Universities UK

Statement of recommended practice:

accounting for further and higher education

Universities UK MANAGEMENT GUIDANCE

RECOMMENDED PRACTICE

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Introductory statements

Foreword

This Statement of Recommended Accounting Practice (SORP), which takes effect from 1 August 2007, reflects the changes in recent Statements of Standard Accounting Practices (SSAPs), Financial Reporting Standards (FRS), and in best accounting practice since 2003 when the current SORP came into effect. As previously, the SORP combines the requirements of institutions of both further and higher education throughout the United Kingdom, reflecting the collaboration between the key stakeholders – the Higher and Further Education Funding Councils, the representative bodies, accounting practitioners and the Accounting Standards Board – all of whom are represented on the HE/FE SORP Board. This SORP has benefited from the employment of a technical author, Matthew Hodge of PricewaterhouseCoopers, who has improved the format and coverage of accounting issues relevant to the sector. The Board has been admirably supported by a technical advisory group drawn from the finance directors of institutions of further and higher education. Both the technical group and the Board are indebted to Karen Newcombe for all her work in coordinating the drafting and consultation processes and to Miles Hedges, the Finance Director of The Open University and Chair of that Group for his considerable input.

The SORP allows institutions to provide consistent and comparable financial information to a range of stakeholders and other interested parties, demonstrating and enhancing their public accountability for a combined gross income which approaches £20 billion per year.

Professor Rick Trainor

Chairman of the HE/FE SORP Board

July 2007

Preface

This new Statement of Recommended Practice (SORP) is the fourth to combine the requirements of institutions in the further and higher education sectors. It has been fully revised and developed from the previous SORP: Accounting for Further and Higher Education, issued in 2003.

Further and higher education institutions ('institutions') evolved from a variety of backgrounds, having been founded as Universities or Polytechnics or Colleges. They differ in size and complexity. All have charitable status, though not all are 'exempt' charities, and some are companies limited by guarantee. Further and higher education institutions form a separate identifiable group with special characteristics and are therefore outside the scope of the Charities SORP. This SORP is applicable to all further and higher education institutions throughout the United Kingdom.

The financial statements of institutions should, as far as possible, be prepared on a comparable and consistent basis. They should, where possible, be prepared on a similar basis to the accounts of other corporate organisations, and should follow all relevant financial reporting standards, including those introduced after the publication of this SORP. The Statement of Recommended Practice which follows takes account of best accounting practice, including Statements of Standard Accounting Practice (SSAPs), Financial Reporting Standards (FRSs) and Urgent Issue Task Force (UITF) Abstracts, the requirements of UK Funding Bodies, the accounting provisions of the Companies Act, and other relevant legislation. The concept of the "true and fair view" is regarded as of paramount importance.

It is recognised that from time to time it will be necessary to review this Statement of Recommended Practice in response to changes in accounting practices.

Statement by the Accounting Standards Board (ASB)

The aims of the Accounting Standards Board (the ASB) are to establish and improve standards of financial accounting and reporting, for the benefit of users, preparers, and auditors of financial information. To this end, the ASB issues accounting standards that are primarily applicable to general purpose company financial statements. In particular industries or sectors, further guidance may be required in order to implement accounting standards effectively. This guidance is issued, in the form of Statements of Recommended Practice, by bodies recognised for this purpose by the ASB.

The HE/FE SORP Board (the SORP Board) has confirmed that it shares the ASB's aim of advancing and maintaining standards of financial reporting in the public interest and has been recognised by the ASB for the purpose of issuing SORPs. As a condition of recognition, the SORP Board has agreed to follow the ASB's Code of Practice for bodies recognised for issuing SORPs. The Code of Practice sets out procedures to be followed in the development of SORPs. These procedures do not include a comprehensive review of the proposed SORP by the ASB, but a review of limited scope is performed.

On the basis of its review, the ASB has concluded that the SORP has been developed in accordance with the ASB's Code of Practice and does not appear to contain any fundamental points of principle that are unacceptable in the context of present accounting practice or to conflict with an accounting standard or the ASB's plans for future standards.

28 June 2007
Accounting Standards Board

1. Introduction

Note that text in italics throughout the main body of this SORP denotes terms which are defined in Appendix 1 – Definition of terms.

Effective date of commencement

The provisions of this SORP should be adopted for accounting periods ending on 31 July 2008 and thereafter. Earlier adoption is encouraged. 1

Features of further and higher education institutions necessitating a SORP

The mission of further and higher education institutions is achieved by the creation, transmission and utilisation of knowledge and skills, by the development of individuals, some from disadvantaged backgrounds, and by contributing to the cultural and civic life of a region and the nation. The funding to support these activities is equally widely defined, and encompasses government grants, tuition fees from students, grants from the private and charity sectors, and income from a wide range of sources. All of this funding is specific, to one degree or another, to the activities of the institution, and must be appropriately applied. 2

Some further and higher education institutions also derive part of their funding from charitable giving and endowments. These types of funding can be more specific to certain activities and may or may not have a greater degree of restriction in their application. Income from charitable giving and endowments, however, generally represents a minority proportion of funding, for even the most active of fund raising institutions, and is not central to the funding streams of further and higher education institutions. 3

Scope of this SORP

The recommendations in this SORP are intended to be applicable to all further and higher education institutions in the United Kingdom (referred to as institutions in this SORP). These institutions should prepare their **accounts** on an accruals basis to give a true and fair view of their financial activities in an accounting period. 4

5 Every institution should prepare, on an annual basis, *financial* statements as defined in paragraph 15 and related reports and statements as defined in paragraph 24.

6 Institutions following this SORP should apply all extant accounting and financial reporting standards, UITF Abstracts, relevant legislation and accounts directions from the *Funding Bodies* applicable to the reporting institution. When a financial reporting standard, UITF Abstract, relevant legislation or accounts direction is issued after publication of the most recent edition of this SORP, any of the provisions of the SORP that conflict with the new standard, UITF Abstract, accounts direction or relevant legislation will cease to have effect. This SORP is drafted on the basis of UK accounting standards which the SORP Board believes are appropriate for institutions. In the unlikely event that an institution is required to comply with International Financial Reporting Standards, then it should comply with this SORP as far as possible and disclose the nature of any departure.

Background

7 Further and higher education institutions are complex organisations whose main activities are teaching and research. They are autonomous bodies established by Royal Charter, Act of Parliament or other instrument. Teaching is provided for students from the United Kingdom, the European Union (EU) and other nations across the whole range of academic and vocational subjects. As well as full-time and part-time education, institutions also provide special and short courses for vocational and non-vocational continuing education. Research is carried out within most higher education institutions.

8 In addition to teaching and research, institutions frequently have a range of distinctive activities which are in addition to their main activities, including knowledge transfer, the provision of student residences, catering and other services. Many have established limited liability companies, consortia, partnerships or *joint ventures* to carry out particular kinds of collaborative and commissioned teaching, training and research and other income generating and commercial activities.

Funding

9 Institutions receive their funding from three main sources:

(a) public funds in the form of grants direct from the responsible *Funding Bodies*, student tuition fees paid from public funds, research grants and contracts awarded by research councils, non-UK public sector bodies and government departments. In certain cases, funding is received directly from government departments or agencies; many institutions also receive significant funds from non-UK public sector bodies for the provision of education, training and related services;

(b) the provision of other contract and research services and consultancy, conference and accommodation facilities, staff/student residences and catering, and tuition fees paid wholly or partly by students or employers; and
(c) bequests, endowments and donations which may be for general purposes, or restricted by legally binding conditions to specific purposes.

Regulatory framework

Further and higher education institutions operate in a regulatory framework which, while broadly similar also varies depending on the different requirements of the UK *Funding Bodies*, charity regulators and the various elements of legislation which created each funding body. 10

Each funding body issues an annual accounts direction. In all cases these accounts directions require institutions' *financial statements* to be prepared in accordance with this SORP. The accounts directions also provide information about those disclosures required by the *Funding Bodies* over and above those required by this SORP and UK GAAP. These disclosures usually include items such as a statement of corporate governance, the emoluments of the vice-chancellor or principal, the number of higher paid staff, and details of any compensation for loss of office paid to higher paid staff. 11

2. The financial statements and related reports

Objectives of an institution's financial statements and related reports

12 The objective of *financial statements* and related reports is to provide information that gives a true and fair view of the financial performance and financial position of the reporting institution or *group* that is useful to a wide range of users for assessing the stewardship of the institution's management and for making economic decisions. There are many different users of an institution's *financial statements*. These users include:

(a) the governing body of the institution;
(b) the *Funding Bodies*;
(c) government departments, Parliament, and charity regulators;
(d) the institution's employees (past, present and future);
(e) the institution's students (past, present and future);
(f) lenders and creditors;
(g) other institutions, schools and industry;
(h) grant-awarding bodies, donors and benefactors; and
(i) the general public.

13 The objective set out in paragraph 12 above can usually be met by focusing exclusively on the information needs of *funders and financial supporters*, the defining class of user of the *financial statements*. From the list in paragraph 12 this would include the *Funding Bodies*, government departments, grant awarding bodies, donors, benefactors and the institution's students. Published *financial statements* should give a true and fair view of the institution's financial performance and financial position so that they may be of use, and relied upon, by *funders and financial supporters*. Reports should be consistent with the *financial statements*.

14 *Funders and financial supporters* may have differing needs in detail, but there are certain key characteristics of financial information which are applicable to all, ie *financial* information must be relevant, reliable, comparable and understandable. The main objectives of the *financial statements* and related reports (see paragraph 15 for the *financial statements* required) are, therefore, to provide the following information:

(a) a true and fair view of the financial position of the institution at the balance sheet date and of the income and expenditure, total recognised gains and losses and cash flows for the period then ended;
(b) an explanation of the corporate governance of the institution and an appropriate statement of responsibilities;
(c) a suitable analysis and appropriate disclosure of:
    i. the income from all sources within the period of the account;
    ii. the expenditure on all activities within the period of the account;
    iii. the *assets* and *liabilities* of the institution, classified in suitable form as required by this SORP;

iv. any known or probable circumstances which might significantly affect the institution's financial position; and
v. how the institution is performing financially, including the adequacy of its working capital, its solvency (or insolvency), and its investment performance.

Financial statements

Institutions' *financial statements* should include the following: 15

(a) a statement of principal *accounting policies* and *estimation techniques* (if not provided in the notes to the accounts);
(b) an income and expenditure account - presenting the financial performance of an institution during the accounting period (see Appendix 2);
(c) a statement of historical cost surpluses and deficits (see Appendix 2) – if there is no material difference between the surplus or deficit on an historical cost basis and the result for the year, a statement to this effect should be made below the income and expenditure account and may replace the primary statement;
(d) a balance sheet presenting the financial position of an institution at the end of the accounting period (see Appendix 2);
(e) a consolidated cash flow statement (see Appendix 2);
(f) a statement of total recognised gains and losses if appropriate (see paragraph 16 and Appendix 2); and
(g) notes to the *accounts* (see Appendix 3).

Statement of Total Recognised Gains and Losses

The statement of total recognised gains and losses is required by FRS 3 and will be necessary where institutions revalue their *tangible fixed assets* – see paragraphs 76 to 79 of this SORP on revaluation. It will also be necessary for the recognition of *actuarial gains and losses* in relation to *defined benefit schemes* on the full adoption of FRS 17 required by this SORP. In the unusual event that there have been no recognised gains or losses other than those included in the income and expenditure account, a statement to this effect should be made immediately below the income and expenditure account and may replace the primary statement. 16

Notes to the accounts

17 Appendix 3 to this SORP provides a list of the expected items which may be included in an institution's notes to the *accounts*. This list is not intended to be exhaustive but should be used as a guide for the notes which may be required to address the following:

(a) the basis of preparation of the *accounts* and all significant *accounting policies* and *estimation techniques* (if not provided in a separate statement as part of the financial *statements*);
(b) information and relevant disclosures specified by *financial reporting* and accounting standards or UITF Abstracts;
(c) any additional information that is relevant to ensure that the *financial statements* present a true and fair view; and
(d) the requirements of the Companies Acts (if applicable) and the *accounts directions* from the UK *Funding Bodies* relevant to the institution.

Preparation of the financial statements

18 The *financial statements* should be prepared using the historical cost convention as modified for the revaluation of certain *assets* (see paragraphs 76 to 79 of this SORP). Where *assets* have been revalued, a note of historical cost surpluses and deficits should follow the income and expenditure account as set out in FRS 3 'Reporting Financial Performance' (see Appendix 2) or the statement of total recognised gains and losses. The note will be necessary where an institution includes *tangible fixed assets* or investments at valuation and there is a material difference between the surplus or deficit reported in the income and expenditure account and that which would have been reported on an unmodified historical cost basis.

19 The *financial statements* should contain a positive statement that they are prepared in accordance with applicable accounting standards and this SORP and any material departures there from should be explained clearly in the financial statements.

20 This SORP is prepared on the basis that International Financial Reporting Standards (IFRS) will not be applied by further and higher education institutions and has been prepared solely on the basis of UK GAAP.

Group accounts

21 The *consolidated financial statements* should give a true and fair view of the state of affairs of the group and the institution at the balance sheet date and of the *group's* results and total recognised gains and losses and cash flows for the year then ended, whether channelled through the institution as an entity or through one or more *associates*, *joint venture* entities or *subsidiary undertakings*. The *group's financial statements* should follow the format specified in paragraph 15 and set out in Appendix 2 to this SORP.

All institutions must comply with the financial reporting requirements contained in any UK legislation relevant to their constitution. In addition, compliance with an accounts direction, issued by the lead funding body, is a condition of grant to the extent that it does not contradict this SORP. Where an institution or its subsidiary is constituted as a company, the *financial statements* must be properly prepared in accordance with the provisions of the Companies Act. Where a separately established *subsidiary undertaking* is a charity, that subsidiary's *financial statements* should comply with the disclosure requirements of the Statement of Recommended Practice 'Accounting and Reporting for Charities', subject to the requirements of paragraph 220 of this SORP. 22

Interaction with the Charities SORP

The ASB Statement 'SORPs Policy and Code of Practice' states "where a SORP making body is aware that entities to which the SORP applies may also fall within the scope of another SORP it will be useful to indicate which SORP should apply". The Statement of Recommended Practice 'Accounting and Reporting for Charities' notes that "Where a separate SORP exists for a particular class of charities (e.g. ... to Further and Higher Education institutions), the trustees of charities in that class should adhere to that SORP and any reporting requirements placed on such charities by charity law". The SORP Board agrees with this statement as the further and higher education sector has special financial and reporting issues that are different from other organisations that have charitable status, and therefore in such cases the requirements of the SORP 'Accounting for Further and Higher Education' should take precedence over the SORP 'Accounting and Reporting for Charities' for such institutions. 23

Related reports and statements

The financial statements will be published with related reports. These will include the following: 24

(a) the *Operating and Financial Review* (which may also be called a treasurer's report, members' report, directors' report or report of the governing body);
(b) a statement of corporate governance and internal control;
(c) a statement of responsibilities of the governing body (if not included in the statement of corporate governance), and
(d) an independent auditors' report.

Operating and financial review

25 The SORP Board considers that an *Operating and Financial Review* (OFR) should be included in the report and *financial statements*. This review should provide an overview of the institution's finances and operations and should follow best practice as set out in the Reporting Statement 'The *Operating and Financial Review'* issued by the Accounting Standards Board in January 2006. Specifically the OFR should provide a comprehensive and balanced analysis, consistent with the size and complexity of the institution, of:

(a) the development, performance and operation of the business and operation of the institution during the financial year;
(b) the position of the institution at the end of the year;
(c) the main trends and factors underlying the development, performance and position of the business of the institution and its academic performance during the financial year; and
(d) the main trends and factors which are likely to affect the institution's future development, performance and position.

26 The OFR should be produced in accordance with the following principles, in that it should:

(a) set out an analysis of the institution through the eyes of the institution's governing body (or equivalent);
(b) focus on matters that are relevant to the interests of *funders and financial supporters*;
(c) have a forward-looking orientation, identifying those trends and factors relevant to the *funders and financial supporters*' assessment of the current and future performance of the institution and the progress towards the achievement of long-term academic and business objectives;
(d) complement as well as supplement the financial statements, in order to enhance the overall corporate disclosure;
(e) be comprehensive and understandable;
(f) be balanced and neutral, dealing even-handedly with both good and bad aspects; and
(g) be comparable over time.

27 The OFR should provide information to assist *funders and financial supporters* to assess the strategies adopted by the institution and the potential for those strategies to succeed. The key elements of the disclosure framework recommended to achieve this are, where significant:

(a) the nature of the institution including a description of the competitive and regulatory environment in which it operates, and the institution's objectives and strategies;
(b) the development and performance of the institution, both in the financial year under review and in the future;
(c) the resources, principal risks and uncertainties and relationships that may affect the institution's long-term financial position; and
(d) the position of the institution including a description of the long-term financing, treasury policies and objectives and liquidity of the institution both in the financial year under review and the future.

The form and content of the OFR is not prescribed, the principles set out in paragraph 26 above set a framework for the disclosures to be provided by the governing body (or equivalent) in the OFR. The institution's governing body (or equivalent) should consider how best to use the framework to structure the OFR and the precise content, including the level of detail to be disclosed, relating to the key elements set out in paragraph 27, given the particular circumstances of the institution. Where appropriate, the form and contents may be prescribed by relevant UK legislation. For example, certain institutions are incorporated under the Companies Act and as such will have a requirement to produce a directors' report, including a business review; however, that requirement should be met if the best practice set out in the Reporting Statement is followed. 28

Summary financial information

Where summary financial information of any kind is prepared (including financial information contained in publicity or fundraising material and annual reviews), institutions are reminded that this information should always be fair and accurate. 29

Some institutions publish financial information or summaries in a format different from the full *financial statements*. There are two basic types of such summaries: 30

(a) Summarised *financial statements* which should be based on the full *financial statements* and communicate key financial information without providing the greater detail required in the full *accounts* (for example, as contained in the notes to the *accounts*); and
(b) Summary financial information which presents information on a particular aspect of an institution's finances for example, an analysis of incoming resources or expenditure on particular activities of an institution. Such information does not purport to summarise the full *financial* statements.

