

AUDIT • TAX • ADVISORY

ICAEW Webinar 30 September 2022

How to establish your charity's reserves policy in a post-pandemic world

Now, for tomorrow





Speakers



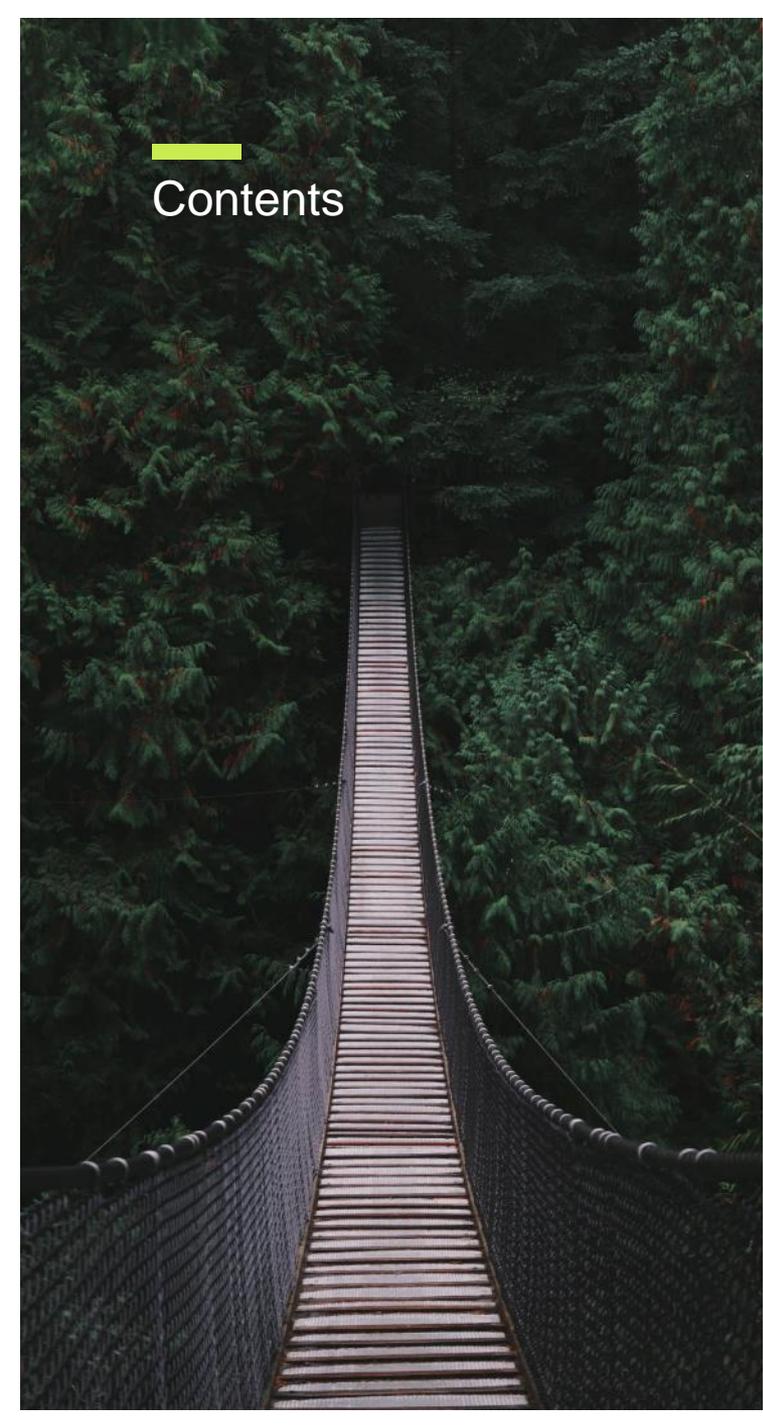
Sudhir Singh

Partner and Head of Not for Profit, MHA



Stephen Vis

Director of Finance and Services, Scripture Union



Contents



The webinar will cover:

- A reminder of what the Charity Commission expects about charity reserves policies
- What should a reserves policy contain?
- How should charities determine what level of reserves is appropriate and who should be involved?
- How should charity risk management inform the consideration of reserves?
- A practical example of how Scripture Union reviewed and revised its reserves policy
- What should charities disclose in their financial statements?

Rather than the future for charities seeming more secure as the effects of the Covid pandemic subside, it seems even more uncertain. So how should charities consider the level of reserves that is appropriate? What is too much, too little or just right?

Charity Commission Guidance "CC19"



The screenshot shows the GOV.UK website page for 'Charity reserves: building resilience (CC19)'. The page header includes the GOV.UK logo, navigation links for 'Topics' and 'Government activity', and a search icon. The breadcrumb trail is 'Home > Charity money, tax and accounts > Charity reserves: building resilience (CC19)'. The Charity Commission for England and Wales logo is displayed. A large blue banner contains the title 'Guidance Charity reserves: building resilience' and the publication date 'Published 29 January 2016'. Below the banner, there are links for 'Applies to England and Wales', 'Publication for Scotland', and 'Publication for Northern Ireland'. The main content area is divided into a 'Contents' section on the left and a '1. Introduction' section on the right. The '1.1 What is this guidance about?' section begins with the text: 'This guidance is written for trustees of charities of all sizes and types, whether they are companies, charitable incorporated organisations, trusts or unincorporated'.

