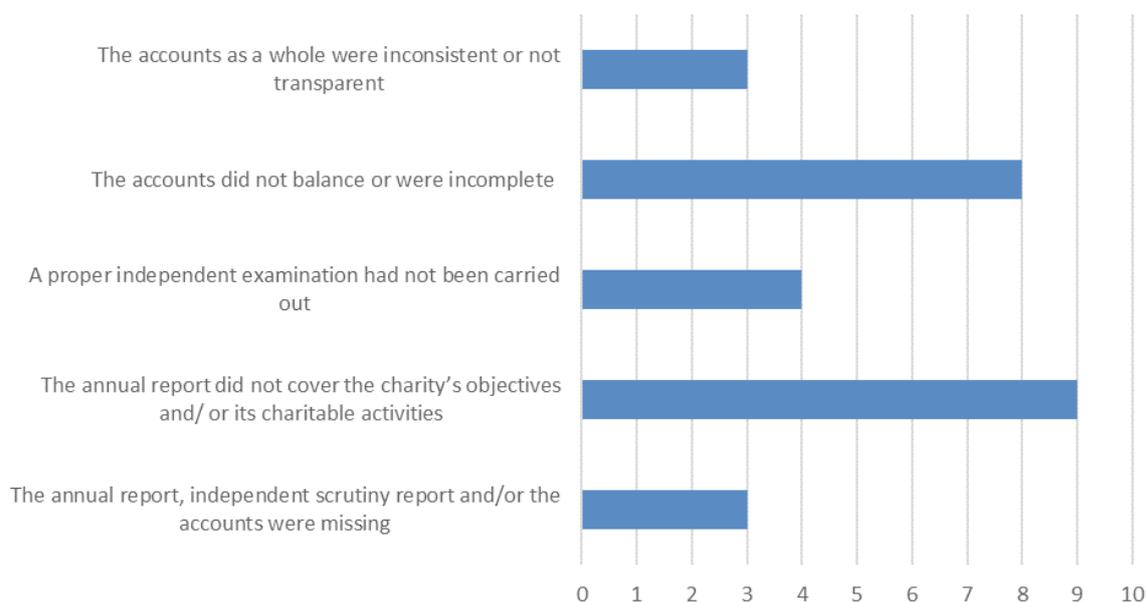
75% of the accounts that we reviewed were of acceptable quality, in other words they met the basic standard that we had set. This is similar to last year's 77%.

We found a high level of compliance with several of the criteria that we measured. In particular:

- all except 3 charities filed all of the required documents in some form
- all of the charities that required an audit had filed an audit report and none of those reports contained a modified opinion
- all except one of the charities that was required to prepare accruals accounts had done so
- all except one charity had provided both a SOFA and balance sheet (or the receipts and payments account equivalent)
- all of the accounts provided an analysis of expenditure and all of the larger charities that were required to use the full SORP analysis had done so

However, 27 charities (25% of the sample) did not meet our basic standard. The reasons why can be summarised into the 5 categories illustrated and discussed in the sections that follow.

### Reasons for failure



#### The accounts as a whole were inconsistent or not transparent

Two of these 3 charities had incurred large overspends in the year that appeared to put their solvency at risk, but the annual reports did not comment on the reasons why or explain what the trustees were doing to ensure each charity's continued operation. The picture of the charity's activities given in the other charity's annual report was completely different to the analysis of expenditure in the accounts.

#### The accounts did not balance or were incomplete

Most of these 8 charities' accounts simply did not balance. In other words, the total of the funds held according to the SOFA did not agree to the total of the funds held according to the balance sheet (accruals accounts) or the bank balances held according to the receipts and payments account did not agree to the figure shown in the statement of assets and liabilities (receipts and payments accounts). In some cases, it was possible to work out why they were different but the reader should not have to do this. A further charity had not included a statement of assets and liabilities and an incorporated charity had prepared receipts and payments accounts. The receipts and payments option is not available to companies.

#### A proper independent examination had not been carried out

These 4 charities had submitted very brief reports that claimed to be some form of independent scrutiny. These are not acceptable as an independent examiner's report. Lack of knowledge of the required wording for the examiner's certificate indicates that the person carrying out the scrutiny has not carried out their independent examination correctly and is unaware of our directions to examiners and so the user cannot rely on any assurances they have given.