31 The distinction between summarised *financial statements* and summary information is as follows:

Characteristics of Summarised Financial Statements:	**Characteristics of Summary Financial Information:**
Includes a summary of the income and expenditure account and/or balance sheet	Draws information from only parts of the annual *accounts*
The summary is derived from the annual *accounts*	May be based on interim *accounts* or other financial information as well as the annual *accounts*
A financial statement that purports to be an income and expenditure account or balance sheet or summary thereof	Makes no reference to either of these primary statements
Represents the entire finances of an institution or *group*	Represents analysis, e.g. of a particular activity

32 As the form in which such information or summaries will be produced will vary considerably, depending on the purpose for which they have been prepared, it is not practicable to give detailed recommendations on the content of summary financial information or summarised *financial statements*. The general principles which should be followed are set out below.

Summarised Financial Statements

33 Summarised *financial statements* should:

(a) contain information on both the income and expenditure account and the balance sheet;
(b) be consistent with the annual *accounts*; and
(c) not be misleading by either omission or inappropriate amalgamation of information.

Summarised *financial statements* should also be accompanied by a statement, signed on behalf of the governing body, indicating: 34

(a) that they are not the full *financial statements* but a summary of information relating to both the income and expenditure account and the balance sheet;
(b) whether or not the full *financial statements* from which the summarised *financial statements* are derived have as yet been audited by an independent external auditor; and
    i. where they have been externally audited, whether the report of the independent external auditor contained any concerns such as a qualified opinion, limitation of scope, etc;
    ii. where the report contains any concerns, e.g. is qualified, contains an explanatory paragraph or emphasis of matter, sufficient details should be provided in the summarised *financial statements* to enable the reader to appreciate the significance of the report;
(c) details of how the full *financial statements* and the independent external auditor's report can be obtained; and
(d) the date on which the full *financial statements* were approved.

Where institutions are registered under the Companies Act then they should also have full regard to the additional legislative requirements for their summary financial information. 35

If the full accounts have been externally audited, a statement from the independent external auditor, giving an opinion as to whether or not the summarised *financial statements* are consistent with the full *financial statements*, should be attached. 36

Summary Financial Information

Any other summary financial information, in whatever form, should be accompanied by a statement on behalf of the governing body as to: 37

(a) the purpose of the information;
(b) whether or not it is from the full annual *financial statements*;
(c) whether or not these *financial statements* have been audited; and
(d) details of how the *financial statements* can be obtained.

Summary financial information will not necessarily contain information on both the income and expenditure account and balance sheet but should nevertheless present information consistent with the annual *accounts* and not be misleading by either omission or inappropriate amalgamation of information. 38

Statement of corporate governance and internal control

39 The SORP Board considers that it is best practice to produce a statement of corporate governance and internal control with the *financial statements*, and this is specifically required by some *Funding Bodies* in their accounts directions. In preparing their corporate governance statement institutions should consider the best practice guidance issued by *Funding Bodies*, including the requirement to publish details of their systems of internal control and how such a system is linked to institutional objectives and implemented across the organisation. Guidance is also available from the British Universities Finance Directors Group (BUFDG) on the production of a statement of corporate governance, and this is available on the BUFDG website at http://www.bufdg.ac.uk. Institutions should ensure as a minimum that they comply with the requirements of the accounts directions from the *Funding Bodies*.

3. Accounting principles

Application of accounting policies and estimation techniques

The *accounting policies* on which the *financial statements* of an institution are produced should be in accordance with applicable accounting standards and UITF Abstracts in force (see also paragraph 6) and consistent with the requirements to present a true and fair view. It is not considered to be appropriate for institutions to base their *accounting policies* on the requirements of International Financial Reporting Standards (IFRS) except where the requirements of IFRS have already been incorporated into UK GAAP. In the unlikely event that an institution is required to comply with IFRS then it should comply with this SORP as far as possible and disclose the nature and effect of any departure from this SORP. 40

This SORP also sets out that the *accounting policies* are for material items only. Where the standards or this SORP permit choice, the most appropriate policy for providing a true and fair view should be selected. The institution should judge the appropriateness of *accounting policies* and any selection of policies to its particular circumstances against the objectives of relevance, reliability, comparability and understandability. 41

The constraints that an institution should take into account in judging the appropriateness of *accounting policies* to its particular circumstances are: 42

(a) the need to balance the four objectives (relevance, reliability, comparability and understandability) set out in paragraph 41 above; and
(b) the need to balance the cost of providing information with the likely benefit of such information to users of the institution's *financial statements*. However, paragraph 6 states that *accounting policies* should be consistent with the requirements of accounting standards, UITF Abstracts and the SORP. Accordingly, cost and benefit considerations will not justify the adoption of an accounting policy that is inconsistent with those requirements.

An institution should regularly review its *accounting policies* to ensure that they remain the most appropriate to its own particular circumstances. Where this is judged not to be the case, a new policy should be adopted giving due weight to the impact a change in accounting policy would have on comparability between periods. 43

Institutions should apply the disclosure requirement of FRS 18 'Accounting Policies' ensuring appropriate disclosure of *accounting policies* and *estimation techniques* have been made. Sufficient information should be disclosed within the *financial statements* to enable users to understand the *accounting policies* adopted and how they have been implemented. 44

45 Where *estimation techniques* are required to enable the *accounting policies* adopted to be applied, an institution should select *estimation techniques* that enable its *financial statements* to give a true and fair view and are consistent with the requirements of accounting standards, UITF Abstracts and this SORP.

4. Application of accounting policies

Introduction

As stated in paragraphs 6 and 41 to 42 of this SORP, institutions should prepare their *accounts* in accordance with extant UK financial reporting and accounting standards, UITF Abstracts, relevant legislation and the *accounts* directions so that their *financial statements* present a true and fair view of the financial activities of the institution. 46

This section provides guidance on the selection and application of *accounting policies*, as well as applying UK accounting standards and other relevant guidance to situations specific to the further and higher education sector. 47

The following guidance on *accounting policies* is consistent with the accounting concepts and principles referred to in the previous section and should be followed in respect of the recognition of transactions as income and expenditure, and balances as assets, *liabilities or funds* in the *financial statements* of institutions. 48

This section is organised so as to broadly follow the format of the primary statements. 49

Income recognition

Income received by institutions falls into two broad categories and should be accrued for and recognised in the income and expenditure account in the period to which it relates: 50

(a) income which can be applied at the discretion of the institution to any of its activities; such income is referred to as *'general income'* and examples include recurrent grant from the *Funding Bodies* (which may have some restrictions), student tuition fees and income earned by the institution from its activities; and

(b) income which is for specific purposes, such purposes being designated by the grant-making body, contractor or donor under a specific agreement or contract, and which can only be applied for those specific purposes. Examples include the income from research grants and contracts, grants for specific purposes, restricted endowment income, and restricted charitable donations. Such income is only credited to the income and expenditure account when the conditions attaching to its receipt have been met. Often the conditions relate to undertaking a specific programme of work for which the most appropriate proxy measure may be incurring the appropriate expenditure, including expenditure on indirect costs. As noted in paragraph 14 (c) the *financial statements* should include disclosure of income from all sources within the period of account. Reference should also be made to the requirements of UITF Abstract 40 'Revenue recognition and service contracts', the requirements of which are also referred to in paragraph 161.

51 Application Note G to FRS 5 'Revenue Recognition' requires that revenue should be recognised only when a 'right to consideration exists' and states that such a right will exist only to the extent that performance of the contractual obligation has taken place. Any payments received in advance of such performance should be recognised on the balance sheet as *liabilities*. The application note also gives guidance on the following specific complex situations that give rise to revenue:

(a) long-term contractual performance;
(b) separation and linking of contractual arrangements;
(c) bill and hold arrangements;
(d) sales with right of return; and
(e) presentation of turnover (income) as principal or agent (see paragraph 55 below).

Accounting for grants

52 Revenue-based grants from government and other bodies should be passed through the income and expenditure account when the conditions relating to the grant have been satisfied (see paragraph 50 above).

53 Grants or other contributions from government and other bodies should be accounted for on an accruals basis and recognised in the *accounts* when the conditions for their receipt have been complied with and there is reasonable assurance that the grant or contribution will be received.

Deferred capital grants

54 Where an institution receives a grant to finance, or partly finance, the purchase, construction or development of an asset, and the asset is capitalised, the grant should be credited to *deferred capital grants* and an annual transfer made to the income and expenditure account over the useful economic life of the asset at the same rate as the *depreciation* charge on the asset for which the grant was awarded. Such grants effectively subsidise future activities and just as the revenue (if any) from those activities is recognised in the accounting periods over which the services are provided, so the grant should be released to income over the estimated useful life of the *assets* whose *acquisition* has been subsidised by the grant. Furthermore, the condition that normally has to be satisfied for the recipient to comply with the terms of the grant is that the capital item should be used for the purposes for which the grant was given rather than merely being acquired for future use to support that purpose: the best measurement of usage is by apportioning the benefit of the grant over the estimated useful life of the asset and thus releasing it to income over that period. This is achieved by crediting the grant to *'deferred capital grants'*, disclosed on the funds side of the balance sheet separately from endowments and reserves, and released to income over the estimated useful life of the related asset.

Agency arrangements

Application Note G to FRS 5 'Revenue Recognition' gives guidance on situations where institutions act as a principal or agent. Where the institution is an agent it would not normally be exposed to the majority of the benefits and risks associated with the exchange transaction (including performance of the transaction, price or credit risk). Where the institution disburses funds it has received as paying agent on behalf of a funding body or other body, and has no beneficial interest or risks related to the receipt and subsequent disbursement of the funds, these funds should be excluded from the income and expenditure of the institution. Any commissions received whilst acting as agent would be included as income. 55

Institutions should provide a memorandum disclosure note, if required by the funder, on *agency funds* in the notes to the *accounts* which shows movements on the funds during the year, and any unspent balances at the year-end. 56

Accounting for tuition fees

Institutions should recognise tuition fees when the rights to consideration exist and contractual performance has taken place. 57

Where tuition fees are rebated (for example, through a prompt payment reduction) consideration needs to be given to the substance of the transaction. Application note G to FRS 5, 'Reporting the substance of transactions', on revenue recognition states that revenue is measured 'at the fair value of the right to consideration and this is normally the price in the contract, net of discounts'. Where the amount of the tuition fee is reduced, or in substance, the right to consideration of tuition fees is reduced, income receivable should be shown net of the discount. 58

Such tuition fee discounts are different from bursary payments, and reference should also be made to the guidance on accounting for bursaries below. 59

Accounting for bursaries and scholarships

A bursary or scholarship is a payment made to a student from an institution's own funds. These payments are made to students dependent on certain criteria, such as the financial position of the student. Such criteria are determined through the institution's internal policies, or may be determined by regulatory bodies. 60

It is expected that bursaries and scholarships will be accounted for gross as expenditure and will not be netted off fee income. This reflects the nature of the transaction, which will be a payment of funds by the institution. 61

62 Where bursaries or scholarships are paid from *endowment funds*, reference should be made to the accounting and disclosure requirements set out in paragraphs 132 to 158.

63 Bursaries paid from the funds of third parties, where the institution is acting in an agency capacity, should be accounted in accordance with the guidance provided under the section 'Agency Arrangements' in paragraphs 55 to 56.

Segmental reporting

64 SSAP 25 'Segmental Reporting' requires the disclosure of income, segment result and segment net *assets* by class of business and geographical segment where material other segments exist.

65 Institutions normally undertake one class of academic activity, which includes both teaching and research. This activity is undertaken by the same staff using the same premises and is financed by the same income streams. Institutions may also have significant other activities undertaken by different staff using different premises and financed by other income streams. In a minority of cases institutions may have material segments of other activities (such as a university press) or significant geographical operations (such as those in another territory) where SSAP 25 should be applied.

Accounting for Value Added Tax (VAT)

66 Irrecoverable VAT on inputs should be included in the costs of such inputs. Any irrecoverable VAT allocated to *tangible fixed assets* should be included in their cost.

Accounting for current and deferred tax

67 All institutions are charities, either registered with the Charity Commission or the Office of the Scottish Charities Regulator, or exempt charities within the meaning of Schedule 2 of the Charities Act 1993, and as such are charities within the meaning of Section 506(1) of the Taxes Act 1988. Institutions are therefore potentially exempt from taxation in respect of income or capital gains received within categories covered by Section 505 of the Taxes Act 1988 and Section 256 of the Taxation of Chargeable Gains Act 1992 to the extent that such income or gains are applied to exclusively charitable purposes.

68 It is therefore unlikely that deferred tax will have significant implications for institutions. However, subsidiary entities (where their activities are not charitable) must comply with FRS 19 and recognise deferred tax on any timing differences that have originated and not reversed by the balance sheet date. This deferred tax will then need to be consolidated in the *group financial statements.*

Institutions must ensure that they consider any taxable activities which might arise as a result of their relationships with subsidiary companies that pay corporation tax. In such cases deferred tax should be recognised in respect of any or all timing differences that have originated but not reversed by the balance sheet date, except as required otherwise by FRS 19. Deferred tax should not be recognised on permanent differences. 69

Accounting for tangible fixed assets

Initial measurement

Tangible fixed assets should be initially measured at cost, including irrecoverable VAT. Only those costs that are directly attributable to bringing the asset into working condition for intended use should be included in its measurement. 70

Repairs and maintenance

Expenditure to ensure that a tangible fixed asset maintains its previously recognised standard of performance should be recognised in the income and expenditure account in the period in which it is incurred. 71

Enhancement

Tangible fixed assets being enhanced should be treated as set out in FRS 15 'Tangible Fixed Assets': 72

(a) costs incurred in relation to a tangible fixed asset after its initial purchase or production should be capitalised to the extent that they increase the expected future benefits to the institution from the existing tangible fixed asset beyond its previously assessed standard of performance;

(b) the cost of any such enhancements should be added to the gross carrying amount of the tangible fixed asset concerned.

Recognition of tangible fixed assets

Tangible fixed assets should be capitalised and should be included in the balance sheet at cost or valuation. 73

Classification of tangible fixed assets

74 Classes of tangible fixed assets should follow the classifications required by the Companies Act . The four classes are:

(a) land and buildings;
(b) plant and machinery;
(c) fixtures, fittings tools and equipment; and
(d) payments on account and assets in the course of construction.

A fifth class of *'heritage assets'* may also be required, subject to the provisions set out in paragraphs 100 to 104 below.

75 These classes may be subdivided according to definitions arising from an institution's operations. For example, the land and buildings class of *assets* might be subdivided into teaching facilities, research laboratories and student accommodation.

Revaluation

76 Where an institution adopts a policy of revaluation, paragraphs 42 and 61 of FRS 15 require that revaluations should be applied to entire classes of *tangible fixed assets*, but need not be applied to all classes of *tangible fixed assets*. This means that where an individual tangible fixed asset is revalued, then all other *tangible fixed assets* in the same class must be revalued.

77 Increases in value should be taken to the *revaluation reserve* except to the extent that they reverse revaluation losses on the same asset that were previously recognised in the income and expenditure account, in which case they should be recognised in the income and expenditure account.

78 All revaluation losses caused by a clear consumption of economic benefits should be recognised in the income and expenditure account. Other decreases in valuation (not caused by the clear consumption of economic benefits) should first be set against any previous revaluation surplus for that asset. Thereafter, they should be reported in the income and expenditure account unless it can be demonstrated that the *recoverable amount* of the asset is greater than its revalued amount, in which case the loss should be recognised in the statement of total recognised gains and losses to the extent that the *recoverable amount* of the asset is greater than its revalued amount.

79 Valuations must be updated on a regular basis with a professional valuation being undertaken by a *qualified valuer* at least every five years. An interim valuation should be carried out in the third year after a full valuation by a *qualified valuer* who may be either internal or external to the institution. Institutions should ensure that the carrying value of assets in the accounting periods between valuations is materially accurate.

Basis of valuation

Where a tangible fixed asset is subject to a policy of revaluation its carrying amount should be its *current value* as at the balance sheet date. 80

The following valuation bases should be used for revalued properties that are not impaired: 81

(a) non-*specialised properties* should be valued on the basis of *existing use value* (EUV), with the addition of notional directly attributable *acquisition* costs where material. Where the *market value* (MV) is materially different from EUV, the MV and the reasons for the difference should be disclosed in the notes to the *accounts*;
(b) specialised properties should be valued on the basis of depreciated replacement cost;
(c) properties surplus to an entity's requirements should be valued on the basis of MV, with expected directly attributable selling costs deducted where material.

