

CHARITY SECTOR

CHARITIES RESERVES POLICY MANAGEMENT



BEST PRACTICE EXAMPLES

Charities are required to publish a reserves policy to explain to all stakeholders why they are setting money aside rather than spending it on their principal aims.

In our most recent review of charity reserves, we found that improved charity reserves policies and disclosures could help individual charities become more sustainable and protect the reputation of the sector as a whole. We have therefore outlined below two policies that we consider good examples of best practice.

A robust reserves policy

A robust reserves policy should set out the following three key elements:

1. How much the charity needs to hold in reserve and why
2. How and when the charity's reserves can be spent
3. How often the reserves policy will be reviewed

Our review, and our experience working with charities, shows that few charities review and update their reserves policy as part of ongoing financial planning. In almost all cases, the reserves policy is only reviewed at the year end when the statutory accounts are being signed off. Reviewing the reserves a charity holds and why they are held should be part of ongoing financial planning throughout the year – much as reviewing strategy, risk appetite and management information already is.

RESERVES POLICY AND MANAGEMENT

Reserves are maintained at a level that enables the Charity to manage financial risk and short-term income volatility. They allow the Charity to sustain optimal levels of research over the long term, ensuring that financial commitments can be met as they fall due.

Our reserves policy takes into consideration that we commit expenditure over the medium term, since our research commitments span many years, whilst recognising that, as we are a fundraising charity, we are subject to the effects of short-term volatility in income. We therefore hold funds in reserve to ensure that we can meet our research commitments in the face of such fluctuations. We use a rolling five-year plan to model how we will fund the delivery of our strategy, ensuring reserves remain at an appropriate level.

We have a single reserves measure. This measure mandates that the Charity holds a minimum level of cash and investments to ensure that the Charity will be able to discharge its financial commitments as they fall due over the course of the five-year plan.

We monitor 'managed cash and investments', which includes all amounts available to finance the general activities of the Charity, net of any overdraft or credit line which has been drawn upon. Council have agreed that 'managed cash and investments' should exceed a minimum of three months but is not expected to exceed five months annualised forecast cash outflow.

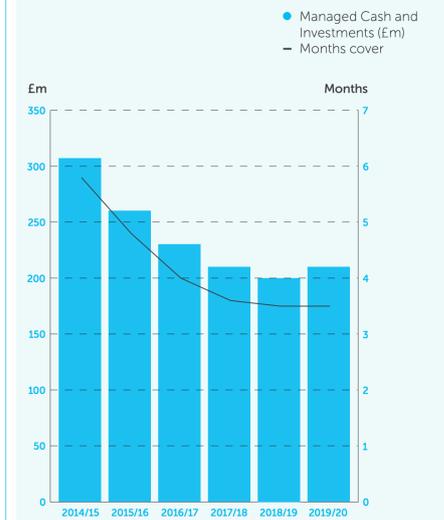
Our reserves measured at 31 March 2015 are as follows:

	31 March 2015 £m	31 March 2014 £m
Managed cash and investments		
Cash and investments	318	293
Less: funds under separate management ¹	(11)	(11)
Managed cash and investments	307	282
	Months	Months
Months of annualised forecast cash outflows	5.7	5.7

¹ Consolidated endowments and charities.

At 31 March 2015, although the 'managed cash and investments' level is nearly six months of forecast cash outflows, the Charity's five-year plans include projections for reserves to reduce as the Charity increases charitable expenditure and completes its funding contribution for construction of the Crick. The indicative shape is shown below.

INDICATIVE FUTURE RESERVES (£M)



Source: Cancer Research UK Annual Report & Accounts 2014/15, page 23

It is not always clear that charities are designing reserves policies that are fit for purpose. We believe that to be effective and useful, a reserves policy should be risk-focused and assessed against the economic environment. The policy should also take into account the level of working capital required to continue core work. Charities will need an understanding of, and agreement on, what core work the charity wants to protect, how much that costs and how it is funded.