GOV.UK Topics Government activity

Home > Charity money, tax and accounts > Charity reserves: building resilience (CC19)

CHARITY COMMISSION FOR ENGLAND AND WALES

Guidance
Charity reserves: building resilience
Published 29 January 2016

Applies to England and Wales
[Publication for Scotland](#)
[Publication for Northern Ireland](#)

Contents

- 1. Introduction
- 2. Key messages for trustees
- 3. Understanding reserves and the need for a reserves policy
- 4. Explaining reserves in the annual report

1. Introduction

1.1 What is this guidance about?

This guidance is written for trustees of charities of all sizes and types, whether they are companies, charitable incorporated organisations, trusts or unincorporated



Trustees should develop a reserves policy that:

- fully **justifies and clearly explains** keeping or not keeping reserves*
- identifies and plans for the maintenance of essential services for beneficiaries*
- reflects the **risks of unplanned closure** associated with the charity's business model, spending commitments, potential liabilities and financial forecasts*
- helps to address the risks of unplanned closure on their beneficiaries (in particular, vulnerable beneficiaries), staff and volunteers*
- publish the reserves policy** (even if not required to by law) and*
- ensure it is tailored to the charity's circumstances – it should not be just a standard form of wording.*
- It should explain to funders, beneficiaries, the public and the commission exactly what reserves are kept (or not kept) for and when they are to be used*
- larger charities are required to publish their **assessment of the risks** that the charity faces and how to manage them in their annual report*
- make sure that their reserves policy is put in place and operated*
- regularly monitor and review the effectiveness of the policy** in the light of the changing funding and financial climate and other risks*



Why are my free reserves?

Unrestricted funds	£xxx,xxx
NBV of tangible fixed assets	£(xxx,xxx)
Designated funds	£(xxx,xxx)
Programme related investments	£(xxx,xxx)
Free reserves	£xxx,xxx

But don't forget

1. Restricted and endowment funds
2. Other characteristics of underlying assets and liabilities e.g. long term pension scheme obligations; volatility of values
3. Unrecognised liabilities
4. Subsidiary and branch funds for charity groups



Dispelling some misconceptions

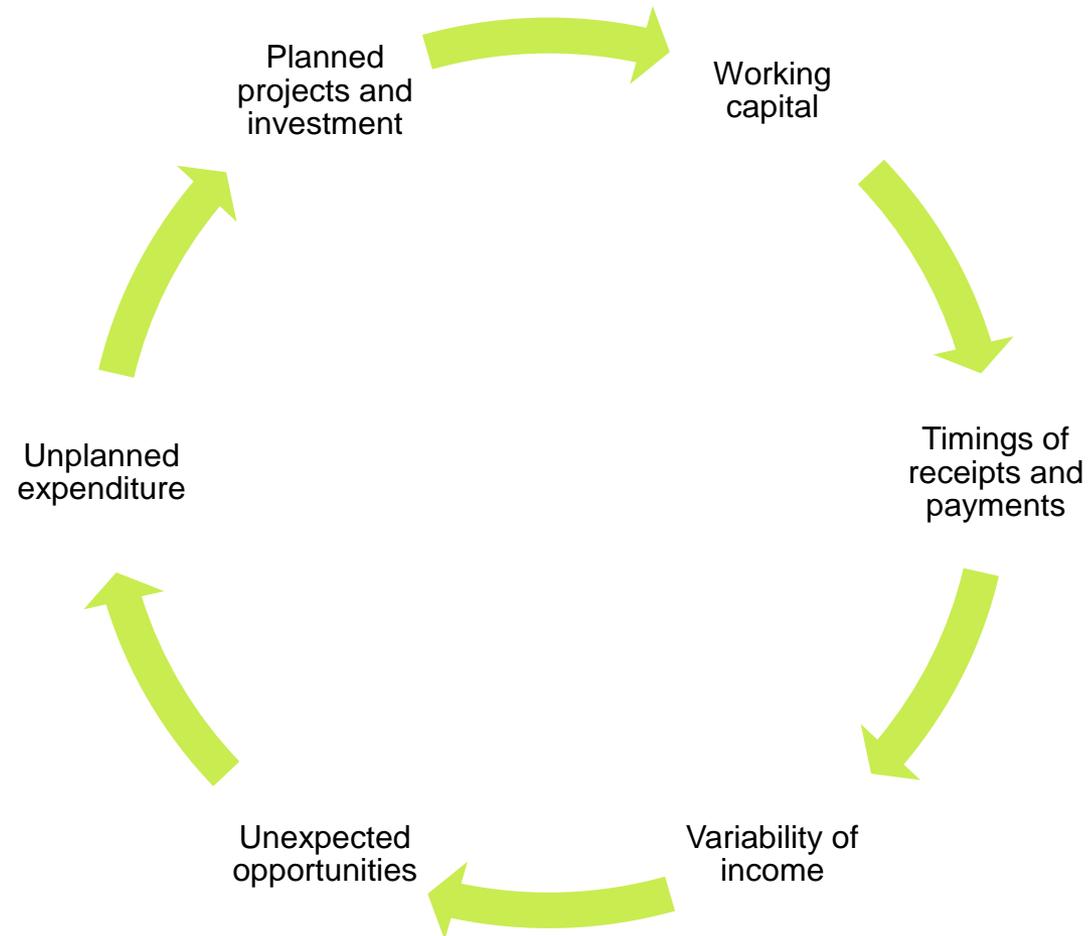
- 📖 There is no rule of Thumb – 3-9 months reserves, etc
- 📖 Going concern = Short Term – Reserves policy = Long Term Resilience
- 📖 What is Long Term for charities?
- 📖 Risks of winding up – are they real?
- 📖 Watch out for long term trends – death from a thousand cuts/
indicators of financial difficulties
- 📖 Setting a target or a range
- 📖 Months or £'s?
- 📖 Charities must have reserves