For valuing land and buildings, the RICS Valuation Standards provide detailed guidance on the valuation requirements of FRS 15 The method used for the valuation and name and qualification of the valuer should be disclosed in the notes to the *accounts*. If land is held specifically for development, investment and subsequent sale then the requirements of the section on 'Investment properties' (paragraphs 114 and 115 below) should be followed. 82

Tangible fixed assets other than properties should be valued using *market value*, where possible. Material notional directly attributable *acquisition* costs should be added. If *market value* is not obtainable, *assets* should be valued on the basis of *depreciated replacement cost*, in accordance with paragraph 60 of FRS 15. 83

Disclosures

In addition to the disclosure requirements set out in paragraph 74 above and paragraph 88 below there are detailed disclosure requirements for each class of revalued *tangible fixed assets* which should be disclosed in accordance with paragraph 74 of FRS 15. 84

Institutions should also provide the disclosures required by paragraph 100 of FRS 15 for each *class of tangible fixed assets*; ie the *depreciation* methods and rates used, an analysis of cumulative provisions for depreciation and a reconciliation of movements of *tangible fixed assets* in the accounting period. 85

Frozen valuations

FRS 15 allowed institutions to adopt transitional arrangements at the time of first adopting FRS 15 for the initial recognition of their *tangible fixed assets*. One option was to adopt a revaluation policy, the remaining two options dealt with alternatives to not adopting a revaluation policy. The accounting treatment for each option is summarised below. 86

87 Where the institution did not adopt a policy of revaluation, but the carrying amount of its tangible fixed assets reflected previous revaluations, it had two options:

(a) to restate *tangible fixed assets* to historical cost (less *depreciation*), as a change of accounting policy;
(b) to hold *tangible fixed assets* at their book amounts, subject to the requirement to test them for *impairment* in accordance with FRS 11 if an indication exists that *impairment* may have occurred – it is important to note that this option was available only on the first application of FRS 15.

88 Where the institution had opted to hold *tangible fixed assets* at their book amounts disclosure is required that the institution has taken advantage of the transitional provisions of FRS 15. The institution should disclose the date of the last valuation and the fact that the valuation had not been updated. Institutions which used this option should disclose:

(a) the amount of *tangible fixed assets* held at valuation;
(b) the years of valuation and the basis adopted;
(c) the historical cost equivalents for the revalued assets;
(d) the amount of a *revaluation* reserve and any transfers from that reserve to realised reserves;
(e) a note of historical cost profits as required by FRS 3; and
(f) disclosure of historical cost and *depreciation* – paragraph 74 (a)(iv) of FRS 15.

89 The disclosure requirements set out in paragraph 88 above can be satisfied in completion of the note of historical cost surpluses and deficits which follows the income and expenditure account and by appropriate, additional text disclosures within the notes on *tangible fixed assets* and the *revaluation reserve*. Alternatively institutions may present a separate note complying with the requirements set out in paragraph 88, (a) to (f) above.

Disposal of tangible fixed assets

90 The gain or loss arising from the disposal of *tangible fixed assets* is the difference between the carrying amount of the fixed asset and the net sale proceeds whether carried at historical cost or valuation. Gains or losses should be reported in the income and expenditure account in accordance with FRS 3. The net sale proceeds would exclude any proceeds required to be surrendered under the financial memorandum between the institution and the relevant Funding Body. Such proceeds should be included in the income and expenditure account and, if material, disclosed separately in line with accounting standards. Any proceeds which an institution is required to surrender should be specifically identified and disclosed in the *financial statements*.

Depreciation

Depreciation of all *tangible fixed assets* should be provided for in accordance with FRS 15. Exceptions to charging *depreciation* may only arise if either the asset is freehold land, or if neither the charge nor the accumulated *depreciation* is material (but it should be noted that in this latter case, the asset should be subject to an annual *impairment* review in accordance with FRS 11). 91

Depreciation should be based on the amount at which the tangible fixed asset is included in the balance sheet, (except for freehold land which should not be depreciated as noted in paragraph 91 above). In establishing the estimated useful life of an asset, the level of maintenance expenditure, which may have an effect on the asset life, and the consequent rate of *depreciation* should be considered. If material, a depreciable asset's anticipated useful economic life must be reviewed annually and the accumulated and future depreciation adjusted in accordance with FRS 15. 92

Subsequent expenditure on a tangible fixed asset which maintains or enhances the previously assessed standard of performance of the asset does not negate the need for *depreciation*. 93

Component accounting

FRS 15 requires that where a tangible fixed asset comprises two or more major components with substantially different useful economic lives, each component should be accounted for separately for *depreciation* purposes and depreciated over its individual useful economic life. For example, a building should be split for *depreciation* purposes between the structure of the building and items within the structure, such as general fittings. The requirements of FRS 15 to capitalise and depreciate separately the components of what could previously have been treated as a single item ensures that the *assets* are charged to the income and expenditure account over the periods in which they are consumed. 94

Assets used by institutions

A number of institutions occupy premises which are owned by other bodies and for which no rental or a nominal rental is made. In some cases there may be no formal agreement to occupy. Where an institution enjoys the use of an asset which it does not own and for which no rental or a nominal rental is paid, whether or not such use is regulated by a licence or lease, the *financial statements* must disclose this and, if practicable, a value should be attributed to this benefit and be capitalised, with a corresponding credit to *deferred capital grants* (which should subsequently be released to the income and expenditure account in accordance with paragraph 54), and thereafter depreciated over the period of use (see also the accounting principles applied to gifts in kind in paragraphs 154 to 156). Where no formal occupancy agreement exists, the institution should consider regularising the position by the establishment of a lease or licence, as this will assist in determining a value for the benefit. 95

Assets held for resale

96 *Tangible fixed assets* surplus to requirements should be held at the lower of cost and *net realisable value. Net realisable value* will normally be the market value, with expected directly attributable selling costs deducted if material.

97 Where an institution has *tangible fixed assets* which are surplus to requirements in the long term, these should be tested for *impairment* under the provisions of FRS 11. Where it can be shown that an *impairment* has occurred, these assets should be written down in value.

98 Where an institution is committed to the disposal of a tangible fixed asset, such *assets* should be carried at cost or valuation, or written down to their *net realisable value*, whichever is lower. Where all the following criteria are met, such *assets* should be transferred from fixed assets to current *assets* (at their existing carrying value subject to *impairment* as noted above):
(a) the asset is not being replaced;
(b) there is a commitment to sell the asset (e.g. being advertised for sale);
(c) the asset is no longer in use.

99 Where a transfer to current assets takes place then any subsequent material profit or loss on disposal of the assets should be disclosed as an exceptional item after the operating result in the income and expenditure account.

Heritage assets

100 A *heritage asset* is an asset with historic, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture. FRS 15 requires that all tangible fixed assets should be capitalised in the balance sheet and, in principle, this includes *heritage assets*.

101 For financial reporting purposes, historic assets used by the institution itself and corporate art are not *heritage assets*. Historic *assets* used to deliver the institution's operations (i.e. teaching, training or research) should be accounted for in line with the guidance provided in this SORP on *tangible fixed assets*.

102 Newly purchased *heritage assets* should be initially measured and recognised at their cost.

103 When *heritage assets* were acquired in past accounting periods and not capitalised, it may be difficult or costly to attribute a cost or value to them. In such cases these *assets* may only be excluded from the balance sheet if 'reliable cost information is not available and conventional valuation approaches lack sufficient reliability' or significant costs are involved in the reconstruction or analysis of past accounting records or in valuations which are onerous compared to the additional benefit derived by users of the *accounts*.

Information on *heritage assets* (whether or not they have been capitalised) should be given in the notes to the *accounts*. The notes should contain: 104

(a) an analysis or narrative that enables the user to appreciate the age, scale and nature of the *heritage assets* held and the use made of them;
(b) either:
    i. details of the cost (or value) of additions and disposals of *heritage assets* during the accounting period;
    or
    ii. where details of cost or value are not available (non-capitalisation in previous periods), a brief description of the nature of the *assets* acquired or disposed of, together with the sales proceeds of any disposals; and
    (c) accounting policy notes explaining the institution's capitalisation policy in relation to *heritage assets* and the measurement bases adopted for their inclusion in the accounts.

Inherited fixed assets

Where an institution has inherited *tangible fixed assets* from a local authority, these inherited *assets* should be included in the balance sheet at valuation on the date of receipt. Future valuations should be in line with the policy adopted by the institution in respect of FRS 15. In certain exceptional circumstances, it may not be possible to obtain a value for inherited or donated *assets*. FRS 15 (paragraph 18) permits an asset to be excluded from capitalisation either where no reliable cost or valuation can be obtained or where the cost of obtaining a valuation is greater than the benefit to the users of the *financial statements*. The policy must be applied on an asset by asset basis. 105

Exchequer interests

Exchequer interests in those *assets* funded through the public purse imply a retained interest in such assets by central government and its agencies. The SORP Board considers that the possibility of having to repay any funds relating to such *assets* is, in most cases, extremely remote and therefore does not expect a *contingent liability* to be disclosed in the *accounts*. 106

Website development costs

107 Design and content costs for websites that are for the general use of the institution and its staff should not be capitalised. Where an institution has developed a website to support specific teaching or training courses, or for specific research projects, then any design and content costs may be capitalised in line with UITF Abstract 29 'Website development costs', in which the capitalised costs should be amortised over the useful economic life of the courses or projects. Alternatively, such costs should be written off as incurred; this would be appropriate treatment if there were uncertainty over the life of the course or its viability. Maintenance and operating costs relating to such websites should be charged to the income and expenditure account as incurred.

Accounting for leases and hire purchase contracts

108 Disclosure should be made of the accounting polices relating to both finance and operating leases. Institutions should follow the disclosure requirements of SSAP 21 'Accounting for Leases and Hire Purchase Contracts' for both operating and finance leases and as required as lessors and lessees.

109 Institutions should recognise and capitalise material finance leases in accordance with the tests set out in the standard. A finance lease is one that transfers substantially all of the risks and rewards of ownership of a fixed asset to the lessee. Where transactions do not meet the requirements of the tests set out in the standard (the present value of the minimum lease payments does not amount to 90 per cent or more of the *fair value* of the leased asset), it should not be automatically assumed that the lease is not a finance lease. FRS 5 requires that the substance of the transaction be reflected and therefore the lease may still need to be classified as a finance lease if the institution controls access to the economic benefits of the asset.

110 Where PFI contracts (or similar funding arrangements) exhibit some of the characteristics of leases or hire purchase contracts reference should be made to the requirements of FRS 5, Application Note F.

111 Where contracts are treated as operating leases, paragraph 37 of SSAP 21 needs to be considered in terms of the proper allocation of costs to accounting periods over the period of the lease.

Accounting for investments

Listed investments held as fixed assets or *endowment assets* should be shown at *market value*. Investments in *subsidiary undertakings* should be shown at cost, subject to a review for *impairment*, in the institution's balance sheet; the *subsidiary undertaking* should be included in the consolidated balance sheet in accordance with paragraphs 206 to 216 below. Investments in *associates*, as defined in FRS 9, should be shown in the consolidated balance sheet at attributable share of net *assets* (see FRS 9, paragraph 26). *Current asset investments*, which may include listed investments, should be shown at the lower of cost and *net realisable value*. The *market value* of listed investments held as *current asset investments* should be disclosed. 112

Subject to the requirements to account for *specific income* in line with the associated expenditure (as described in paragraph 50 above), and with the exception of permanent endowments managed on a total return basis (see paragraph 150), all income from investments and capital increases/decreases arising on realisation or revaluation of investments should be treated as follows: 113

(a) income from *fixed asset investments, endowment assets* and *current asset investments* should be brought into the income and expenditure account in full as a credit. However, income derived from investment *assets* held for restricted (specific) purposes imposed by the donor or funder, as described in paragraph 50, will be recognised in the income and expenditure account in full as a credit on a receivable basis unless conditions attaching to the funding limit the institution's right to the investment income (see also paragraph 151 which deals with income earned in excess of that applied to restricted (specific) purposes);
(b) increases in value arising on the revaluation of *fixed asset investments* should be carried as a credit to the *revaluation reserve* via the statement of total recognised gains and losses; a diminution in value should be charged to the income and expenditure account as a debit to the extent that it is not covered by a previous revaluation surplus;
(c) increases/decreases in value arising on the revaluation or disposal of *endowment assets* i.e. the appreciation/*depreciation* of *endowment assets* should be added to or subtracted from the funds concerned and be accounted for through the balance sheet by debiting or crediting the *endowment asset* and crediting or debiting the *endowment fund* and should also be reported in the statement of total recognised gains and losses.

Investment properties

114 Interests in land and/or buildings that are held for their investment potential should be included in the balance sheet at their *market value* without charging *depreciation*. An investment property is an interest in land and/or buildings:

(a) in respect of which construction work and development have been completed; and
(b) which is held for its investment potential, any rental income being negotiated at arm's length.

115 The following are exceptions from the definition:

(a) a property which is owned and occupied by an institution for its own purposes is not an investment property; and
(b) a property let to and occupied by another *group* entity is not an investment property for the purposes of its own *accounts* or the *group accounts*.

Accounting for research and development

116 SSAP 13 'Accounting for Research and Development' normally applies to commercial research and development rather than higher education research. Nevertheless this SORP follows the requirements of the standard. Where institutions undertake commercial research and development they should ensure they follow the accounting treatment set out in the standard. Pure and applied research may not be treated as an asset, irrespective of the funding source. Expenditure on pure and applied research would therefore be treated as a part of the continuing activities of the institution. Only expenditure on development activities which produces new products or services with a reasonable expectation of commercial success and which satisfies the stringent criteria in paragraphs 10 to 12 of SSAP 13 can be carried forward and amortised over the period expected to benefit. Institutions should follow the disclosure requirements of paragraphs 19 and 20 of SSAP 13. Reference should also be made to the guidance provided in this SORP on accounting for *intangible assets* (see next section below).

Accounting for goodwill and intangible fixed assets

117 Positive *purchased goodwill* should be capitalised and classified as an asset on the balance sheet. Reference should also be made to the guidance provided in this SORP on *business combinations* (see paragraphs 223 to 229).

An intangible asset purchased separately from a business should be capitalised at its cost. An intangible asset acquired as part of the *acquisition* of an institution or other entity should be capitalised separately from goodwill if its value can be measured reliably on initial recognition. It should initially be recorded at its *fair value*, subject to the constraint that, unless the asset has a *readily ascertainable market value*, the *fair value* should be limited to an amount that does not create or increase any negative goodwill arising on the acquisition. 118

An internally developed intangible asset may be capitalised only if it has a *readily ascertainable market value*. The existence of funding to develop the asset is not considered to be an appropriate proxy for *market value*, and should not be used as such. 119

Where goodwill and *intangible assets* are regarded as having limited useful economic lives, they should be amortised on a systematic basis over those lives. FRS 10 'Goodwill and *Intangible assets'* has the rebuttable presumption that the useful economic life should be limited to 20 years. *Impairment* tests must be carried out at the end of the first year and thereafter subject to normal periodic reviews for indications of *impairment.* Institutions should follow the requirements of FRS 10 in relation to the method of amortisation, review of economic lives and the requirement to review positive goodwill for *impairment.* 120

If an *acquisition* of an institution or another entity appears to give rise to negative goodwill, the *fair values* of the acquired *assets* should be tested for *impairment* and the *fair values* of the acquired *liabilities* checked carefully to ensure that none has been omitted or understated. Negative goodwill remaining after the *fair values* of the *assets* and *liabilities* have been checked should be recognised and separately disclosed on the face of the balance sheet in fixed assets. 121

Negative goodwill up to the *fair values* of the non-monetary *assets* acquired should be recognised in the income and expenditure account in the periods in which the non-monetary *assets* are recovered, whether through *depreciation* or sale. 122

Any negative goodwill in excess of the *fair values* of the non-monetary *assets* acquired should be recognised in the income and expenditure account in the periods expected to be benefited. 123

Purchased goodwill (positive or negative) arising on a single transaction should not be divided into positive and negative components. 124

Institutions should comply with the disclosure requirements of FRS 10 as set out in paragraphs 52 to 60 of the FRS. 125

Impairment

126 *Impairment* arises when the higher of net recoverable value or *value in use* of an asset (or an *income generating unit*) is below its carrying value. A review for *impairment* of a tangible fixed asset or goodwill should be carried out if events or changes in circumstance indicate that the carrying amount of the asset or goodwill may not be recoverable.

127 FRS 11 'Impairment of Fixed Assets and Goodwill' requires the cost of *impairment*s to be charged on an asset by asset basis. An *impairment* loss caused by a clear consumption of economic benefit should always be recognised in the income and expenditure account in the period to which it relates. Other *impairment* losses on revalued fixed assets should be recognised in the statement of total recognised gains and losses and set against any revaluation surplus until the carrying amount of the fixed asset reaches depreciated historical cost and thereafter in the income and expenditure account.

128 Central to FRS 11 is the need to define what constitutes an '*income generating unit*' which suffers the *impairment*. Institutions will need to assess what this means for their own individual circumstances. An *income generating unit* might be an individual fixed asset, a department, school or faculty. When making this assessment the institution should consider the standard's requirements i.e. to identify *income generating unit*s into "as many largely independent income streams as reasonably practicable".

129 Institutions will need to establish appropriate indicators of *impairment* and, if there are such indications, appropriate reviews or tests of *impairment*. These reviews will determine whether there is *impairment* and quantify the financial impact for the *financial statements*. Indications of *impairment* include:

(a) operating losses;
(b) evidence of physical damage or obsolescence;
(c) a significant, adverse change in:
    i. the environment or competitive market in which an institutions fixed asset operates in for instance the entrance of a new supplier of a course or service;
    ii. the regulatory or statutory environment;
    iii. any indicator of value used to measure the *fair value* of a fixed asset on *acquisition*, for example, income streams from courses, or underperformance against the recurrent funding agreement with the funding body;
(d) a commitment by the governing body (or equivalent) to undertake a significant reorganisation;
(e) a major loss of key employees;
(f) a significant increase in market interest rates or other market rates of return that are likely to materially impact on the fixed assets recoverable amount;
(g) a significant decline in the market value of a tangible fixed asset during the period.;
(h) withdrawal from the provision of a course or service.