We consider these examples of best practice particularly because they:

- ▶ set the tone of the financial approach of the organisation
- ▶ clearly define the charity's reserves policy and why it is holding reserves
- ▶ provide details on the measurement criteria
- ▶ show the current level of reserves against targets and provides an explanation on variances. Furthermore, they provided details on indicative future reserves levels, based on the impact of the charity's own five year strategy
- ▶ make clear why the charity is holding the reserves at the level it is
- ▶ provide details on the level of working capital that the charity determines sufficient to protect the continuity of work
- ▶ show comparison of like-for-like data year-on-year
- ▶ link to both the liquidity policy as well as the investment policy.

It's important to include this level of detail as it allows the users of the accounts (i.e. beneficiaries, funders, employees, members and the general public) to understand the approach to future planning of those charged with governance within the charity.

The reserves policy allows this by demonstrating that the charity's money is being used to good effect, and why a charity is maintaining or seeking a certain level of reserves. If high levels of reserves are maintained with no explanation, this may be subject to scrutiny and possible investigation by the charity commission.

RESERVES POLICY AND MANAGEMENT

Reserves are maintained at a level that enables the Charity to manage financial risk and short-term income volatility. They allow the Charity to sustain optimal levels of research over the long term, ensuring that financial commitments can be met as they fall due.

Our reserves policy states that managed cash and investments should exceed three months but are not expected to exceed five months' forecast cash outflows. Although since 2016 levels have been greater than five months' cover, the Charity's medium-term plan includes projections for reserves to reduce as we increase charitable expenditure, bringing the anticipated cover to four months, as shown diagrammatically opposite.

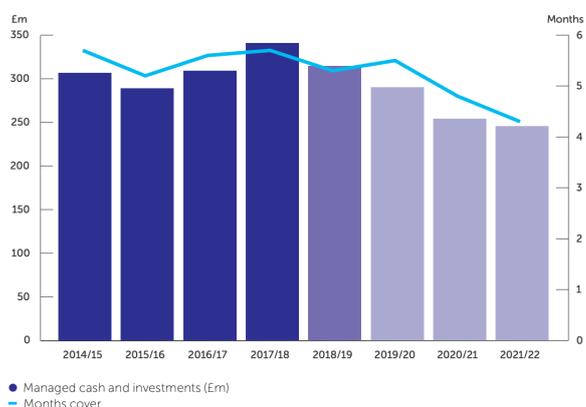
Reserves measured at 31 March are shown on the previous page.

INVESTMENT POLICY AND PERFORMANCE

The investment policy supports the reserves policy. The Charity seeks to adopt a cautious, prudent and well-diversified investment stance to balance potential returns with appropriate levels of risk. Smoking causes around a quarter of all cancer deaths in the UK and it is the Charity's policy not to invest, directly or indirectly, in tobacco companies.

The Charity's aim is to ensure that investments maintain their capital value, in real terms, across an investment cycle. Goldman Sachs Asset Management manages the majority of our investments. The portfolio is invested in a range of securities in line with levels agreed between the Charity and Goldman Sachs. The net investment gain for the year was £11 million (2017: £19 million gain).

HISTORIC AND INDICATIVE FUTURE RESERVES



FIVE-YEAR FINANCIAL HISTORY

The five-year record shows strong increases in charitable expenditure supported by fundraising growth.

Spend on charitable activities has increased steadily supported by fundraising growth. Reserves are forecast to be drawn down across the course of our five-year plan.

	2014	2015	2016	2017	2018
Underlying income (£m) ¹	590	609	635	647	634
Fundraising and trading income (£m)	490	516	529	544	527
Income from charitable activities (£m)	95	87	95	92	101
% of each £1 donated available to beat cancer ²	82%	80%	80%	80%	81%
Total spend on charitable activities (£m) ³	414	461	470	474	466
Managed cash and investments (£m)	282	307	289	309	341

¹ Underlying income does not include gains generated by property transactions. A pension curtailment gain in 2015 is also excluded.

² See page 35 for how the percentage available to beat cancer is calculated.

³ Total spend on charitable activities includes capital contributions to the Francis Crick Institute.

Source: Cancer Research UK Annual Report & Accounts 2017/18, page 36

Showing prior year comparisons and future indicative levels provides additional evidence that the charity is adhering to their policy and helps to build further credibility.

If you would like BDO to review your reserves policy, get in touch.

FOR FURTHER INFORMATION:

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