Not just for a rainy day
1997

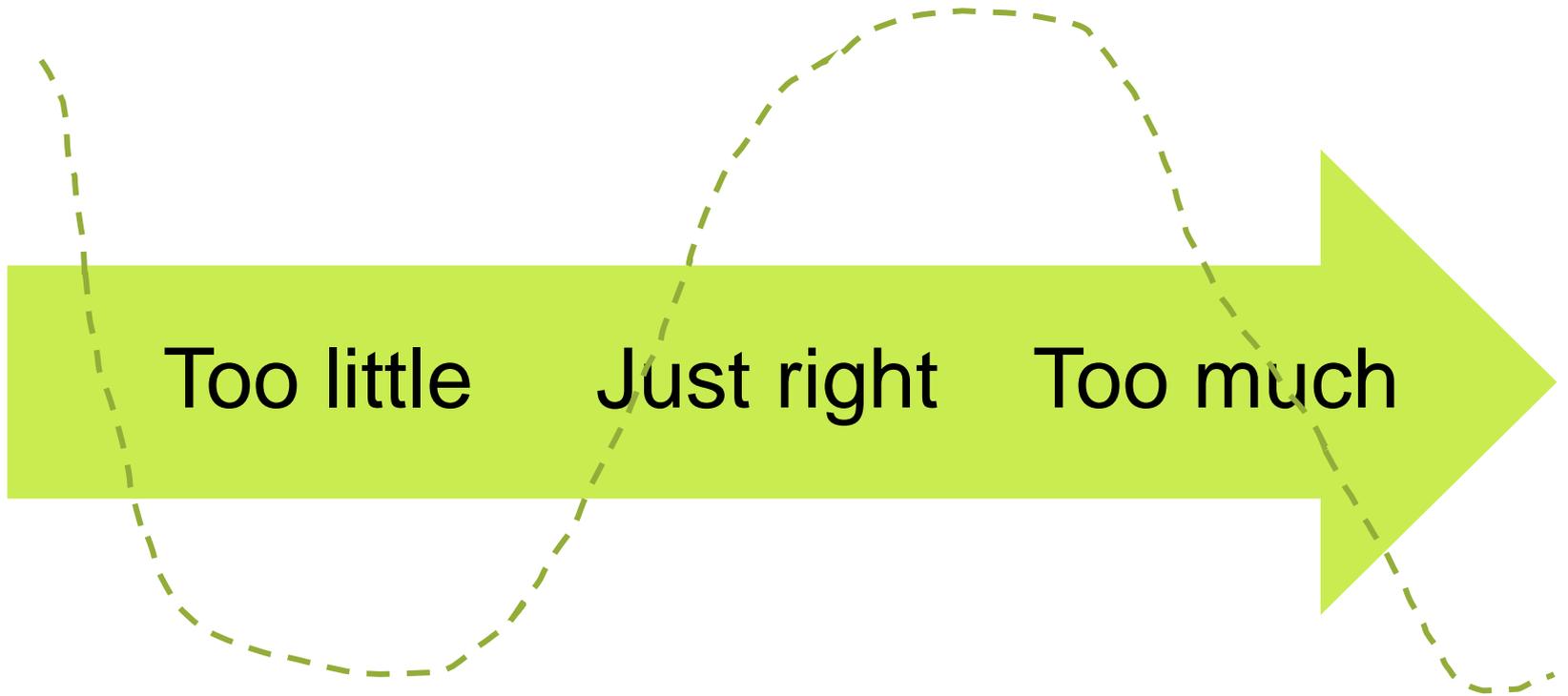


Why are reserves needed?





Getting it right...