The standard does not discriminate between temporary or permanent *impairment*. Temporary diminutions in carrying values must be accounted for in the same way as permanent diminutions. FRS 11 requires *impairment* losses recognised in previous periods to be reversed in certain circumstances where the *recoverable amount* of the *assets* concerned subsequently increases. Where an *impairment* loss recognised in the previous period is reversed in the current period, the *financial statements* should disclose the reason for this reversal including any changes in the assumptions on the calculation of the *recoverable amount*. 130

Disclosure

Institutions should follow the presentation and disclosure requirements set out in paragraphs 67 of 73 of FRS 11 in accordance with their own circumstances. 131

Accounting for charitable donations

The governing bodies of institutions in the further and higher education sectors often, legally, oversee a number of *charitable funds* within their institution. Such *charitable funds* may be endowments, specific donations or the results of appeals. As trustees, they have a fiduciary duty to protect the *assets* of the fund, spend funds appropriately (and in accordance with any restrictions) and ensure accountability for such funds. Institutions should fully disclose within the notes to the *accounts* and any reports that accompany the *accounts* appropriate information on the nature, structure and fund balances of the *charitable funds*. 132

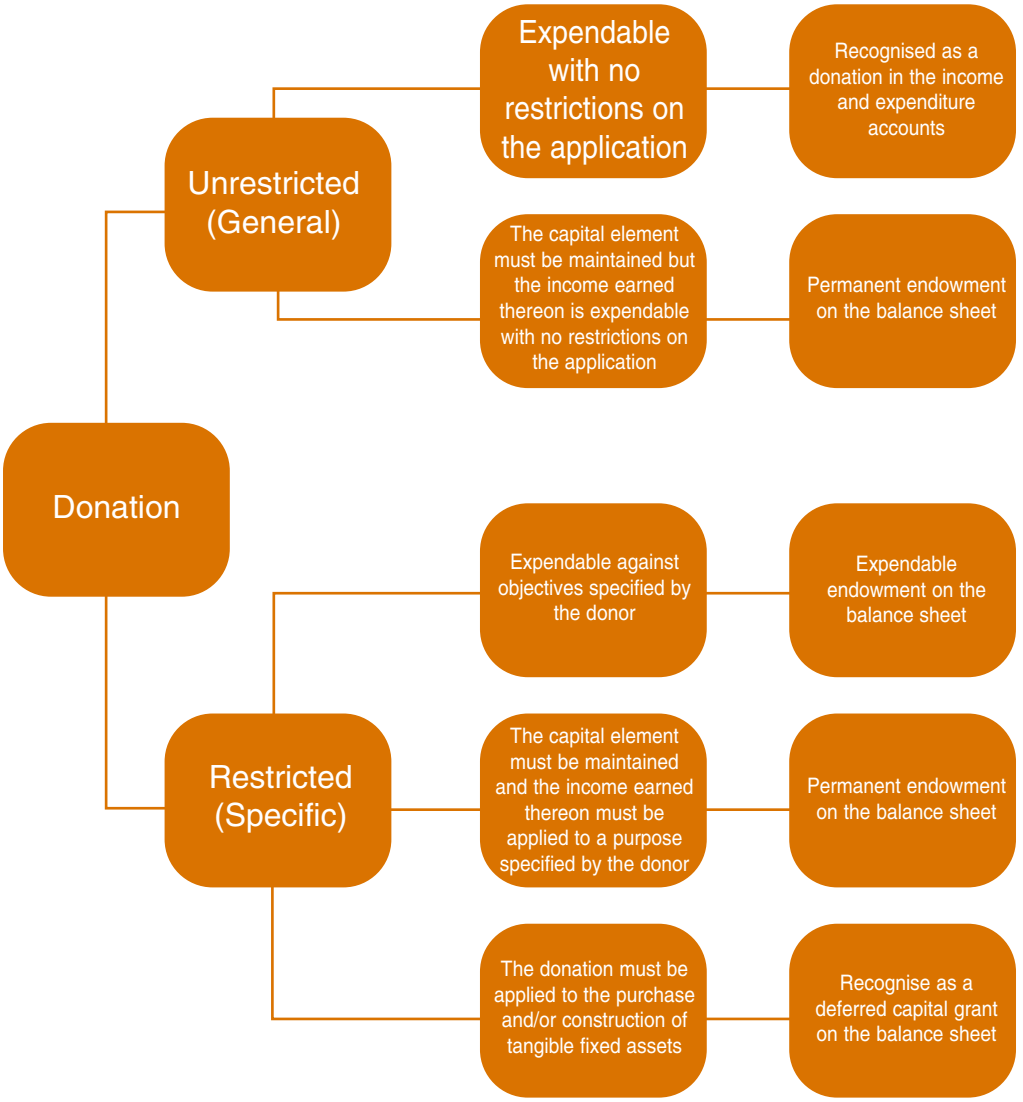
Restricted and unrestricted donations

This SORP introduces the terms 'restricted' and 'unrestricted' to distinguish how charitable donations should be accounted for to reflect the wishes of the donors. These terms are intended to correspond with the terms 'specific' and 'general' used in previous editions of this SORP, and have been adopted to assist in the clarity of the *financial statements*. The terms 'restricted' and 'unrestricted' apply to charitable donations only, and are not intended to be applied to other sources of funding as described in paragraph 50. 133

Charitable donations are classified as restricted or unrestricted by reference to the facts and circumstances surrounding the donation. Differing accounting treatments will need to be applied to reflect these classifications, and it is therefore important that institutions understand these implications when accepting donations, organising appeals or planning other fundraising activities. 134

The notes to the *accounts* should separately disclose the aggregate of those charitable donations which are restricted. Different categories of material restricted charitable donations should be disclosed where it would assist in the understanding of the financial position and performance of the institution. 135

136 A summary of the different accounting treatments applicable to charitable donations is set out in the diagram below. These are discussed in more detail in the subsequent paragraphs.



Expendable charitable donations

Where an institution receives a donation, bequest or gift with no specific terms attached to its use, it should be recorded as a charitable donation in the income and expenditure account. This type of expendable charitable donation is classified as unrestricted. 137

The institution should only recognise the charitable donation in its *accounts* when the charitable donation has been received or if, before receipt, there is sufficient evidence to provide the necessary certainty that the donation will be received and the value of the incoming resources can be measured with sufficient reliability. Where the institution has been notified of material donations e.g. legacies which have not been recognised in the income and expenditure account (because the conditions for recognition have not been met), this fact and an estimate of the amounts receivable should be disclosed in the notes to the *accounts*. 138

Many further and higher education institutions receive expendable charitable donations with specific terms attached to them which are general to the objectives of the institution. As set out earlier in this SORP, the primary activities of further and higher education institutions are teaching and research. Where the terms of the donations contain restrictions that are sufficiently general that the restriction has no material impact, the donation is, in substance unrestricted, and should be accounted for in accordance with paragraph 137 above. 139

Unapplied expendable charitable donations should not, as a matter of principle, be accumulated. Where an expendable charitable donation is given for a specific purpose, then it should be applied to that purpose as soon as practicably possible. If the expenditure is greater the institution should then apply its general funds to this purpose. This is because it is an underlying principle of charity law that income is spent within a reasonable period of receipt. 140

Where the terms of an expendable charitable donation are more specific to a certain purpose (i.e. they cannot be applied against the general activities of an institution) and there is some form of restriction placed on the donation by the donor, then they should be accounted for as an expendable endowment in accordance with the guidance set out below. For disclosure purposes, a distinction should be made between the original capital donation and any income earned thereon (accumulated income). 141

Endowment funds

An *endowment fund* is a form of charitable trust which is held on trust to be retained for the benefit of the institution. *Endowment funds* can be sub-divided into their capital element and an accumulated income fund. These two elements are further dealt with in paragraphs 151 and 152 below. 142

143 Where charitable donations are restricted to a particular objective specified by the donor, then they should be accounted for as an *endowment fund*, unless that objective is the purchase and/or construction of tangible fixed assets, in which case the donation should be recognised as a *deferred capital grant* (see paragraphs 153 and 155).

144 If a permanent capital sum (i.e. a fund which is intended to be permanently invested to generate an income stream) is provided by a donor for the general benefit of the institution, then it should also be accounted for as an *endowment fund*. In this situation, the capital fund must be maintained (and is therefore restricted) but the income thereon can be applied to the general purposes of the institution and is therefore unrestricted. Similarly, where the institution has the power to expend the capital of the *endowment* it should be accounted for as an *endowment fund*.

Permanent endowment funds

145 In many instances *endowment funds* are permanent, because the governing body, as trustees, is required to maintain permanently the capital of the *endowment fund*. Where an endowment is permanent this will be indicated by the wishes of the donor. This type of *endowment fund* cannot be spent as though it were income. Income from the *endowment funds* should be accounted for in accordance with either paragraph 150 or 151 below.

146 This concept of "permanence" does not however necessarily mean that the *assets* held in the *endowment fund* cannot be exchanged (though in some cases the trusts will require the retention of a specific asset for actual use e.g. a historic building), nor does it mean that they are incapable of *depreciation* or loss. What it does mean is that the permanent *endowment fund* cannot be used as if it were income (eg, to make payments or grants to others). However, certain payments must be made out of the *endowment fund*, such as the payment of investment management fees where these relate to investments held within the *endowment fund*. Where *assets* held in a permanent *endowment fund* are exchanged, their place in the fund must be taken by the *assets* received in exchange. "Exchange" here may simply mean a change of investment, but it may also mean, for example, the application of the proceeds of sale of freehold land and buildings in the purchase or improvement of freehold property. Operational assets, because they are used over time for the general purposes of the institution, cannot be classified as *endowment assets*.

Expendable endowment funds

147 Where charitable donations are restricted (specific) to a particular objective specified by the donor, and the governing body, as trustees, has the power of discretion to convert the endowed capital into income, then this type of charitable fund will be an expendable *endowment fund*.

148 Income from the *endowment funds* should be accounted for in accordance with paragraph 151 below. Where capital is expended this should be recognised by transferring the relevant amount from expendable *endowment funds* to general reserves. Expendable *endowment funds* should be distinguished from permanent *endowment funds* on the face of the balance sheet.

Endowment assets

149 The *assets* relating to the *endowment funds*, be they cash, bonds, equities or investment property, should be recorded as *endowment assets*. The value of *endowment assets* on the face of the balance sheet must always be equal to the total value of *endowment funds* (both permanent and expendable) shown in reserves, so as to demonstrate the matching of *assets* and funds.

Income from permanent endowment fund managed on a total return basis

150 In some instances, where they have the power to do so, institutions may apply a total return approach to investment management of permanent *endowment funds* and the accounting treatment, which will differ from that set out at paragraph 113 of this SORP and, in accordance with the Charities SORP, will be as follows. In any one accounting period, total return is the whole of the investment return received by the institution on the permanent *endowment funds*, regardless of how it has arisen, and the following approach to accounting for this should be adopted:

(a) the entire investment return initially accrues to an unapplied total return fund. That part of the investment return which has been applied in the accounting period to the restricted purposes of the permanent *endowment fund* should be recognised as 'Endowment and investment income' in the income and expenditure account. Only that part of the investment return which has been applied in the accounting period should be recognised in the income and expenditure account. The application of the investment return will be determined by any restrictions on the permanent endowment *fund*.

(b) the total return, less any part of the return which has previously been applied for the purposes of the permanent *endowment fund* (see paragraph 150 (a)), remains in the unapplied total return fund and is shown in the Statement of Total Recognised Gains and Losses. This unapplied total return fund remains part of the permanent endowment fund until such time as a transfer is made to the income and expenditure account to match the application of expenditure against the permanent *endowment fund's* purpose.

(c) the notes to the *accounts* should give particulars of the movements in the value of the aggregate unapplied total return for the whole of the accounting period. This note should reconcile the aggregate balance held as unapplied total return at the beginning with that at the end of the accounting period.

Endowment income from other funds

151 The associated endowment income should be credited to 'Endowment and investment income' in the income and expenditure account on a receivable basis. Any realised gains or losses from dealing in the related *assets* should be retained within the *endowment* in the balance sheet. Any income earned in excess of that applied to the restricted (specific) purpose should be transferred from the income and expenditure account after the result for the year has been struck to accumulated income within *endowment funds* in the balance sheet, as the institution has no right to that element of income for its general purposes because of the restrictions of the *endowment funds*. Accumulated income is a part of the *endowment fund* which is distinct from the capital element of *endowment funds*.

152 The notes to the *accounts* should disclose separately the capital value of *endowment funds* and any accumulated income that has yet to be applied to the purposes of the *endowment funds*, if material in the context of the group accounts, and this will require a prior period adjustment in the first period of application; indeed, if the accumulated income is so material that its disclosure is fundamental to the understanding of the institution's financial position then it should be shown on the face of the balance sheet within the heading of *endowment funds*. Nothing in this paragraph limits the institution's legal obligation to hold separately the capital and accumulated income in respect of individual *endowment funds*.

Donations for fixed assets

153 Where an institution receives a donation which is to be applied to the cost of a *tangible fixed asset*, and is therefore restricted to this restricted (specific) purpose, it should be shown on the balance sheet as a *deferred capital grant*. The deferred capital grant should be released to the income and expenditure account over the same estimated useful life that is used to determine the *depreciation* charge associated with the *tangible fixed asset*. Where a donation is restricted to the purchase of land (and which is therefore not subject to depreciation), then this should also be shown as a deferred capital grant until it is applied to the purchase of the land. In the accounting period in which it is applied to the purchase of the land the full amount should be released from *deferred capital grants* and the associated credit should be taken to the income and expenditure account as a donation in other income.

Gifts in Kind, including donated tangible fixed assets

154 Gifts in kind, other than *tangible fixed assets* donated for use by the institution, should be credited to donations in other income in the income and expenditure account.

155 *Tangible fixed assets*, with the exception of land, donated for use by the institution (e.g. property for its own occupation) should be valued, and the value credited to deferred capital grants and the debit taken to the relevant fixed asset category of the balance sheet when receivable. Land donated for use by the institution should also be valued, but the associated credit should be taken to the income and expenditure account as a donation in other income.

In all cases the amount at which gifts in kind are included in the income and expenditure account should be either a reasonable estimate of their gross value to the institution or the amount actually realised. 156

Disclosure of material charitable funds

Where *charitable funds* are material in relation to the *group* as a whole, disclosure should be provided in the notes to the *accounts* for each material individual *charitable fund* of: 157

(a) the *assets* and *liabilities*;
(b) income and expenditure relating to the *charitable fund*;
(c) disclosure of how each material *charitable fund* has arisen, the restrictions imposed and the purpose of the *charitable fund* should be provided. An indication should also be given as to whether or not sufficient resources are held in an appropriate form to enable the *charitable fund* to be applied in accordance with any restrictions;
(d) material transfers between different *charitable funds* should be disclosed separately, without netting off, and should be accompanied by an explanation of the nature of the transfers and the reasons for them.

Any *charitable fund* in deficit should always be disclosed separately, and an explanation provided. 158

Designated funds

There may be instances where institutions wish to designate elements of their income and expenditure account reserves to specific purposes. For the purposes of this SORP, such designations are considered to be an internal matter for each institution and therefore should not be disclosed in the primary statements or the notes to the *accounts*. 159

Accounting for stocks and long-term contracts

Stocks should be recognised in the balance sheet at cost or *net realisable value* whichever is lower in accordance with SSAP 9 'Accounting for Stocks and Long Term Contracts'. 160

Institutions should also, where relevant, apply the measurement requirements in SSAP 9 for long-term contracts, which state that it is appropriate to recognise income and gains in the income and expenditure account while contracts are in progress. These requirements should be applied in relation to research grants and contracts, European and other long-term contracts. Institutions should also refer to FRS 5 application Note G 'Revenue Recognition' which provides additional guidance on the recognition of income on long-term contracts. Institutions should consider whether any long-term projects might actually be service contracts and need to be accounted for in accordance with UITF Abstract 40 'Revenue recognition and service contracts'. 161

Accounting for financial instruments

162 The definition of financial instruments is wide and includes cash, debt and equity investments, trade receivables and payables, debt, certain *provisions*, net cash-settled commodity contracts and derivatives (including embedded derivatives).

163 The accounting standards relating to financial instruments (FRS 25 'Financial instruments: disclosure and presentation', FRS 26: 'Financial instruments: measurement', the two amendments to FRS 26, and FRS 29 '(IFRS 7) Financial Instruments: disclosures') will apply as follows (see also Section 5 application of accounting standards). The presentational requirements of FRS 25 are applicable to all institutions. The requirements of FRS 26 will apply to institutions qualifying as listed entities (including those with listed debt in issue) or those institutions adopting *fair value* accounting. The disclosure requirements of FRS 25 and FRS 29 first apply on adoption of FRS 26. The requirements of these standards are complex, and reference should be made to them for individual issues.

164 For institutions which do not have listed debt (and are not applying fair value accounting in accordance with the Companies Act or FRS 26) the relevant parts of FRS 4 remain applicable. Institutions should also give due consideration to the requirements of FRS 25, FRS 26 and FRS 29 when accounting for previously off-balance sheet arrangements (such as that applied to student residence schemes).

165 Institutions should keep their categorisation of *assets* and *liabilities* under review to ensure that the accounting treatment and presentation is in line with these standards.

