The Transfer of Charitable Funds (England and Wales)

Briefing paper, June 2015

This briefing has been produced by the HFMA's Charitable Funds Special Interest Group and is an updated version of an online briefing first issued in November 2012. It takes account of developments since then and in particular the release of new Statements of Recommended Practice. The guidance this briefing sets out applies to all accounting periods beginning on or after 1st January 2015.

Introduction

Reorganisations of NHS services often lead to the linked charitable funds also being reorganised. Where hospitals or hospital services are transferred between NHS bodies (for example, between hospitals and/ or community services) the opportunity may be taken to align the management of the linked charitable funds. The mechanism for effecting transfers of charitable funds differs between England and Wales.

This guidance has been produced by the HFMA's Charitable Funds Special Interest Group and looks at how to account for transfers of charitable funds. It considers the accounting treatments that should be followed.

The accounting framework

Charity accounting follows UK Generally Accepted Accounting Practice (UK GAAP) and not International Financial Reporting Standards (IFRS). Charities also report under:

- Accounting and reporting by charities: statement of recommended practice applicable to charities preparing their accounts in accordance with the financial reporting standard applicable in the UK and Republic of Ireland (FRS 102). This is known as SORP 2014 (FRS 102) OR
- 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). This is known as SORP 2014 (FRSSE).

Both SORPs offer application guidance but do not over-ride accounting standards.

In relation to the treatment of mergers, paragraph 24.30 of the SORP 2014 (FRS 102) and paragraph 24.31 of SORP 2014 (FRSSE) state that:

"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 exceeds 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."

The relevant accounting standards and pronouncements in FRS 102[1] (published August 2014 and effective for periods beginning on or after 1 January 2015) are:

- Section 19 – business combinations and goodwill
- Paragraphs 34.75 to 34.86 – public benefit entity combinations.

The FRSSE[2] does not refer to mergers so reference should be made to the SORP as well as paragraphs 34.75 to 34.86 of FRS 102.

Trusteeship cannot simply be acquired. Transfers of charitable funds are effected by a process involving the Department of Health or Welsh Government. These bodies identify what transfer of charitable funds is appropriate and direct the transfer to take place. The decision to effect a transfer is not made by the existing trustees of NHS charitable funds.

The decision as to which treatment to adopt should be made such that the financial statements for the combination give a 'true and fair' view.

Merger accounting

Merger accounting is a uniting of interests resulting in the creation of a new combined entity. A merger is reflected in the financial statements as if the new reporting entity, comprising all parties to the transaction, had always existed. It is a simple aggregation of the assets and liabilities with the prior year comparative figures being that of the combining entities added together.

Paragraph 27.4 of both charities SORPs (FRSSE and FRS 102) state that a charity combination must be accounted for as a merger if all three 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 purely on the basis of a consensus between the parties to the combination rather than purely by exercise of voting rights
- There is no significant change to the classes of beneficiaries of the combining entities or the purpose of the benefits provided as a result of the combination.

In the context of NHS transfers, the transfer is effected by the Department of Health or Welsh Government and so no party to the combination is able to portray itself as acquirer. Since the beneficiary class of the NHS patient is common to all NHS charities, there is no significant change to beneficiary class or purpose. Lastly, most NHS charities have no paid staff and the Trustee Board is not nominated by the NHS charities involved but is established by the Department of Health or Welsh Government

[1] https://www.frc.org.uk/Our-Work/Codes-Standards/Accounting-and-Reporting-Policy/Standards-in-Issue/FRS-102-The-Financial-Reporting-Standard-applicabl.aspx
[2] https://www.frc.org.uk/Our-Work/Codes-Standards/Accounting-and-Reporting-Policy/FRSSE.aspx

However, to apply merger accounting two or more charities must come together. Merger accounting should not be applied where only certain funds are transferred because a fund is not a charity. However special trusts, endowment or restricted income funds, may be construed as equivalent to a charity if they are separate components of a ‘group’ registration. A feature of many special trusts is that they are potentially capable of separate registration as a charity but for administrative convenience these funds are treated as being a component of a registered charity.

Acquisition accounting

An acquisition is the enlargement of a continuing entity. An acquisition is reflected in the consolidated financial statements as if the acquirer purchased the acquiree’s assets and liabilities as a bundle of assets and liabilities on the open market.

SORP 2014 (FRS 102) paragraph 24.30 provides that where an acquisition of another charity is not a merger, is carried out for nil or nominal consideration and is, in substance a gift, the excess of assets over liabilities acquired is reported as a gain and recognised as donated income and conversely an excess of liabilities over assets acquired is reported as a loss and recognised as a charitable expense.