Prudent financial management framework



Managing in uncertain times



Cost of living

Price and wage
Inflation

Fraud

Political
uncertainty

Brexit

Energy
costs

Staff and skills
shortages

Social
welfare
funding

Regulatory
changes

Cyber
risks

Greater
charity
need

Geopolitical
turmoil

NHS and
Social Care
crisis

Sustainability

Increasing
poverty

Climate
change

Economic
recession

Woke agenda
attacks

Febrile
fundraising
environment

Ukraine/
Russian
conflict

Mixed political
support



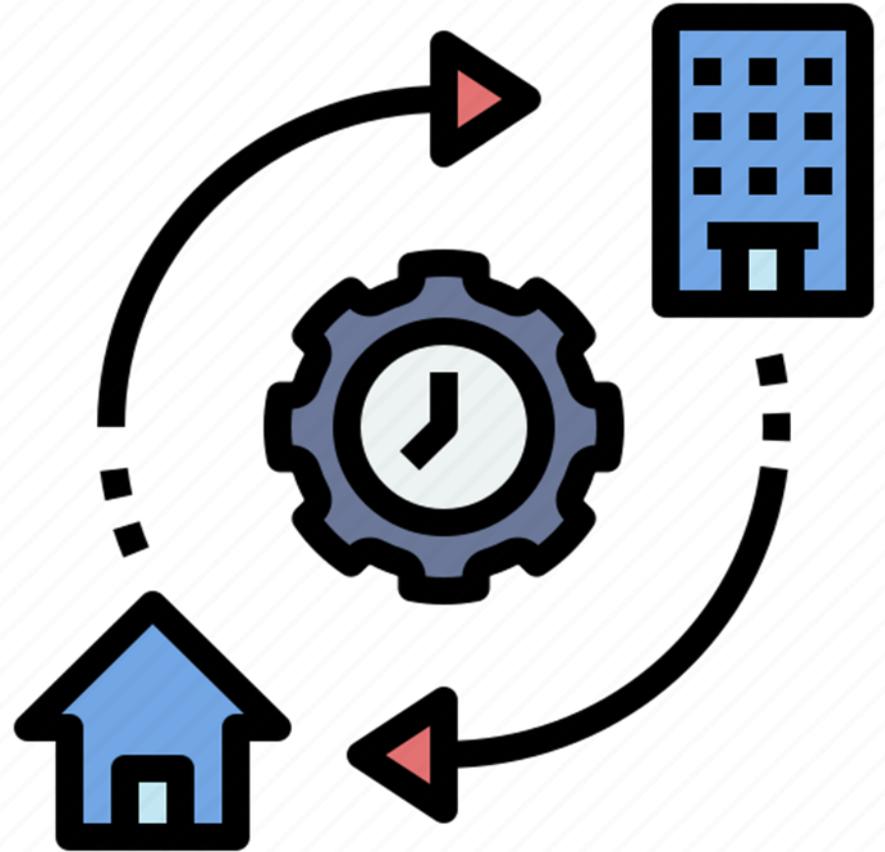
Scripture Union

Scripture Union is a Christian charity, inviting children and young people to explore the difference Jesus can make to the challenges and adventures of life

30 Sept 2022



Update to our Reserves Policy





Risk Based Approach

Previous policy was based upon months of expenditure.

CoVID was said to be a once in a lifetime pandemic, and as we started to exit the other side, it felt an appropriate time to review our Reserve Policy

- **We wanted to ensure that we maximised the money available for our charitable purpose**
- There was a sense amongst the Trustees, and Audit and Finance Committee members, that our General Reserves were quite high
- **We had our Risk Register that was reviewed annually by Trustees and more frequently by Management Team**
- MHA and Sudhir mentioned that we may want to adopt a Risk Based Approach using our Risk Register to set our Target Level for Reserves.



Quantification and Concurrence

Approach proposed was fairly straightforward:

- **For each item on our Risk Register, quantify the risk impact to Reserves**
- **Assess which of these risks might happen concurrently, and use this concurrent assessment to determine the minimum level of General Reserves that were required.**
- **Sounds simple, but how?**



Risk : A
safeguarding issue
impacts our
reputation





Oxfam – a case to learn from

1. In early 2018 Oxfam were in the news for a safeguarding issue in Haiti, and Save the Children were also in the news over summer 2018.
2. At the time press reports suggested Oxfam would lose 7000 regular donors;
 - 35% people said they were less likely to donate to humanitarian aid/ rising to 52% of those who had donated.
3. High headline numbers of impact included loss of Government funded programmes which are not relevant to us as a Charity and so..



Oxfam - a case to learn from

1. We downloaded the accounts to determine the Donation Revenue for Oxfam in 2017, and compared against the Donation Revenue in 2020 (latest available accounts)
2. This suggested a 33% reduction in Donations across the 3 years
3. We used this as a suggestion of the possible revenue impact to our charity, and then separately assessed it would take us 9 to 12 months for us to:
 - i. determine the level of the income drop, and
 - ii. implement cost savings that would allow us to reduce costs to match this reduced donations level
4. This was then applied to our prior year donation income and helped us assess the size of the revenue gap that would flow through against Reserves.



Risk : Cyber Incident





Cyber incident

1. Found this harder as very little is published externally about how much it costs to recover from a Cyber incident.
2. I made the assumption of £25,000 cost impact, and made clear in the report to the Trustees this was a guesstimate.
3. Whilst reviewing our approach, one of our Trustees – who worked in IT - advised that this was likely to be too low, and recommended we double the assessment.
4. More recent information would suggest to me that we should again increase this impact assessment



Risk : Sudden stock market movement





Stock markets

1. We are fortunate to have some Investments , and clearly these move with the stock markets.
2. At the start of the CoVID pandemic the stock market dropped by 20-30%
3. We used this to assess the scale of impact for possible loss due to economic event.