166 In summary, the standards referred to above will require institutions to consider the following:

(a) compound financial instruments comprising an equity and a liability element (such as convertible debt) should be split into those respective elements and accounted for separately ('split accounting');
(b) *liabilities* should be regarded (and classified) as falling due within one year even if the original term was for a period longer than a year, and/or an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the *financial statements* are authorised for issue [FRS 25, para 50];
(c) a financial asset and a *financial liability* should be offset when, and only when, an institution currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously (this should be considered particularly in relation to cash balances) (FRS 25, para 42);

(d) qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk. The qualitative disclosures describe management's objectives, policies and processes for managing those risks. The quantitative disclosures provide information about the extent to which the institution is exposed to risk, based on information provided internally to the institution's key management personnel. Together, these disclosures provide an overview of the institution's use of financial instruments and the exposures to risks they create;
(e) in certain circumstances, different elements of embedded derivatives should be separately accounted for;
(f) in order to apply hedge accounting, strict criteria, including the existence of formal documentation and the achievement of effectiveness tests, must be met (see paragraphs 71 to 102 of FRS 26).

Accounting for provisions, contingent liabilities and contingent assets

The use of a *provision* is restricted to a liability where there is some uncertainty as to the timing or amount that has been incurred. 167

Provisions should be recognised in the *financial statements* when: 168
(a) an institution has a present obligation (legal or constructive) as a result of a past event;
(b) it is probable that a transfer of economic benefits will be required to settle the obligation; and
(c) a reliable estimate can be made of the amount of the obligation.

Provisions for restructuring should only be recognised when the institution is demonstrably committed to that restructuring and when as a result of this commitment there is valid expectation that there will be a transfer of economic benefits. 169

The amount recognised as a *provision* should be the best estimate of the expenditure required to settle the obligation at the balance sheet date. The amount recognised as a *provision* should be discounted to present value where the time value of money is material. The discount rate used should reflect current market assessments of the time value of money and reflect any risks specific to the liability. The best estimate should be determined by the judgement of the institution's management and should take account of: 170

(a) past experience of similar transactions;
(b) opinions of independent experts (where appropriate);
(c) uncertainties caused by weighting all possible outcomes (i.e. 'expected value'); and
(d) appropriate *accounting policies* as outlined in FRS 18.

171 It should be noted that there are no grounds for recognising a *provision* for future repairs and maintenance in respect of freehold buildings. This is because these costs relate to the future operation of an institution, rather than to a past event. As such they should either be capitalised as *assets* or written off as operating expenses when incurred, as appropriate.

172 The existence of a contractual or legal obligation to pay for goods or services to be supplied at a future date does not necessarily justify a *provision*. It may require disclosure as a capital commitment or, if the contract is onerous, as a *contingent liability* or a *provision*.

173 An institution should make a *provision* for the present obligation that arises under a contract or lease that is onerous. The onerous aspect of the contract should be valued as the least net cost of exiting from the contract that is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

Contingent liability

174 A *contingent liability*, which is not recognised but is disclosed by way of a note, arises when the definition of a *provision* is not met and includes three scenarios:

(a) a possible rather than a present obligation;
(b) a possible rather than a probable outflow of economic benefits;
(c) an inability to measure the economic outflow.

Contingent asset

175 A contingent asset, which is not recognised but is disclosed by way of a note, is defined as a possible, rather than present, asset arising from a past event. Contingent *assets* should be assessed continually to ensure they are treated appropriately in the *financial statements*. If in any period it becomes virtually certain that an inflow of economic benefits will occur then the asset and its associated gain should be recognised in that accounting period. It is important that any disclosure avoids giving misleading indications of the likelihood of a gain arising.

Disclosure

176 For each class of *provision* the institution should follow the disclosure requirements in paragraphs 89 to 94 of FRS 12 'Provisions, Contingent Liabilities and Contingent Assets' setting out the carrying amount of the *provision*, *provisions* made in the period and providing appropriate description of the *provision*. In extremely rare cases disclosure of some or all of the information required by paragraphs 89 to 94 of FRS 12 might prejudice seriously the position of the institution in dispute with other parties on the *provision*. In such cases an institution need not disclose the information unless the disclosure is required by law; but should disclose the general nature of the dispute together with the fact that and the reason why the information has not been disclosed.

Accounting for retirement benefits

Institutions should fully adopt the requirements of FRS 17 'Retirement Benefits'. The requirements for the recognition and measurement of *retirement benefits* differ for defined benefit and *defined contribution schemes*. Full adoption requires the recognition of the various components of defined benefits and defined contribution scheme *assets* and *liabilities* within the *financial statements*. 177

Measurement of defined benefit schemes assets and liabilities

Assets in a *defined benefit scheme* should be measured at their *fair value* at the balance sheet date. *Defined benefit scheme liabilities* should be measured on an actuarial basis using the *projected unit method*. 178

The projected unit method considers promised benefits for pensioners and deferred pensioners and accrued benefits for members in service taking into account projected earnings. 179

The objective of the valuation is to make the best estimate of the future cash outflows that will arise in respect of the benefits earned by employees at the valuation date. This normally requires the expertise of an actuary. The ground rules regarding the assumptions underlying the valuation of accrued *liabilities* are: 180

(a) the assumptions should be mutually compatible and provide the 'best estimate' of the future cash outflows;
(b) the governing body, which is responsible for the assumptions used in preparing the financial statements, should take appropriate advice;
(c) the financial assumptions that are affected by economic conditions should reflect market expectations at the balance sheet date; and
(d) the assumptions should reflect expected future events that will affect the cost of the benefits to which the employer is committed at the balance sheet date.

Demographic and financial assumptions underlie an actuarial valuation of pension scheme *liabilities* and should take account of all existing legal and constructive obligations. Demographic assumptions include statistical matters such as: 181

(a) mortality rates (before and after retirement);
(b) age, sex and marital status of membership;
(c) rates of leaving employment before retirement;
(d) early retirements; and
(e) members' surviving spouses and dependants covered by the scheme.

182 The main financial assumptions relate to inflation, that is, general price inflation, salary inflation, inflation in pensions in payment and in deferred pensions. The valuation of scheme *assets* and *scheme liabilities* needs to be internally consistent. Therefore, each of the inflation assumptions should reflect the same level of general price inflation that is reflected in the discount rate at the balance sheet date.

183 The estimated accrued *liabilities* should be discounted to their present value at the current rate of return on a high quality corporate bond of a currency and term that matches the *scheme liabilities*. This should be taken to be an AA-rated bond.

Recognition of defined benefit scheme assets and liabilities in the balance sheet

184 The surplus/deficit in a *defined benefit scheme* is the excess/shortfall of the value of the *assets* in the scheme over/below the present value of the *scheme liabilities*. The institution should recognise an asset in the balance sheet to the extent that it is able to recover a surplus either through reduced contributions in the future or through refunds from the scheme. *Liabilities* should be recognised in the balance sheet to the extent that they reflect a legal or *constructive obligation*.

185 Institutions should analyse the change in the defined benefit asset or liability (other than arising from contributions to the scheme) into the following components:

Periodic Costs

(a) the current service cost;
(b) the interest cost;
(c) the expected return on assets; and
(d) actuarial gains and losses.

Non Periodic Costs

(e) past service costs; and
(f) gains and losses on settlements and curtailments.

Recognition of defined benefit schemes assets and liabilities in the income and expenditure account and statement of recognised gains and losses

186 This SORP requires that any amounts debited or credited to the income and expenditure account in relation to *defined benefit scheme*s should be separately identified in the notes to the *accounts*. The current service cost should be based on the most recent actuarial valuation at the beginning of the period, with the financial assumptions updated to reflect conditions at that date. It should be included within staff costs in the income and expenditure account. Any contributions from employees should be set off against the current service cost.

Past service costs should be recognised in the income and expenditure account on a straight-line basis over the period in which the increases in benefit vest. To the extent that the benefits vest immediately, the *past service cost* should be recognised immediately. *Past service costs* should be included within staff costs in the income and expenditure account. 187

The *interest cost* should be based on the discount rate and the present value of the *scheme liabilities* at the beginning of the period. The *interest cost* should, in addition, reflect changes in the *scheme liabilities* during the period. 188

The expected return on *assets* is based on long-term expectations at the beginning of the period and is expected to be reasonably stable. For quoted corporate or government bonds, the expected return should be calculated by applying the current redemption yield at the beginning of the period to the *market value* of the bonds held by the scheme at the beginning of the period. For other *assets* (for example, equities), the expected return should be calculated by applying the rate of return expected over the long term at the beginning of the period (given the value of the *assets* at that date) to the *fair value* of the *assets* held by the scheme at the beginning of the period. The expected return on *assets* should, in addition, reflect changes in the *assets* in the scheme during the period as a result of contributions paid into and benefits paid out of the scheme. The expected rate of return should be set by the management board or directors having taken advice from an actuary. 189

The net of the *interest cost* and the expected return on *assets* should be included as other finance costs (or income) in the income and expenditure account. 190

Losses on *settlements* and *curtailments* not allowed for in the actuarial assumptions should be measured at the date on which the employer becomes demonstrably committed to the transaction and recognised in the income and expenditure account covering that date as staff costs. Gains arising on a settlement or curtailment not allowed for in the actuarial assumptions should be measured at the date on which all parties whose consent is required are irrevocably committed to the transactions and recognised in the income and expenditure account as a deduction against staff costs covering that date. 191

Actuarial gains and losses arising from any new valuation and from updating the latest actuarial valuation to reflect conditions at the balance sheet date should be recognised in the statement of total recognised gains and losses for the period. 192

Presentation of defined benefit scheme assets and liabilities in the balance sheet

The total of any defined benefit pension assets and the total of any defined pension liabilities should be presented separately on the face of the balance sheet following other net assets and before capital and reserves. The net pension reserve arising as a result of the recognition of pension assets and liabilities should also be included on the face of the balance sheet unless the net pension reserve is immaterial on the grounds of context, nature and value. 193

Disclosure – requirements for defined benefit schemes

194 The disclosures for *defined benefit schemes* should set out the nature of the scheme and should follow the disclosure requirements set out in paragraphs 76 to 82 of FRS 17. The disclosure requirements in the standard are extensive, but overall require disclosure of information to enable users of the institution's *financial statements* to evaluate the nature of the institution's participation in *defined benefit schemes* and the financial effects of changes in those schemes. In summary the disclosures required include:

(a) the principal actuarial assumptions used at the balance sheet date including disclosure of mortality rates where it is considered to be a material assumption;
(b) a reconciliation of the opening and closing balances of the present value of scheme *liabilities* showing separately the effects during the period;
(c) a reconciliation of the opening and closing balances of the fair value of scheme assets showing separately the effects during the period;
(d) for each major category of scheme *assets*, the percentage or the amount that each major category constitutes of the fair value of the total scheme assets;
(e) the institution's best estimate of contributions expected to be paid to the scheme beginning after the balance sheet date;
(f) a narrative description of the basis used to determine the overall expected rate of return on *assets*; and
(g) the amount for the current and previous four periods of the present value of the *scheme liabilities*, the fair value of the scheme *assets* and the surplus or deficit in the scheme.

195 There is also a requirement to disclose an analysis of *scheme liabilities* into amounts arising from schemes that are wholly unfunded and amounts arising from schemes that are wholly or partly funded. Where there is an obligation to provide retirement healthcare benefits then the costs of these should be subjected to a sensitivity analysis and disclosed. Institutions may want to make reference to the ASB's Best Practice Reporting Statement on disclosures related to Retirement Benefit Schemes.

Measurement and recognition of defined contribution pension schemes

196 The cost of a defined contribution scheme is equal to the contributions payable to the scheme for the accounting period. The cost should be recognised within staff costs in the income and expenditure account.

Disclosure requirements for defined contribution schemes

Institutions operating *defined contribution schemes* are required to disclose in the notes to the *accounts*: 197

(a) the nature of the scheme (i.e. defined contribution);
(b) the cost for the period; and
(c) any outstanding or prepaid contributions at the balance sheet date.

Multi-employer schemes

Where institutions have *defined benefit schemes* which are part of a multi-employer scheme, institutions which are unable to identify their share of the underlying *assets* and *liabilities* on a consistent and reasonable basis should account for their participation on a defined contribution basis. In addition to the defined contribution disclosures required by paragraph 75 of FRS 17, the institution should disclose: 198

(a) the reason why sufficient information is not available to account for the scheme as a defined benefit scheme;
(b) the fact that the scheme is a defined benefit scheme but that the institution is unable to identify its share of the underlying assets and liabilities; and
(c) any available information about the existence of the surplus or deficit in the scheme and the implications of that surplus or deficit for the institution.

Institutions participate in a number of multi-employer schemes. Each institution should consider on a case by case basis with the scheme's administrators and the scheme's actuaries whether the *assets* and *liabilities* in the scheme can be separately identified. 199

Retirement benefit schemes operated by institutions

Universities Superannuation Scheme and Superannuation Arrangements of the University of London

These schemes are multi-employer *defined benefit schemes* which are externally funded and contracted out of the State Second Pension (S2P). The *assets* of these schemes are held in separate trustee-administered funds. These schemes have confirmed that it is not possible to identify each institution's share of the underlying *assets* and *liabilities* of the schemes and hence institutions are able to apply the exemption set out in paragraph 198 above and contributions to the schemes should be accounted for as if they were *defined contribution schemes*. 200

Teachers' Pension Scheme and National Health Service Pension Scheme

201 These schemes are multi-employer *defined benefit schemes*. These schemes require institutions to pay a contribution to central government reflecting benefits earned during the year. These contributions are not put aside into a separate fund, nor are additional contributions thereafter required by central government in relation to those benefits. The pensions are paid by central government. The government treats the pension scheme as an unfunded *defined benefit scheme*.

202 It is not possible for these schemes to identify separately each institution's share of the underlying *assets* and *liabilities* in the scheme on a consistent and reasonable basis. Therefore these schemes should be treated as though they were *defined contribution schemes*.

Local Government Pension Schemes

203 The Local Government Pension Scheme (LGPS) including the Local Government Pension Scheme in England and Wales and the Local Government Pension Scheme in Scotland, are multi-employer schemes where it is normally possible for individual employers as admitted bodies to identify their share of *assets* and *liabilities*. Therefore it is considered where institutions are admitted bodies to the LGPS (in England and Wales) and the LGPS in Scotland that these schemes should be accounted for as *defined benefit schemes* (provided that the assets and *liabilities* relating to member institutions can be measured on a reliable and consistent basis) and the exemption set out in paragraph 199 above for *defined benefit schemes* is unlikely to apply.

Pooled valuations LGPS

204 As noted above, the vast majority of LGPS schemes should be accounted for as *defined benefit schemes*. However, some LGPS administrators have indicated that they can only provide institutions with a "pooled valuation" (*assets* and *liabilities* are only identified on an aggregate basis for a *group* of institutions and/or other admitted bodies that then share a common contribution rate). If, in this exceptional circumstance, the institution has confirmed that it is not possible for the scheme's actuary to identify the institution's share of the underlying *assets* and *liabilities* on a consistent and reasonable basis then institutions may be able to apply the multi-employer exemption set out in paragraph 198.

Early Retirement Costs

205 FRS 17 notes that '*Retirement benefits* do not include termination benefits payable as a result of either (i) an employer's decision to terminate an employee's employment before the normal retirement date or (ii) an employee's decision to accept voluntary redundancy in exchange for those benefits, because these are not given in exchange for services rendered by employees.' Therefore payments made to employees as a result of early retirement, arising from these circumstances, would need to be recognised, measured and provided for in full and in accordance with FRS 12.

Consolidated accounts – accounting for subsidiaries, joint venture entities and associates, and collaborations

Where an institution has collaborations, *associates* or *subsidiary undertakings*, the *financial statements* should be prepared on a consolidated basis in accordance with FRS 2 (revised) 'Subsidiary Undertakings' and/or FRS 9 'Associates and Joint Ventures' and where relevant, the Companies Act. *Consolidated financial statements* should present a true and fair view of the surplus or deficit and cash flows of the *group* and the *assets*, *liabilities* and reserves of the institution and the *group*. 206

The notes to be disclosed in the institution's *accounts* should also be disclosed in the *group accounts* unless there are no additional amounts or details in relation to subsidiaries, *associates* or *joint venture entities*. The disclosures relating to FRS 2 and 9 should follow the requirements of those standards. 207

An institution should also consider whether or not an entity, or body, in which it has an interest is a *quasi-subsidiary* as defined by FRS 5 'Reporting the Substance of Transactions'. 208

Where the objects of another entity are substantially or exclusively confined to the benefit of the institution, the issue of *control* requires particular consideration. In such cases formal powers of *control* may not exist but *dominant influence* may arise less formally. For example, the benefiting institution may set out in outline the nature or timing of the support it wants to achieve. Alternatively the benefiting institution may intervene on a critical matter. Where evidence exists of such *dominant influence* being exercised the criteria for *consolidation* should be regarded as being met. 209

Each institution will need to clarify its relationship with its students' union to determine whether *consolidation* is required in the light of all relevant legislation and accounting standards. In particular, the institution should consider whether it has the power to exercise, or actually exercises, a *dominant influence* or *control* over the students' union, or whether it and the students' union are managed on a unified basis. 210

Subsidiaries

Subsidiary undertakings may be excluded from *consolidation* where inclusion of all *subsidiary undertakings*, taken together, is not material. 211

212 FRS 2 (revised) requires that a *subsidiary undertaking* should be or is permitted to be excluded if:

(a) inclusion is not material for the purposes of giving a true and fair view;
(b) the institution's rights over the *assets*, or the management of the *subsidiary undertaking*, are severely restricted; or
(c) subsequent resale of the *subsidiary undertaking* was intended at the time of *acquisition* and the *subsidiary undertaking* has not previously been included in the *consolidated financial statements*.