## The annual report did not cover the charity's objectives and/or its charitable activities

The most common failing in these 9 annual reports was that either they provided little or no meaningful information on the charitable activities carried out or it was not clear how the activities described were intended to achieve the charity's objectives. There were also examples of charities that did not adequately describe their objectives and the reader could not infer those objectives from the charity's name.

## One or more of the annual report, independent scrutiny report and the accounts were missing

The reason why these 3 sets of accounts were incomplete appears to have been that the versions submitted online by the charities had one or more pages missing.

## What action we took

We have reviewed the most recent accounts of the 27 charities that did not submit accounts of acceptable quality. Twenty-four of these charities have filed at least one more set of accounts. Two charities no longer need to file their accounts because their income is less than £25,000 and the final charity has ceased to operate and been removed from the register. The action that we are taking can be summarised as follows:

- no further action is required (7 charities), usually because more recent accounts have been submitted and are of acceptable quality
- providing guidance to the trustees (17 charities), where the areas for improvement are such that the guidance should enable the trustees to be able to prepare future sets of accounts to an acceptable standard
- requiring action from the trustees (3 charities), where the most recent accounts contain serious deficiencies and in most cases need to be corrected and resubmitted

## Lessons for other charities

It is a statutory requirement to prepare an annual report and accounts and arrange for them to be subject to independent scrutiny, if required. More positively, they provide an important opportunity for the trustees to take stock of what the charity has achieved over the last year and to demonstrate to the charity's supporters, potential funders and the public that they have managed its resources effectively and are meeting its objectives.

We have produced extensive guidance to assist trustees and independent examiners on the preparation and scrutiny of the annual report and accounts. This includes a pro-forma annual report and both receipts and payments and accruals accounts (SORP 2005). These provide a useful structure for preparing documents that meet the reporting requirements. Our guidance can be downloaded from [GOV.UK](https://www.gov.uk).

## Appendix 1: how we carried out the review

### Sample selection

In September 2016, we selected a random sample of 107 charity accounts filed with us that had accounting years ending during the 12 months to 31 March 2015. This approach enabled us to cover a complete annual return cycle and allowed sufficient time for the charities that had filed late to be included in the population.

### Measuring 'acceptable quality'

The definition of what constitutes 'acceptable quality' in the context of a set of accounts is a matter of judgement. The focus of our assessment was on whether each set of accounts met the basic requirements of the users of those accounts rather than on strict technical compliance with the reporting requirements. We based our view of the user's requirements on the Populus survey of public trust and confidence (June 2016). Populus found that 'ensuring that a reasonable proportion of donations make it to the end cause' and 'make a positive difference to the cause they work for' remain the most important factors driving public trust and confidence in charities. Populus also concluded that the public 'show a clear preference for charities that satisfy their needs for transparency and impact'.

We also discussed our criteria with both an internal and external sector reviewer, neither of whom are accountants. Their comments have helped us to clarify and refine our criteria. In particular, we have replaced the indicators of financial risk with a single question that uses the reader's judgement when reading the accounts. However, the results are comparable with those reported in previous years.

We have used the following assessment criteria:

<b>Trustees' annual report (annual report)</b>
Has an annual report been submitted in some form?
Does the annual report explain what the charity was there to achieve (its purposes)?
Does the annual report explain what the charity had done during the year to carry out its purposes (its activities)?
Are any significant risks evident from the accounts and/or the independent scrutiny report covered in the annual report?
<b>Independent scrutiny report</b>
Has an independent scrutiny report been submitted?
Has an audit report been submitted if an audit was required?
Has the auditor or examiner used the correct wording in his/her report?

<b>The accounts</b>
Have accounts been submitted?
Have accruals accounts been prepared when required?
Do the accounts include either a receipts and payments account (if receipts and payments accounts) or a statement of financial activities (if accruals accounts)?
Does the receipts and payments account or statement of financial activities provide an analysis of expenditure and has the SORP analysis of expenditure been used where required?
Do the accounts include either a statement of assets and liabilities (if receipts and payments accounts) or a balance sheet (if accruals accounts)?
Do the closing balances on each statement reconcile to each other?
<b>Overall presentation</b>
Is the set of accounts as a whole understandable, transparent and internally consistent?

We assessed the documents provided on the basis of their content, rather than on what they were called. Therefore, we assessed the handful of what appeared to annual general meeting papers as if they were annual reports. Where appropriate, we also took into account whether the reader could reasonably infer the charity's objectives from its name, for example a playgroup. A sample of assessments were peer reviewed to provide a consistency check.