Concurrence

But we also then considered which of our risk factors could happen at the same time, and so it was possible that :

- i. a sudden stock market movement could happen at the same time as:
- ii. the failure of our key distributor , and
- iii. this could also occur at the same time as a Cyber incident which may have led to a safeguarding reputational impact

So we set our Reserves based on covering this “worse case” situation

**A risk based reserves
policy....**

**Linking practice and
theory**



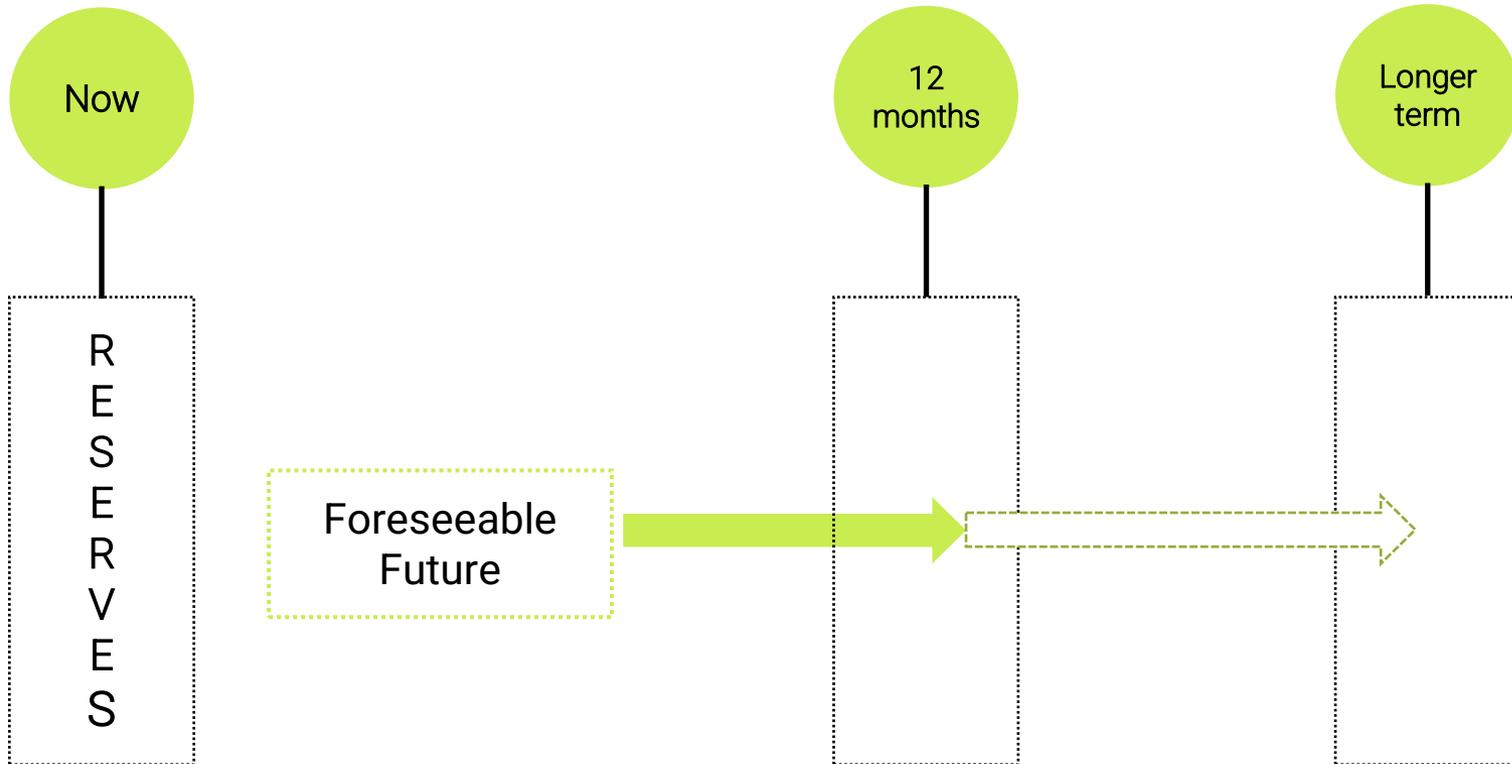


Linking risks to reserves policy scenarios

Risk Scenarios	Likelihood	Impact	Mitigated Impact
Scenario 1	Virtually certain – next 6 months	Medium - £500k	£250k
Scenario 2	Likely – in next year	High - £1m	£750k
Scenario 3	Probable – next two years	Very high - £5m	£1m
TOTAL			£2m
Reserve range			£250k to £2m?