Where the combination of charities is neither a gift nor a merger then it is accounted for as an acquisition. In an acquisition the comparative figures are those of the acquiring entity alone and are not restated. The gain (where the consideration is less than the net assets acquired) is reported in the Statement of Financial Activities (SoFA) as ‘other income’ (refer to SORP 2014 (FRS 102) paragraph 24.33). Any loss on acquisition (where the consideration is less than the value of assets acquired is shown as negative goodwill on the balance sheet which must be written off in the reporting period of the acquisition (refer to SORP 2014 (FRS 102) paragraph 24.30). The transfers line should not be used as this line reports transfers between existing funds under trustee control.

The types of transfer involved

The Charity Commission’s NHS guidance sets out 8 examples of a transfer – see Section E of the NHS charities guidance[3] issued by the Charity Commission in 2012. Other useful guidance on the Charity Commission’s role can be found on their website[4].

These examples are used to illustrate the accounting treatments to be applied. This guidance assumes familiarity with these examples and for more information about them refer to the Charity Commission’s guidance.

In some instances, the minimum reporting required from a statutory viewpoint would not necessarily be considered best practice. Where this is the case both have been included. The reference (Ref) column relates to the relevant Charity Commission example (see sections E and G.5 of the NHS charities guidance).

[3] www.gov.uk/government/uploads/system/uploads/attachment_data/file/360670/NHS_charities_guidance.pdf

[4] https://www.gov.uk/government/publications/nhs-charities-guidance

Common types of transfer and accounting solutions to apply

Ref	Summary of scenario	Accounting treatment – 'giving' charity	Accounting treatment – 'receiving' charity
1a	Merger of two or more NHS charities with only a single charity resulting from the combination.	**Statutory minimum**: giving charity dissolves upon merger and is only required to produce cessation accounts if for a full year. **Best practice**: giving (i.e. ceasing) charity produces accounts up to the point of cessation.	Treat as a merger with prior year comparatives reporting pre merger results of the combining charities (on the assumption that the criteria for merger accounting are met).
2a	An NHS charity dissolves and passes its funds to two or more other NHS charities.	**Statutory minimum**: giving charity dissolves upon cessation and is only required to produce cessation accounts if for a full year. **Best practice**: giving (i.e. ceasing) charity produces accounts up to the point of cessation.	Treat as an acquisition and report the gain (or loss) in the SoFA. Comparatives not restated.
3a	One or more funds transferred by one NHS charity to another but the gifting charity continues to operate.	Giving charity treats the gift as a one-off transfer which is normally shown as an expense under charitable expenditure in the SoFA.	Treat as a gift and report the gain (or loss) in the SoFA. Comparatives not restated.
4a	The funds associated with a particular clinical specialty are transferred from one NHS charity to another.	Giving charity treats the gift as a one-off transfer which is normally shown as a transfer (expense) under charitable expenditure in the SoFA.	Treat as an acquisition and report the gain (or loss) in the SoFA. Comparatives not restated.
5a	One or more NHS charities are combined for effective administration.	**Statutory minimum**: giving charity dissolves upon merger and must produce cessation accounts if for a full year. **Best practice**: giving (i.e. ceasing) charity produces accounts up to the point of cessation.	If recipient NHS charity already exists then treat as an acquisition and report the gain (or loss) in the SoFA. Comparatives not restated. If a new NHS charity is established for the purpose then treat as a merger with prior year comparatives reporting pre merger results of the combining charities (on the assumption that the criteria for merger accounting are met).
6a	An existing NHS charity holds one or more	The gift is reported as charitable expenditure in the	Each receiving charity reports income as voluntary income (grants

	charitable funds to which it and one or more other NHS bodies are entitled for the benefit of NHS patients.	SoFA.	received) in the SoFA.
7a/ 8a	Change in the legal form of governance but no other changes to funds held or area of benefit.	**Statutory minimum**: if charity registration number changes, the giving charity dissolves on the legal change and is only required to produce cessation accounts if for a full year. **Best practice**: giving (i.e. ceasing) charity produces accounts up to the point of cessation. However, if the charity registration number is unchanged following the legal change then the giving charity simply produces accounts for its last full year.	If the corporate trustee is changing from an NHS Trust to an NHS Foundation Trust or the body of trustees is changing from a s11 body to a s54 body then it is merely a change in legal form as in substance the trustee arrangement is unchanged. Treat effectively as a continuation of the charity with prior year comparatives reporting the results of the charity for the last full year under the previous arrangement.