213 Where *subsidiary undertakings* are excluded, paragraphs 27 to 29 of FRS 2 (revised) set out the differing treatments to be adopted for each category of *subsidiary undertaking* to be excluded from the *consolidation*.

214 Where an *associate* or *subsidiary undertaking* is excluded from *consolidation,* provided that this exclusion complies with FRS 2 (revised), the notes to the *accounts* must disclose (in accordance with the requirements of FRS 2 (revised) and, where an institution is incorporated as such, the Companies Act):

(a) the name of the associate or *subsidiary undertaking* excluded;
(b) any qualification contained in the auditors' report on the associate or *subsidiary undertaking's financial statements* for the relevant financial year;
(c) the aggregate amount of the *associate's* or *subsidiary undertaking's* capital and reserves at the end of its relevant financial year and its profit or loss for the period, unless the *associate* or *subsidiary undertaking* is included in the *consolidated financial statements* using the *equity* method;
(d) the reasons why the *associate* or *subsidiary undertaking* is not dealt with in the *consolidated financial statements*, the reason disclosed should be in accordance with the Companies Act and the reasons set out in paragraph 212 above;
(e) details of balances and transactions between the excluded associate or *subsidiary undertaking(s)* and the rest of the *group*;
(f) the nature and the extent of transactions of the excluded subsidiary undertakings with the rest of the *group*;
(g) for an excluded *subsidiary undertaking* carried other than by the *equity* method, any amounts included in the *consolidated financial statements* in respect of:
    i. dividends received and receivable from that undertaking; and
    ii. any write-down in the period in respect of the investment in that undertaking or amounts due from that undertaking;
(h) any guarantees or indemnities given by the *group* or a member of it in respect of the associate or *subsidiary undertaking*.

Joint venture entities and associates

The institution's share of income and expenditure in a *joint venture entity* should be recognised in the institution's income and expenditure account in accordance with paragraph 21 (first indent) of FRS 9 whilst that of an *associate* should be recognised in the institution's income and expenditure account in accordance with paragraph 27 of FRS 9. Similarly the institution's share of *assets* and *liabilities* in a *joint venture entity* should be recognised in accordance with paragraph 21 (second indent) of FRS 9 whilst that of an *associate* should be recognised in accordance with paragraph 29 of FRS 9. FRS 9 requires the *equity method* to be used when consolidating *associates*. *Joint venture entities* should be accounted for using the *gross equity method*. For *joint venture entities* (and NOT for *associates*) paragraph 23 of the FRS 9 provides the "fuller information" option (based on the *gross equity method*) in terms of columnar presentation. This SORP recommends that, where appropriate, a columnar format should be used to disclose these transactions in the primary statements, based on that shown as 'example 2' in FRS 9. This would show as separate columns for the income and expenditure account and balance sheet: 215

(a) transactions relating to the institution or group;
(b) interests in joint venture entities; and
(c) total

Other joint arrangements

Such *associates* and *joint venture entities* might include spin-off companies, *charitable trusts*, and other entities established for joint work with other institutions and entities. Joint arrangements that are not entities are no more than collaborative exercises (for example, joint research or training projects). However, where material, these collaborative exercises should be disclosed in the notes to the accounts. Participants in joint arrangements should account for their own *assets*, *liabilities* and cash flows in accordance with the terms of the agreement. 216

Accounting periods and dates for subsidiaries, joint venture entities and associates

The *financial statements* of all *subsidiary undertakings* to be used in preparing the *consolidated financial statements* should, wherever practicable, be prepared to the same financial year-end and for the same accounting period as the parent institution. 217

Where an *associate*, *joint venture* entity or *subsidiary undertaking*'s financial year does not coincide with that of the institution, interim *financial statements* should be prepared to the same date as the parent institution. Where it is not practicable to use such interim *financial statements*, the *financial statements* of the *associate*, *joint venture* entity or *subsidiary undertaking* should be used providing that the year end is not more than three months before the relevant year end of the parent undertaking of the *group*. In such cases, material changes in the intervening period should be taken into account by adjustments in the preparation of the *consolidated financial statements*. 218

219 The *financial statements* must disclose for each *associate*, *joint venture* entity or *subsidiary undertaking* which is included in the *consolidated financial statements* on the basis of information prepared to a different date, or for a different accounting period from that of the parent undertaking:

(a) the name of the *joint venture* entity, *associate* or *subsidiary undertaking*;
(b) the accounting date or period of the *associate* or *subsidiary undertaking*;
(c) the reason for using a different accounting date;
(d) the accounting period, if it is of a different length from that of the institution.

Accounting policies for subsidiaries, joint venture entities and associates

220 Subject to paragraph 41 of FRS 2 (revised), uniform *group accounting policies* should be used for determining the amounts to be included in the *consolidated financial statements*, if necessary by adjusting for *consolidation* the amounts which have been reported by *subsidiary undertakings* in their individual *financial statements*. *Accounting policies* likely to require consideration by the reporting institution would be those relating to the revaluation of *tangible fixed assets* an institution may adopt in accordance with paragraphs 76 to 83, the treatment of *deferred capital grants* and the format of the performance statement which should follow the format required by the institution for the income and expenditure account set out in Appendix 2. It should be noted that this is not an exhaustive list.

Intra Group Transactions

221 To the extent that they are reflected in the book value of *assets* to be included in the *consolidation*, gains or losses on any intra-*group* transactions should be eliminated in full. Amounts in relation to debts and claims between undertakings included in the *consolidation* should also be eliminated. The elimination of gains or losses relating to intra-*group* transactions should be set against the interests held by the *group* and the minority interest in respective proportion to their holdings in the undertaking whose individual *financial statements* recorded the eliminated gains or losses.

222 As *associates* and *joint venture entities* are not part of the *group*, balances between the reporting institution and its *associates* or *joint ventures* are not eliminated and therefore unsettled normal trading transactions should be included as current *assets* or *liabilities*. However, FRS 9 requires that where gains or losses are included in the carrying amount of assets of either entity, the part relating to the reporting institution's share should be eliminated.

Accounting for business combinations

Institutions must assess, in accordance with FRS 6 whether a combination of an institution with another institution is an *acquisition* or *merger*. Merger accounting should only be used where combinations are not, in substance, the *acquisition* of an entity (or another institution) by an institution but the formation of a new reporting institution as a substantially equal partnership where no party is dominant. 223

To this end FRS 6, 'Acquisitions and Mergers' sets out five criteria (see FRS 6 paragraphs 6 to 12), that must be met for *merger* accounting to be used. Of these five criteria the first three are relevant to institutions. Criteria 4 and 5 are not considered applicable to institutions because they do not have equity shareholders. When the relevant criteria are met, *merger* accounting should be used. If all the remaining relevant criteria are not met the combination should be regarded as an *acquisition* of an entity (or institution) and *acquisition* accounting should be used. 224

Institutions should consider the substance of the transactions and not solely the legal form when considering whether or not a combination meets the criteria set out in FRS 6. 225

Institutions should follow the disclosure requirements set out in paragraphs 21 and 23 to 37 of FRS 6 for any combination it enters into. 226

With *merger* accounting the carrying values of the *assets* and *liabilities* acquired are not required to be adjusted to *fair value*, although appropriate adjustments should be made to achieve uniformity of *accounting policies*. The results and cash flows of the combining institution should be brought into the *financial statements* of the combined institution from the beginning of the period in which the combination occurred. The comparative figures should be adjusted to include the results for all the combining institutions or other entities for the previous period and their balance sheets for the previous balance sheet date. 227

Combinations not accounted for as *merger* accounting should be accounted for by *acquisition* accounting. On *acquisition* the identifiable *assets* and *liabilities* of the institutions or entities acquired should be measured at *fair value* that reflect the conditions on *acquisition* and should be included in the acquiring institution's consolidated balance sheet. The results and cash flows of the acquired institution or entity should be brought into the *financial statements* only from the *date of acquisition*. The figures for the previous period for the acquiring institution should not be adjusted. Institutions should follow the requirements of FRS 7 '*Fair value*s in Acquisition Accounting' (paragraphs 9 to 22) when determining *fair value* of the *assets* and *liabilities*. 228

Goodwill on *acquisition* must be accounted for in line with the requirements of this SORP as set out in paragraphs 117 to 125 above. 229

Related party transactions

230 Institutions should disclose material transactions undertaken by the reporting entity with a related party. Related parties are defined in accordance with FRS 8 'Related Party Disclosures'. For further commentary on where *related party transactions* might occur see paragraph 232 below. Disclosure should be made irrespective of whether a price is charged, in accordance with the requirements of FRS 8 (paragraph 6) and should include:

(a) the names of the transacting related parties;
(b) a description of the relationship between the parties;
(c) a description of the transactions;
(d) the amounts involved;
(e) any other elements of the transactions necessary for an understanding of the *financial statements*;
(f) the amounts due to or from related parties at the balance sheet date and the *provisions* for doubtful debts due from such parties at that date; and
(g) amounts written off in the period in respect of debts due to or from related parties.

231 FRS 8 requires that transactions material to either party be disclosed and provides a definition of *materiality*. Although the standard excludes disclosure of transactions with government departments and their sponsored bodies, the SORP requires disclosure of funding body grants on the face of the income and expenditure account, the balance sheet (for *deferred capital grants*), and in the relevant notes to the *accounts*. Transactions between *group* entities that are eliminated on *consolidation* do not require disclosure in either the *group* or parent's *financial statements*.

232 Related parties, for institutions, are most likely to be found amongst:

(a) those members of the governing body (and their 'close family') who hold influential posts in local (or any) public bodies (including for example local authorities, non departmental public bodies etc) and private sector organisations with which the institution has transactions;
(b) senior staff, including those who hold influential posts on other bodies with which the institution has transactions, e.g. an NHS healthcare trust;
(c) associates, collaborations and joint venture entities – particular attention should be paid to transactions with associate and joint venture entities, as these will not be fully eliminated on consolidation.

233 Institutions should also give due consideration as to whether or not bodies such as students' unions and separate development trusts are related parties in the context of FRS 8.

Events after the balance sheet date

Institutions are required to account for events, favourable and unfavourable which occur between the balance sheet date and the date when the *financial statements* are authorised for issue. An institution should not prepare its *financial statements* on a going concern basis if events after the balance sheet date indicate that the going concern assumption is not appropriate. Two types of events can be identified: 234

(a) those that provide evidence of conditions that existed at the balance sheet date (adjusting events after the balance sheet date). An example of an adjusting event would be the receipt of information after the balance sheet date indicating that an asset was impaired at the balance sheet date; and
(b) those that are indicative of conditions that arose after the balance sheet date (non-adjusting events after the balance sheet date). An example of a non-adjusting event would be a decline in market value of investments between the balance sheet date and the date when the financial statements are authorised for issue.

The determination after the balance sheet date of the amount of a gift aid payment to an institution by a *subsidiary undertaking* is an adjusting event, if the subsidiary had a present, legal or a *constructive obligation* at the balance sheet date. Where a present obligation is demonstrable at the year end, an adjustment is made where calculations made after the balance sheet date provide greater accuracy in the measurement of the existing liability. 235

5. Application of accounting standards

236 This section is provided to assist institutions in determining the relevance of SSAPs and FRSs, but because new standards are issued regularly, it is important to refer to the latest information provided by the Accounting Standards Board, including *UITF Abstracts*, which have the same force as SSAPs and FRSs. The summaries below should not be relied upon as a substitute for reading the full text of the standard. Reference should be made to the Accounting Standards Board's website at www.asb.org.uk.

237 237 Institutions must follow all applicable SSAPs and FRSs and guidance from the Accounting Standards Board. The following list is a guide to the standards most likely to be relevant.

Statements of Standard Accounting Practice

SSAPS withdrawn

238 SSAPs 1, 2, 3, 6, 7, 8, 10, 11, 12, 14, 15, 16, 17, 18, 22, 23 and 24 have been withdrawn.

SSAP 4: Accounting for government grants

239 This SSAP is relevant to all institutions. This SSAP sets out the accounting treatment and disclosure of government grants and other forms of government assistance.

SSAP 5: Accounting for Value Added Tax

240 This SSAP is relevant to all institutions. This standard sets out the accounting treatment for Value Added Tax.

SSAP 9: Stocks and long term contracts

241 This SSAP is relevant to all institutions. The standard deals with the valuation of stocks, which are normally to be stated at cost or net realisable value whichever is lower. Other parts of the SSAP deal with valuation rules for long-term contracts.

SSAP 13: Accounting for research and development

242 This SSAP is relevant to all institutions which undertake research. It provides guidance on three broad categories of activity: pure research, applied research and development. The standard defines these categories and specifies the accounting policies that may be followed for each. The SSAP is specific (and refers to the Companies Act) that pure and applied research may not be treated as an asset. It sets out criteria under which the research and development costs of products for commercial exploitation might be capitalised. (See also FRS 10).

SSAP 19: Accounting for investment properties

This SSAP is relevant to those institutions which have investment properties. It requires that assets held as investment properties should be included in the balance sheet at market value. 243

SSAP 20: Foreign Currency Translation

This SSAP is relevant to all institutions which undertake foreign currency translation. Exchange gains and losses should be taken to the income and expenditure account. Institutions should also consider the requirements of FRS 23 'The Effects of Changes in Foreign Exchange Rates' and FRS 24 'Financial Reporting in Hyperinflationary Economies', although these standards will only apply where FRS 26 'Financial Instruments: Measurement' has been applied. 244

SSAP 21: Accounting for Leases and Hire Purchase Contracts

This SSAP is relevant to all institutions which have leases. The standard requires lessees to capitalise finance leases. Where contracts are treated as operating leases, paragraph 37 of this SSAP needs to be considered in terms of the proper allocation to accounting periods over the period of the lease. 245

SSAP 25: Segmental Reporting

This SSAP is relevant to all institutions. The standard contains provisions relating to segmental disclosure requirements. Paragraph 65 in this SORP notes that institutions normally operate a single segment of activity i.e. teaching and research. 246

Financial Reporting Standards

FRS 1: Cash Flow Statements

This FRS is relevant to all institutions. FRS 1 (revised 1996) requires institutions to prepare a cash flow statement in the manner set out in the FRS. The cash flow statement should include all inflows and outflows of cash. 247

FRS 2: (revised) Accounting for Subsidiary Undertakings

This FRS is relevant to those institutions which have *subsidiary undertakings.* FRS 2 sets out the conditions under which an entity qualifies as a parent undertaking which should prepare *consolidated financial statements* for its *Group*, the parent and its subsidiaries. It also sets out the manner in which *consolidated financial statements* are to be prepared. A large part of FRS 2 is directly based on the Companies Act, as amended, and the requirements of the standard are consistent with the Act (parallel legislation exists in Northern Ireland). 248

FRS 3: Reporting Financial Performance

249 This FRS is relevant to all institutions. Its objective is to require institutions to highlight a range of important components of financial performance to aid users in understanding the performance achieved by an institution in a period and to assist them in forming a basis for their assessment of future results and cash flow. FRS 3 requires a layered format for the income and expenditure account split between continuing, newly acquired and discontinued operations. It effectively prohibits extraordinary items and requires exceptional items to be disclosed on a separate line within the activity to which they relate. FRS 3 requires exceptional profits or losses on the sale or termination of an operation, exceptional costs of a fundamental reorganisation or restructuring and exceptional profits or losses on the disposal of fixed assets to be disclosed on the face of the income and expenditure account.

250 The standard also requires a statement of total recognised gains and losses to be included in the *accounts*. The statement reports inter alia gains and losses arising on revaluations and discloses the effect of prior year adjustments. A note of historical surpluses is also required. The purpose of this note is to present the surpluses or deficits of institutions that have revalued assets on a more comparable basis with those that have not.

FRS 4: Capital Instruments

251 This FRS is relevant to all institutions. For example, it applies to institutions using low start financing arrangements and particularly concerns the requirement to allocate the finance costs at a constant rate over the term of the borrowing. The objective of FRS 4 is to ensure that *financial statements* provide a clear, coherent and consistent treatment of capital instruments. The standard requires capital instruments to be presented in *financial statements* in a way that reflects the obligations of the issuer. The standard also prescribes the methods to be used to determine the amounts to be ascribed to capital instruments and their associated costs and specific relevant disclosures. Those provisions of FRS 4 not deleted by FRS 25 and which may be relevant to institutions are those sections on the carrying cost of debt and allocation of finance costs, and repurchase of debt (paragraphs 27-32 of FRS 4), identification of distinct capital instruments (paragraphs 68 and 69 of FRS 4), the term of debt and finance costs (paragraphs 73-76 of FRS 4) and issue costs (paragraphs 92, 94-97 of FRS 4).

FRS 5: Reporting the Substance of Transactions

252 This FRS is relevant to all institutions. FRS 5 requires the economic substance and any resulting *assets,* liabilities, gains or losses of an entity's transactions, rather than just the transaction's legal form, to be reported in its *financial statements*.

Where there is a series of connected transactions the economic substance of the whole series should be determined and accounted for rather than accounting for each individual transaction. In transactions that involve the granting or acquiring of options regard should be given to the likely outcome, the motives of all the parties involved and possible scenarios contemplated at the time the deal was struck when deciding the correct accounting treatment. 253

As well as the recognition of assets and *liabilities*, FRS 5 also addresses the de-recognition of assets that can arise through the transfer of benefits and risks. It provides for complete and partial de-recognition as well as 'netting off' of *assets* and *liabilities* under certain, very restrictive circumstances through 'linked presentation'. As part of the issue of recognition the standard defines the 'quasi-subsidiary', once again through the principle of economic substance, and requires that it should be consolidated in the institution's *consolidated financial statements*. 254

Detailed guidance on accounting for certain 'off-balance sheet' financing arrangements is provided by the standard through a series of application notes. Of particular interest to institutions may be: 255

'B - Sale and repurchase agreements';
'D – Securitised Assets'; and
'F – Private Finance Initiatives and similar contracts'.