Reserves policies and going concern

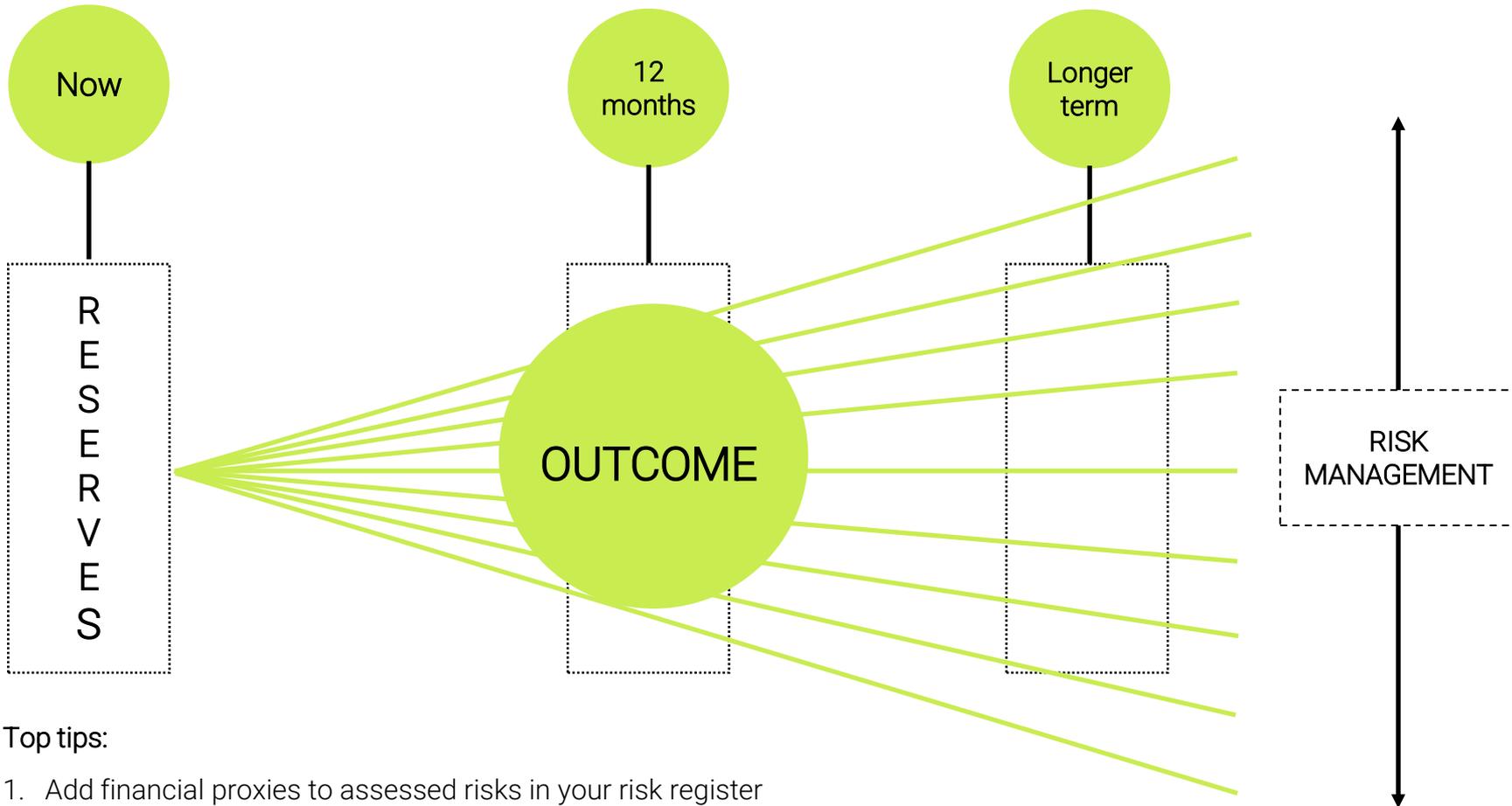


Top tips:

1. Strategic business plans – 2 to 5 years?
2. Multi-year or rolling budgets and forecasts



Linking risk management to reserves requirements

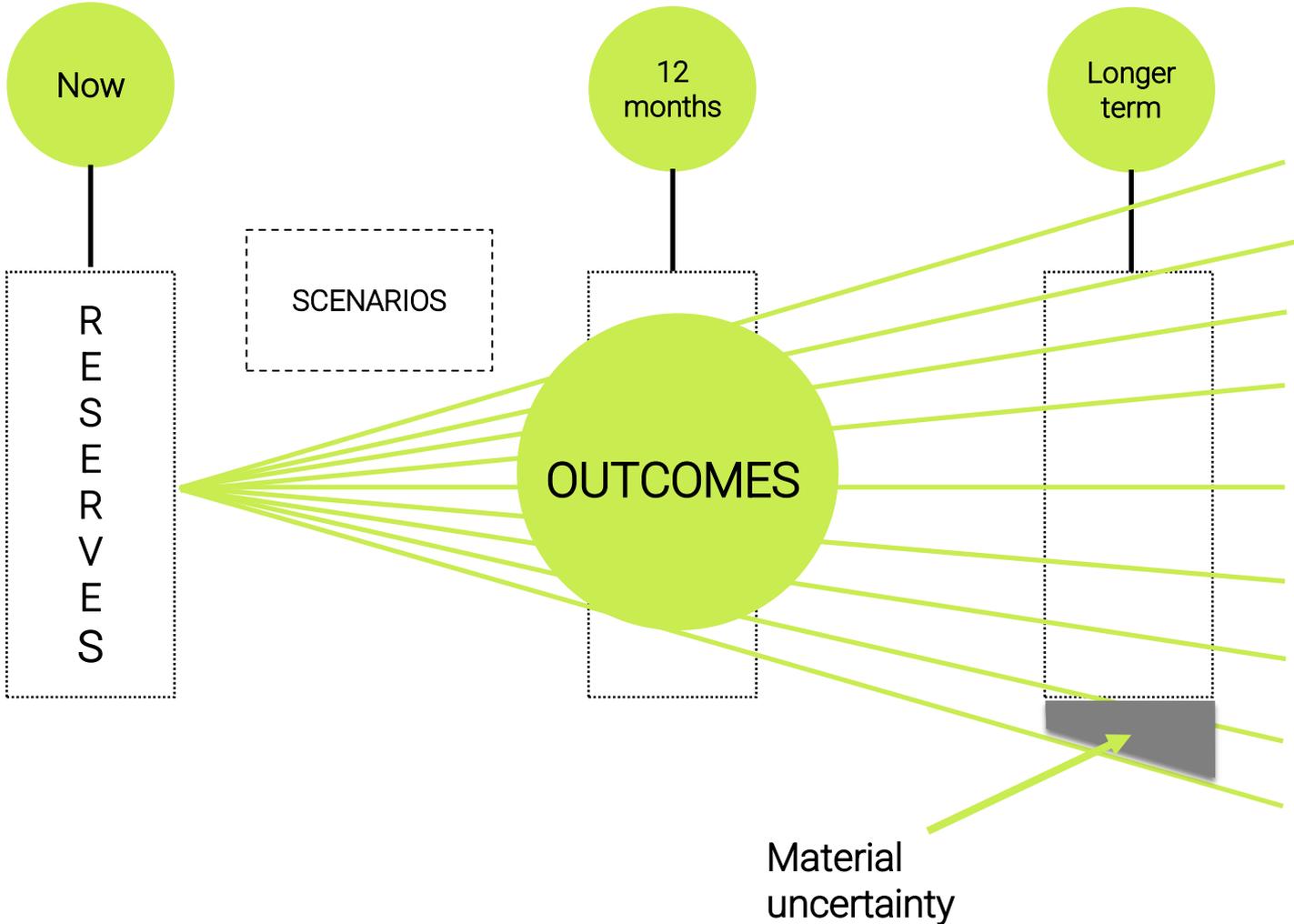


Top tips:

1. Add financial proxies to assessed risks in your risk register
2. Map out potential future scenarios to predict range of possible outcomes

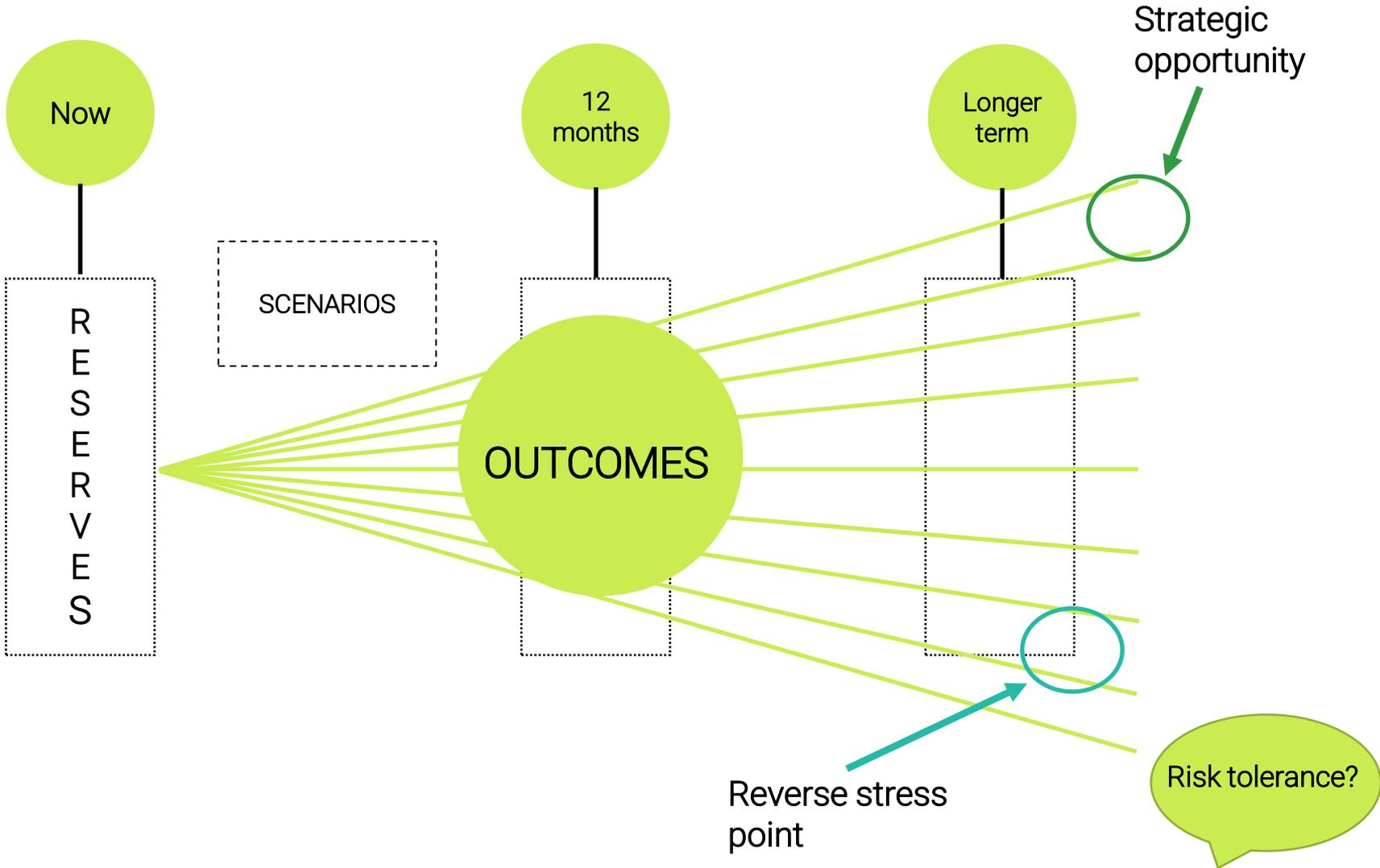


Identifying material uncertainties





The importance of scenario planning





Charity Statement of Recommended Practice – Trustees' Annual Report requirements

- 1.22. 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.

1.48. 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;
- 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.

—
Observations and good practice



Large vs small charities



Summary of policy only



Resilience statements for Public Interest Entities



Charity Commission assessment of reserves policy disclosures (2018)

What did they find?