Application Note G on 'Revenue Recognition' is also of interest to institutions (see paragraphs 42 and 66 to 68). It concerns basic principles regarding the recognition and measurement of revenue. The application note formalises present best practice in the recognition of revenue rather than setting out specific new requirements and brings principles to the practice of revenue recognition in order to improve consistency of accounting treatment. The application note requires that revenue should be recognised only when a 'right to consideration exists' and explains that such a right will exist only to the extent that performance of contractual obligation has taken place. 256

FRS 6: Acquisitions and Mergers

This FRS is relevant to institutions which have business combinations. It sets out the circumstances in which the two methods of accounting for a business combination (acquisition accounting and merger accounting) are to be used. A business combination is the bringing together of separate entities into one economic entity as a result of one entity uniting with another or obtaining control over another entity's net assets and operations. 257

FRS 7: Fair values in Acquisition accounting

258 This FRS is relevant to those institutions which have business combinations. It sets out the principles of accounting for a business combination under the acquisition method of accounting. It sets out how the fair values of identifiable *assets* and *liabilities* should be determined and what 'identifiable *assets* and *liabilities*' means.

259 The objective of the FRS is to ensure that, when a business entity is acquired by another, all the assets and *liabilities* of the acquired entity at the date of *acquisition* are recorded at fair values reflecting their condition.

260 All changes to the acquired *assets* and *liabilities*, and the resulting gains and losses that arise after *control* of the acquired entity has passed to the acquirer are reported as part of the post *acquisition* financial performance of the group.

FRS 8: Related Party Disclosures

261 This FRS is relevant to all institutions. The objective of FRS 8 is to ensure the disclosure of the existence of related parties and the extent and nature of transactions with them. The standard seeks disclosure not regulation of these transactions.

FRS 9: Associates and Joint Ventures

262 This FRS is relevant to those institutions with *associates* and *joint ventures*. The FRS sets out the definitions and accounting treatments for *associates* and *joint ventures*, and two types of interests that a reporting institution may have in other institutions or entities.

FRS 10: Goodwill and Intangible Assets

263 This FRS may be relevant to some institutions. The standard sets out the principles of accounting for goodwill and intangible *assets*. Its objective is to ensure that purchased goodwill and intangible *assets* are charged to the income and expenditure account in the periods in which they are depleted. Internally generated and internally developed goodwill should not be capitalised.

FRS 11: Impairment of Fixed Assets and Goodwill

264 This FRS is relevant to all institutions. The standard sets out the principles and methodology for accounting for impairments of fixed assets and goodwill.

FRS 12: Provisions, Contingent Liabilities and Contingent Assets

This FRS is relevant to all institutions. Its aim is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent *liabilities* and contingent *assets* and that sufficient information is disclosed in the notes to the *financial statements* to enable users to understand their nature, timing and amount. 265

FRS 13: Derivatives and other financial instruments

This FRS is likely to be relevant to a minority of institutions since it applies only to those which issue listed or publicly traded financial instruments. Where relevant, the FRS has been superseded by the disclosure requirements of FRS 29. 266

FRS 15: Tangible Fixed Assets

This FRS is relevant to all institutions. The objectives of FRS 15 are to ensure that: 267

(a) consistent principles are applied to the initial measurement of *tangible fixed assets*;
(b) where an entity chooses to revalue particular classes of *tangible fixed assets* the valuation is performed on a consistent basis for each class and kept up-to-date and gains and losses on revaluation are recognised on a consistent basis;
(c) depreciation of *tangible fixed assets* is calculated in a consistent manner and recognised as the economic benefits are consumed over the assets' useful economic lives;
(d) sufficient information is disclosed in the financial statements to enable users to understand the impact of the institution's accounting policies regarding initial measurement, valuation and *depreciation* of *tangible fixed assets* on the financial position and performance of the institution.

The scope of the FRS applies to all *tangible fixed assets*, with the exception of investment properties as defined in SSAP 19 'Accounting for investment properties'. 268

FRS 16: Current Tax

This FRS is relevant to institutions which pay corporation tax. Where there is a significant element of non-charitable activity, corporation tax may become payable, although in most cases institutions will take action to ensure that the tax charge is offset and therefore not payable. Therefore accounting for current taxation under the standard is unlikely to be widely applicable. Where current taxation is payable, institutions should apply the standard in full. 269

270 The standard defines current tax as "the amount of tax estimated to be payable or recoverable in respect of the taxable profit or loss for a period, along with adjustments to estimates in respect of previous accounting periods". In accounting for current tax, the standard requires that current tax be recognised in the income and expenditure account for the period, except to the extent that it is attributable to a gain or loss that is or has been recognised in the statement of total recognised gains and losses, in which case the tax should be recognised there. The standard also deals with tax on dividends by stating that dividends (incoming and outgoing) should be recognised at an amount that includes any withholding tax, but excludes any other taxes, such as attributable tax credits, not payable wholly on behalf of the recipient.

FRS 17: Retirement Benefits (as amended in December 2006)

271 This standard applies in full to all institutions. This standard sets out the accounting requirements for retirement benefits. The standard sets out the different accounting arrangements for defined benefit and defined contribution schemes.

272 The nature of pension arrangements varies between institutions and between different categories of staff within institutions. The following types of scheme are the most prevalent across the sector: notionally funded national schemes; funded national schemes where assets and *liabilities* cannot be ascribed to particular employer institutions; local government funded schemes; individual employer specific schemes.

FRS 18: Accounting Policies

273 This FRS is relevant to all institutions and should be applied in full. Institutions need to take particular notice of the standard's requirements, as set out in paragraph 58 of the FRS, regarding *financial statements* that fall within the scope of the SORP. This SORP recommends particular accounting treatments with the aim of narrowing areas of difference between institutions and promoting comparability between financial statements. The comparability is further enhanced if users are made aware of the extent of the institution's compliance with the SORP. Therefore FRS 18 requires that an institution's *financial statements* should state whether they have been prepared in accordance with the provisions of the SORP. In the event of departure, the effect of and reasons for such departure should be disclosed.

FRS 19: Deferred Tax

274 This FRS is unlikely to be widely applicable to institutions, except where they operate subsidiary companies which have not taken steps to offset their tax liability. In those circumstances, the standard should be applied in full. See also paragraphs 67 to 69 in this SORP.

FRS 20: Share-based Payment

275 This FRS is unlikely to be applicable to institutions.

FRS 21: (IAS 10) Events after the balance sheet date

This FRS is relevant to all institutions and should be applied in full. The objective of this standard is to prescribe: 276

(a) when an entity should adjust its financial statements for events after the balance sheet date; and
(b) the disclosures that an entity should give about the date when the financial statements were authorised for issue and about events after the balance sheet date.

Further details are provided in paragraphs 234 to 235 of this SORP, which provide guidance in particular on accounting for gift aid transactions. 277

FRS 22: (IAS 33) Earnings per share

This FRS is not applicable to institutions. This standard only applies to entities whose ordinary shares are traded or in the process of issuing such shares. 278

FRS 23: (IAS 21) The effects of changes in foreign exchange rates

This standard is applicable to those institutions applying FRS 26. On application of this standard SSAP 20 is withdrawn. 279

An entity may carry on foreign activities in two ways. It may have transactions in foreign currencies or it may have foreign operations. In addition, an entity may present its *financial statements* in a foreign currency. This standard prescribes how entities should include foreign currency transactions and foreign operations in their *financial statements* and how they should translate *financial statements* into a presentation currency. 280

FRS 24: (IAS 29) Financial reporting in hyperinflationary economies

This standard is applicable to those institutions applying FRS 26. However, it is unlikely to have a wide application to institutions. 281

FRS 24 sets out how an entity whose functional currency is the currency of a hyperinflationary economy should report its operating results and financial position. It also provides guidance on determining whether an economy is a hyperinflationary economy. 282

FRS 25: (IAS 32) Financial Instruments: Disclosure and presentation

This standard is applicable to institutions. The presentation requirements of this standard deal with the classification of capital instruments issued between debt and equity and the implications of that classification for dividends and interest expense. 283

284 The disclosure requirements of the standard apply to institutions applying FRS 26 only.

285 Further details are provided in the main body of this SORP at paragraphs 162 to 166.

FRS 26: (IAS 39) Financial Instruments: Measurement

286 This standard applies to any institution which qualifies as a listed entity (including institutions with listed debt) from accounting periods beginning on or after 1 January 2005 or to institutions that apply the fair accounting rules from 1 January 2006.
The standard introduces the requirements for the measurement of financial instruments.

FRS 27: Life Assurance

287 This standard is unlikely to be applicable to institutions.

FRS 28: Corresponding Amounts

288 This standard is applicable to all institutions. The standard requires corresponding amounts to be shown for items in the primary *financial statements* and notes to the *financial statements*. Where corresponding amounts are not directly comparable with the amount to be shown in respect of the current financial year, they shall be adjusted and the basis for adjustment disclosed in a note to the *financial statements*.

289 The FRS permits a reporting entity not to show corresponding amounts for certain items in the notes to the *financial statements* that were previously exempted under company law. It also does not require corresponding amounts for the earliest period presented where *financial statements* for two or more consecutive periods are presented together.

FRS 29: (IFRS 7) Financial Instruments: Disclosures

290 This standard is only applicable to institutions applying FRS 26. This FRS embodies IFRS 7 'Financial Instruments: Disclosures' and includes amendments to that standard for entities subject to UK accounting standards.

Urgent Issues Task Force Abstracts

291 UITF Abstracts 1, 2, 3, 6, 7, 8, 10 12, 13, 14, 16, 17 18, 20 30, 33 and 37 have been, or are in the process of being, superseded by FRSs, or have been withdrawn.

UITF Abstract 4: Presentation of long-term debtors in current Assets

Is relevant to institutions. In most cases it will be satisfactory to disclose the size of debtors due after more than one year in the notes to the *accounts*. Although normally unlikely to apply to institutions, there may be some instances where the amount is so material in the context of net current *assets* that in the absence of disclosure of debtors due after more than one year on the face of the balance sheet readers may misinterpret the *financial statements*. In such circumstances the amount should be disclosed on the face of the balance sheet within current *assets*. 292

UITF Abstract 5: Transfers from current assets to fixed assets

Is relevant to institutions. Where *assets* are transferred from current to fixed, the current asset accounting rules should be applied up to the effective date of transfer, which is the date of management's change of intent. Consequently the transfer should be made at the lower of cost and *net realisable value*, and accordingly an assessment should be made of the *net realisable value* at the date of transfer and if this is less than its previous carrying value the diminution should be charged in the income and expenditure account to reflect the loss to the institution while the asset was held as a current asset. Whether *assets* are transferred at cost or at *net realisable value*, fixed asset accounting rules will apply to the *assets* subsequent to the date of transfer, including the disclosure requirements relating to valuations (where appropriate). 293

UITF Abstract 9: Accounting for operating in hyperinflationary economies

Is unlikely to be applicable to institutions. 294

UITF Abstract 11: Capital instruments: issuer call options

Is unlikely to be applicable to institutions. 295

UITF Abstract 15 (revised 1999): Disclosure of substantial acquisitions

Is applicable to institutions requiring the disclosures in respect of substantial acquisitions where any of certain ratios exceeds 15 per cent. 296

UITF Abstract 19: Tax on gains and losses on foreign currency borrowings that hedge an investment in a foreign enterprise

Is unlikely to be applicable to institutions. 297

UITF Abstract 21: Accounting issues arising from the proposed introduction of the euro

298 Is unlikely to be applicable to institutions.

UITF Abstract 22: The acquisition of a Lloyd's business

299 Is unlikely to be applicable to institutions.

UITF Abstract 23: Application of the transitional rules in FRS 15

300 Is likely to be applicable to institutions. However, this UITF Abstract is no longer relevant as the transitional rules should have been complied with in their *financial statements* relating to accounting periods ending on or after 23 March 2000 (the effective date of FRS 15). The abstract provides transitional rules on the use of prior period adjustments where *tangible fixed assets*, which were previously treated as a single asset, are identified as having two or more major components with substantially different useful economic lives.

UITF Abstract 24: Accounting for start-up costs

301 Is applicable to institutions. Start-up costs should be accounted for on a basis consistent with the accounting treatment of similar costs incurred as part of the institution's ongoing activities. If there are no such similar costs, start-up costs that do not meet the criteria for recognition as Assets under a relevant accounting standard, such as FRS 15 'Tangible Fixed *Assets*', should be recognised as an expense when they are incurred: they should not be carried forward as an asset. Where start-up costs meet the definition of exceptional items in FRS 3 'Reporting Financial Performance', they should be disclosed in accordance with that standard.

UITF Abstract 25: National Insurance contributions on share option gains

302 Is unlikely to be applicable to institutions.

UITF Abstract 26: Barter transactions for advertising

303 Is unlikely to be applicable to institutions. However, in the unusual event that an institution engages in a barter transaction for advertising, turnover and costs should only be recognised if there is persuasive evidence of the value at which, if the advertising had not been exchanged, it would have been sold for cash in a similar transaction.

UITF Abstract 27: Revisions to estimates of the useful economic life of goodwill and intangible assets

Is applicable to institutions. Where estimates of the useful economic lives of goodwill or *intangible assets* are revised, the carrying value should be amortised over the remaining useful economic life as required by paragraph 33 of FRS 10 regardless of whether the institution has in a previous period rebutted the presumption of a 20-year life. 304

UITF Abstract 28: Operating lease incentives

Is applicable to institutions. All incentives for the agreement of a new or renewed operating lease should be recognised as an integral part of the net payment agreed for the use of the leased asset, irrespective of the incentive's nature or form or the timing of the payments, in the accounting period in which the agreement is reached. 305

UITF Abstract 29: Website development costs

Is applicable to institutions. All planning, maintenance and operating costs should be charged to the income and expenditure account as incurred. Although the abstract allows design and content costs to be capitalised institutions will only pass the test that the primary purpose of the website is to provide a means of delivery of the teaching and research services offered by the institution in fulfilment of its principal objectives where the website is used to support specific courses or research projects. 306

UITF Abstract 31: Exchanges of businesses or other non-monetary assets for an interest in a subsidiary, joint venture or associate

Is applicable to institutions. 307

UITF Abstract 32: Employee benefit trusts and other intermediate payment arrangements

308

Is applicable to institutions.

UITF Abstract 34: Pre-contract costs

Is applicable to institutions. 309

UITF Abstract 35: Death-in-service and incapacity benefits

310 Is applicable to institutions. This Abstract clarifies the accounting required by FRS 17 'Retirement Benefits' for the cost of death-in-service and incapacity benefits, here such benefits are provided through a defined benefit pension scheme. The Abstract requires that, where the benefits are not wholly insured, the uninsured scheme liability and the cost for the accounting period should be measured, in line with other *retirement benefits*, using the *projected unit method*. The effect is that the valuation of uninsured benefits reflects the current period's portion of the full benefits ultimately payable in respect of current members of the scheme; the cost of insured benefits is determined by the relevant insurance premiums.

UITF Abstract 36: Contracts for sales of capacity

311 Is unlikely to be relevant to institutions. Entities in some industries (electricity and telecommunications industries) enter into contracts that convey the rights to use some or all of the capacity of a physical asset. The abstract deals with three issues:

(a) whether a contract for the right to use capacity should be reported as a sale of an asset (or a component of a larger asset) or whether the income from the contract should be measured over its life;
(b) the presentation of transactions in the performance statements – where the criteria for reporting the sale of the asset are met the abstract sets out the limited circumstances where the proceeds should be reported as turnover;
(c) exchanges of capacity – turnover or gains should be recognised only in rare circumstances where *assets* or services provided or received have a *readily ascertainable market value*.

UITF Abstract 38: Accounting for ESOP trusts

312 Is not applicable to institutions.

UITF Abstract 39: (IFRIC Interpretation 2) – Members' shares in co-operative entities and similar instruments

313 Is not applicable to institutions.

UITF Abstract 40: Revenue recognition and service contracts

314 Is applicable to institutions. It requires that revenue from performing services should be recognised as contract activity progresses, rather than on contract completion, when the substance of the contract is that the seller performs its contractual obligations gradually over time.

UITF Abstract 41: (IFRIC interpretation 8), 'Scope of FRS 20 (IFRS 2)'

Is not applicable to institutions. 315

UITF Abstract 42: (IFRIC interpretation 9), 'Reassessment of embedded derivatives'

Is applicable to institutions applying FRS 26. 316

UITF Abstract 43: The Interpretation of equivalence for the purposes of section 228 A of the Companies Act 1985

Is not applicable to institutions. 317

UITF Abstract 44: (IFRIC interpretation 11),'FRS 20 (IFRS 2)- group and Treasury Share Transactions

Is not applicable to institutions. 318

UITF Abstract 45: (IFRIC interpretation 6), 'Liabilities arising from Participating in a specific market – Waste Electrical and Electronic Equipment

Is not applicable to institutions. 319

Financial Reporting Standard for Smaller Entities

Institutions should not adopt the Financial Reporting Standard for Smaller Entities. 320

Appendix 1 – Definition of terms

The definitions which follow have been adopted for the purposes of this statement. The definitions are necessarily summarised and where an FRS or SSAP is referred to this should be read in order to gain a full understanding of the context of the definitions.