Whether the charities had explained their reserves policies in the trustees' annual report: Nearly all, 97%, of charities in our sample included at least a reference to their reserves policy in their trustees' annual report. = **GOOD**

Does the trustees' annual report:

- ✓ Explain the charity's policy on reserves? 92%
- ✓ State the level of reserves held? 67%
- ✓ State why reserves are held? 90%
- ✓ Meet all three requirements? 64%

So, more than a third of the charities' explanations of their reserves policies did not provide all of the basic information required. = **IMPROVEMENT REQUIRED**

NB This was not a qualitative assessment of the standard of financial management just a compliance assessment

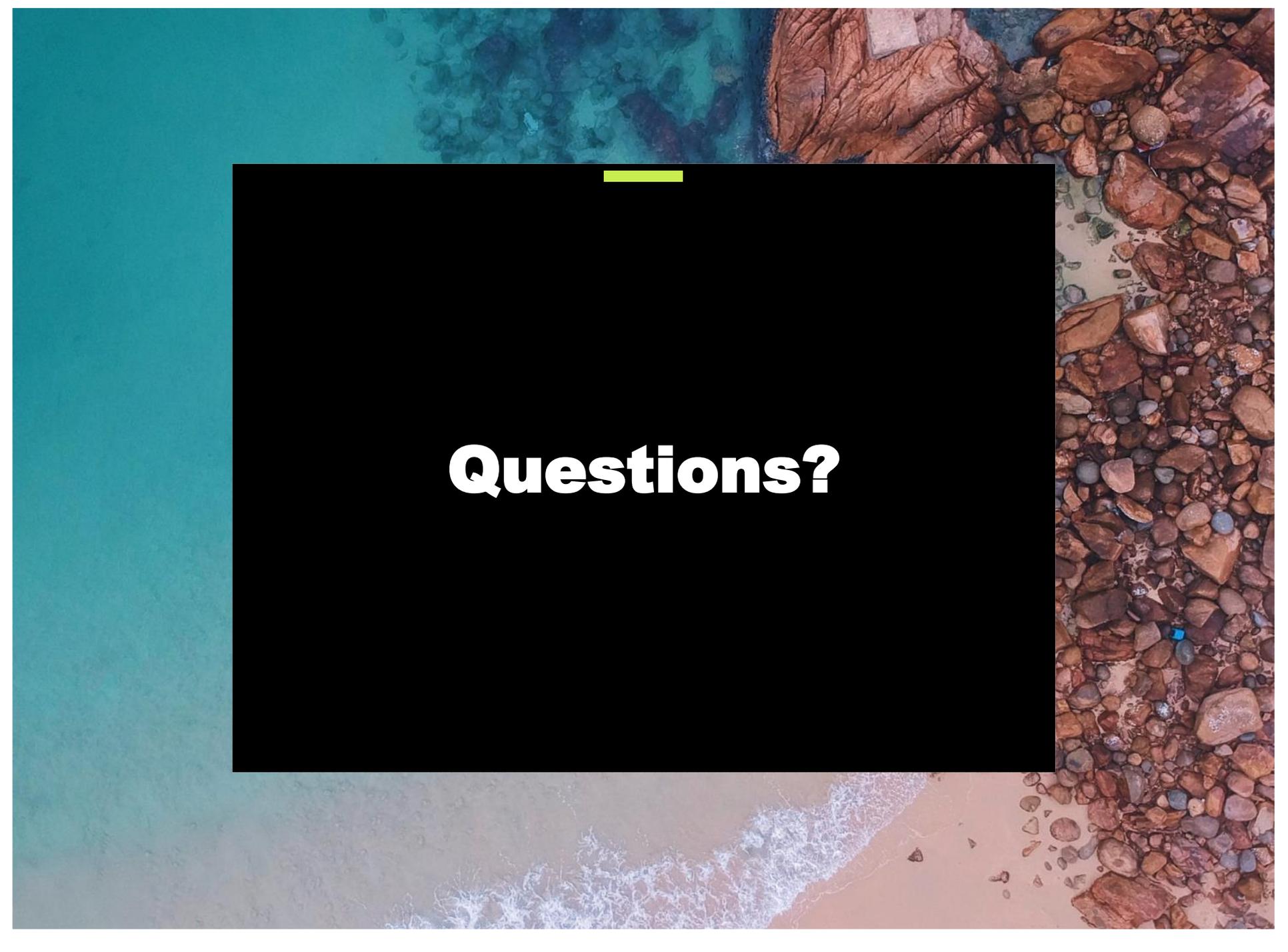
Conclusions

We have covered:

- 😊 Understanding a framework for considering how to set a reserves policy
- 😊 Learning how to integrate key aspects of charity financial management
- 😊 Seeing how strategic financial models can be applied in practice to establish a reserves policy
- 😊 Gaining the ability to develop a good practice reserves policy

<https://www.icaew.com/technical/volunteering-community/trustee-training-modules>

<https://mha-uk.co.uk/charity-trustee-hub/>

An aerial photograph of a coastline. The top half shows clear turquoise water meeting a rocky shore. The bottom half shows a sandy beach with gentle waves washing onto it. A large black rectangle is overlaid in the center, containing the word 'Questions?' in white. A small yellow horizontal bar is at the top of the black rectangle.

Questions?

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