Accounting policies	are defined in FRS 18 as those principles, bases, conventions, rules and practices applied by an entity that specify how the effects of transactions and other events are to be reflected in its *financial statements*.
Accounts	comprise the income and expenditure account (including footnotes), the balance sheet, the cash flow statement and the statement of total recognised gains and losses.
Acquisition	a combination that is not a merger. An acquisition is accounted for by using the acquisition method of accounting.
Actuarial gains and losses	are defined in FRS 17 as changes in actuarial deficits or surpluses that arise because: (a) events have not coincided with the actuarial assumptions made for the last valuation (experience gains and losses); or (b) the actuarial assumptions have changed.
Agency funds	funds received as paying agent on behalf of another body.
Assets	are defined in FRS 5 as the rights or other access to future economic benefits controlled by an entity as a result of past transactions or events.
Associates	are defined in FRS 9 as an entity (other than a *subsidiary undertaking*) in which another entity (the investor) has a participating interest and over whose operating and financial policies the investor exercises a significant influence.
Business combination	is the bringing together of separate institutions, or other entities, or organisations, into one institution as a result of one institution uniting with, or obtaining *control* over the net *assets* and operations of, another institution or entity.
Capital grants	are those grants that have been specifically identified by the grantor to be used for the purchase, construction or development of *assets*.

Charitable funds	are *endowment funds*, specific charitable donations or the results of appeals where the governing body has a fiduciary duty to protect the *assets* of the fund, spend funds appropriately (and in accordance with any restrictions) and ensure accountability.
Class of tangible fixed assets	is a category of *tangible fixed assets* having a similar nature, function or use in the activities of the institution.
Consolidated financial statements	are the *financial statements* of a *group* prepared by statements *consolidation*.
Consolidation	is the process of adjusting and combining financial information from the individual *financial statements* of a parent institution and its *subsidiary undertakings* to prepare *consolidated financial statements* that present financial information for the *group* as a single economic entity.
Constructive obligation	is an obligation that derives from an institution's actions where: (a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and (b) as a result, the institution has created a valid expectation on the part of those other parties that it will discharge those responsibilities.
Control	is the ability of an undertaking to direct the financial and operating policies of another undertaking with a view to gaining economic benefits from its activities.
Contingent liability	is defined in FRS 12 as either a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's *control* or a present obligation that arises from past events but is not recognised because it is not probable that a transfer of economic benefits will be required or because the amount cannot be measured reliably.
Current asset investments	are those investments other than fixed asset investments or endowment asset investments.

Current service costs	are defined in FRS 17 as the increase in the present value of the scheme *liabilities* expected to arise from employee service in the current period.
Current value	is the current value of a tangible fixed asset to the business is the lower of replacement cost and recoverable amount.
Curtailment	is defined in FRS 17 as an event that reduces the expected years of future service of present employees or reduces for a number of employees the accrual of defined benefits for some or all of their future service. Curtailments include: (a) termination of employees' services earlier than expected, for example as a result of closing a factory or discontinuing a segment of a business, and (b) termination of, or amendment to the terms of, a defined benefit scheme so that some or all future service by current employees will no longer qualify for benefits or will qualify only for reduced benefits.
Date of acquisition	is the date on which *control* of the acquired institution or other entity passes to the acquirer institution. This is the date from which the acquired institution or entity is accounted for by the acquirer institution as a *subsidiary undertaking* under FRS 2 'Accounting for subsidiary undertakings'.
Defined benefit scheme	is a pension or other retirement benefit scheme other than a defined contribution scheme. Usually, the scheme rules define the benefits independently of the contributions payable, and the benefits are not directly related to the investments of the scheme. The scheme may be funded or unfunded.
Defined contribution scheme	is defined in FRS 17 as a pension or other retirement benefit scheme into which an employer pays regular contributions fixed as an amount or as a percentage of pay and will have no legal or *constructive obligation* to pay further contributions if the scheme does not have sufficient *assets* to pay all employee benefits relating to employee service in the current and prior periods.

	An individual member's benefits are determined by reference to contributions paid into the scheme in respect of that member, usually increased by an amount based on the investment return on those contributions. Defined contribution schemes may also provide death-in-service benefits. For the purposes of this definition, death-in-service benefits are not deemed to relate to employee service in the current and prior periods.
Depreciable amount	is the cost of a tangible fixed asset (or, where an asset is revalued, the revalued amount) less its residual value.
Depreciation	is the measure of the cost or revalued amount of the economic benefits of the *tangible fixed assets* that have been consumed during the period.
Depreciated replacement cost	is the current cost of replacing an asset with a modern equivalent asset less deductions for physical deterioration and all relevant forms of obsolescence and optimisation.
Depreciated replacement cost (of tangible fixed assets other than property)	is the cost of replacing an existing tangible fixed asset with an identical or substantially similar new asset having a similar production or service capacity, from which appropriate deductions are made to reflect the value attributable to the remaining portion of the total useful economic life of the asset and the residual value at the end of the asset's useful economic life.
Deferred capital grants	are those capital grants where an asset purchased with such a grant has been capitalised. The deferred capital grant related to the asset is included in the balance sheet and released to the income and expenditure account over the life of the asset to which it relates.
Dominant influence	is influence that can be exercised to achieve the operating and financial policies desired by the holder of the influence, notwithstanding the rights or influence of any other party.
Endowment assets	are those assets held for *endowment funds* where the terms of the endowment require the income and/or the capital of the funds to be used for restricted (specific) or unrestricted (general) purposes of the institution.

Endowment funds	are *charitable funds* held on trust to be retained for the benefit of the institution as a capital fund. In most instances this type of charitable fund is permanent, because the governing body, as trustees, are required to permanently maintain the whole of the endowment fund.
Equity instrument	is any contract that evidences a residual interest in the assets of an entity after deducting all of its *liabilities*.
Equity method	is a method of accounting that brings an investment into its investor's *financial statements* initially at its cost, identifying any goodwill arising. The carrying amount of the investment is adjusted in each period by the investor's share of the results of its investee less any amortisation or write-off for goodwill, the investor's share of any relevant gains or losses, and any other changes in the investee's net assets including distributions to its owners, for example by dividend. The investor's share of its investee's results is recognised in its income and expenditure account. The investor's cash flow statement includes the cash flows between the investor and its investee, for example relating to dividends and loans.
Estimation techniques	are defined in FRS 18 as the methods adopted by an entity to arrive at estimated monetary amounts, corresponding to the measurement bases selected, for *assets*, *liabilities*, gains, losses and changes to shareholders' funds. Estimation techniques implement the measurement aspects of *accounting policies*.
Existing use value	is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion, assuming that the buyer is granted vacant possession of all parts of the property required by the business and disregarding potential alternative uses and any other characteristics of the property that would cause its *market value* to differ from that needed to replace the remaining service potential at least cost.

Expected rate of return on assets	is defined in FRS 17 as the average rate of return, including both income and changes in fair value but net of scheme expenses, expected over the remaining life of the related obligation on the actual *assets* held by the scheme.
Fair value	is the amount at which an asset or liability could be exchanged in an arm's length transaction between informed and willing parties, other than in a forced or liquidation sale.
Financial asset	as covered by FRS 25 is any asset that is: (a) cash; (b) an equity instrument of another entity; (c) a contractual right: i. to receive cash or another financial asset from another entity; or ii. to exchange *financial assets* or *financial liabilities* with another entity under conditions that are potentially favourable to the entity; or (d) a contract that will or may be settled in the entity's own equity instruments and is: i. a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or ii. a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another *financial asset* for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.
Financial instrument	as referred to in FRS 25 is any contract that gives rise to a *financial asset* of one entity and a *financial liability* or equity instrument of another entity.

Financial liability	as referred to in FRS 25 is any liability that is: (a) a contractual obligation: i. to deliver cash or another *financial asset* to another entity; or ii. to exchange *financial assets* or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or (b) a contract that will or may be settled in the entity's own equity instruments and is: i. a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or ii. a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another *financial asset* for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.
Financial statements	comprise the accounts (otherwise known as the primary statements), the statement of accounting policies and the notes to the accounts.
Fixed asset investments	are those investments intended to be held for use on a continuing basis. An investment should be classified as a fixed asset only where an intention to hold the investment for the long term can clearly be demonstrated or where there are restrictions regarding the investor's ability to dispose of the investment.
Funders and financial supporters	are the defining class of user for the *financial statements* of public benefit entities. They provide a source of cash or other resources without the incentive of a return, either a direct return (like interest paid on a loan) or in the form of an exchange for direct benefits (goods or services), for themselves. The funder and financial supporter generally provide grants or donations to the entity. The defining class of user includes the present and potential funders and financial supporters of the entity. A present funder or financial supporter would include an individual or entity that had made a contribution in the past if that contribution created an ongoing financial interest.

Funding bodies	refers to the non-departmental public bodies whose role is to distribute public funds to further education and higher education institutions. They include the Higher Education Funding Councils for England and Wales, the Learning and Skills Council, the Scottish Funding Council, National Assembly for Wales and the Training and Development Agency for Schools. It also includes the Department for Employment and Learning, Northern Ireland.
FRS	refers to a financial reporting standard published by the Accounting Standards Board in the United Kingdom.
General income	refers to income that can be applied to any activity of the institution at the discretion of the institution. Examples of such income are funding body recurrent grant (which may have some restrictions), tuition fees and income from general endowments.
Group	refers to the reporting institution and all its subsidiary undertakings.
Gross equity method	is a form of equity method under which the investor's share of the aggregate gross *assets* and *liabilities* underlying the net amount included for the investment is shown on the face of the balance sheet and, in the profit and loss account, the investor's share of the investee's turnover is noted.
Heritage assets	are assets with historic, artistic, scientific, technological, geophysical or environmental qualities that are held and maintained principally for their contribution to knowledge and culture.
Identifiable assets and liabilities	are the *assets* and *liabilities* of the acquired institution or entity that are capable of being disposed of or settled separately, without disposing of a business of the institution or entity.
Impairment	is a reduction in the recoverable amount of a fixed asset or goodwill below its carrying amount.

Income generating unit	is a *group* of *assets*, *liabilities* and associated goodwill that generates income that is largely independent of the reporting entity's other income streams. The *assets* and *liabilities* include those directly involved in generating the income and an appropriate portion of those used to generate more than one income stream.
Intangible assets	are non-financial fixed assets that do not have physical substance but are identifiable and are controlled by the entity through custody or legal rights.
Interest cost	is defined in FRS 17 as the expected increase during the period in the present value of the scheme *liabilities* because the benefits are one period closer to settlement.
Joint Venture	is defined in FRS 9 as an entity in which the reporting entity holds an interest on a long-term basis and is jointly controlled by the reporting entity and one or more other ventures under a contractual arrangement.
Liabilities	are defined in FRS 5 as an entity's obligations to transfer economic benefits as a result of past transactions or events.
Linked presentation	as referred to in FRS 5 is a special form of presentation used for certain non-recourse finance arrangements which shows, on the face of the balance sheet, the finance deducted from the gross amount of the item it finances.
Market value	is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion.
Materiality	is an expression of the relative significance or importance of a particular matter in the context of the *financial statements* as a whole. A matter is material if its omission would reasonably influence the decisions of the users of the institution's reports and *financial statements*. Likewise, a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the *financial statements* or of individual items included in them. Materiality is not capable of general mathematical definition as it has both qualitative and quantitative aspects.

Merger	is a combination that results in the creation of a new reporting institution formed from the combining parties, in which the governing body (or equivalent) of the combining institutions come together in a partnership for the mutual sharing of the risks and benefits of the combined institution, and in which no party to the combination in substance obtains *control* over any other, or is otherwise seen to be dominant, whether by virtue of the proportion of the influence of its governing body, directors or otherwise.
Net realisable value	is the amount at which an asset could be disposed of, less any direct selling costs.
Obligating event	is an event that creates a legal or *constructive obligation* that results in an entity having no realistic alternative to settling that obligation.
Onerous contract	is a contract in which the unavoidable costs of meeting the obligations under it exceed the economic benefits expected to be received under it.
Operating and financial review (OFR)	is a narrative explanation, provided in or accompanying the *financial statements*, of the main trends and factors underlying the development, performance and position of an institution during the financial year covered by the *financial statements*, and those which are likely to affect the entity's future development, performance and position.
Past service cost	is defined in FRS 17 as the increase in the present value of the scheme *liabilities* related to employee service in prior periods arising in the current period as a result of the introduction of, or improvement to, retirement benefits.
Purchased goodwill	is the difference between the cost of an acquired entity and the aggregate of the fair values of that entity's identifiable *assets* and *liabilities*. Positive goodwill arises when the acquisition cost exceeds the aggregate fair values of the identifiable *assets* and *liabilities*. Negative goodwill arises when the aggregate fair values of the identifiable assets and *liabilities* of the entity exceed the acquisition cost.

Projected unit method	is an accrued benefits valuation method in which the scheme *liabilities* make allowance for projected earnings. An accrued benefits valuation method is a valuation method in which the scheme *liabilities* at the valuation date relate to: (a) the benefits for pensioners and deferred pensioners (i.e. individuals who have ceased to be active members but are entitled to benefits payable at a later date) and their dependants, allowing where appropriate for future increases; and (b) the accrued benefits for members in service on the valuation date. The accrued benefits are the benefits for service up to a given point in time, whether vested rights or not.
Provision	is defined in FRS 12 as a liability of uncertain timing or amount.
Qualified valuer (internal or external)	is a person conducting the valuation who holds a recognised and relevant professional qualification and having recent post-qualification experience, and sufficient knowledge of the state of the market, in the location and category of the tangible fixed asset being valued. An internal valuer is a director, officer or employee of the entity. An external valuer is a valuer who, together with any associates, has no material links with the institution, an agent acting on behalf of the institution, or the subject of the assignment.
Quasi-subsidiary	is a company, trust, partnership or other vehicle that, though not fulfilling the definition of a subsidiary, is directly or indirectly controlled by the reporting entity and gives rise to benefits for that entity that are in substance no different from those that would arise were the vehicle a subsidiary.
Recoverable amount	is the greater of the net realisable value of an asset and, where appropriate, the value in use.
Readily ascertainable market value	is, in relation to an intangible asset, the value that is established by reference to a market where: (a) the asset belongs to a homogeneous population of assets that are equivalent in all material respects; and (b) an active market, evidenced by frequent transactions, exists for that population of *assets*.

Related party transaction	is defined in FRS 8 as the transfer of assets or liabilities or the performance of services by, to or for a related party irrespective of whether a price is charged.
Reports and financial statements	comprise the *financial statements*, a statement of corporate governance, a statement of the responsibilities of the council, board of governors or institutional equivalent, the auditors' report and the operating and financial review (treasurer's report, members' report or institutional equivalent).
Restricted charitable donations	are subject to restrictions on their application, which may be determined by the donor, or with their authority (e.g. through a public appeal) or created through legal process, but still within the wider objects of the institution.
Retirement benefits	are under FRS 17 all forms of consideration given by an employer in exchange for services rendered by employees that are payable after the completion of employment. Retirement benefits do not include termination benefits payable as a result of either; (a) an employer's decision to terminate an employee's employment before the normal retirement date; or (b) an employee's decision to accept voluntary redundancy in exchange for those benefits, because these are not given in exchange for services rendered by employees.
Revaluation reserve	is the sum of unrealised amounts arising from the revaluation of the institution's *tangible fixed assets*.
Scheme liabilities	are, under FRS 17, the *liabilities* of a defined benefit scheme for outgoings due after the valuation date. Scheme *liabilities* measured using the projected unit method reflect the benefits that the employer is committed to provide for service up to the valuation date.

Settlements	relate to, under FRS 17, an irrevocable action that relieves the employer (or the defined benefit scheme) of the primary responsibility for a pension obligation and eliminates significant risks relating to the obligation and the assets used to effect the settlement. Settlements include: (a) a lump-sum cash payment to scheme members in exchange for their rights to receive specified pension benefits; (b) the purchase of an irrevocable annuity contract sufficient to cover vested benefits; and (c) the transfer of scheme *assets* and *liabilities* relating to a group of employees leaving the scheme.
Specialised properties	are properties that are rarely if ever sold in the market, except by way of a sale of the business or institution of which it is part, due to uniqueness arising from specialised nature and design, its configuration, size, location, or otherwise.
Specific income	is income that can only be applied to a specific purpose or activity so designated by the grantor or donor. Examples of such income are *Funding body* grants for specific purposes, research grants and some research contracts and income from Restricted Endowments.
SSAP	refers to a Statement of Standard Accounting Practice published by the Accounting Standards Board in the United Kingdom.
Subsidiary undertaking	is analogous to the definition in the Companies Act and FRS 2 and is a body corporate or partnership or unincorporated association carrying on a trade or business with or without a view to profit. It may also include charitable trusts, students' unions and other similar bodies.

An undertaking is a subsidiary of a parent undertaking where the parent:
(a) holds a majority of voting rights; or
(b) is a member of the undertaking and can appoint or remove directors having the majority of the votes on the board; or
(c) has a right to exercise a dominant influence over the undertaking by virtue of provisions either in its memorandum or articles or in a 'control contract'; or
(d) is a member of the undertaking and operates *control* via an agreement with other shareholders; or
(e) owns a participating interest in the undertaking and actually exercises *dominant influence* or operates unified management.

Tangible fixed assets	are defined in FRS 15 as those assets that have physical substance and are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes on a continuing basis in the reporting entity's activities.
UITF Abstracts	refer to the Urgent Issues Task Force Abstracts which are issued by the Accounting Standards Board in the United Kingdom.
Unrestricted charitable donations	are expendable at the discretion of the institution in furtherance of the institution's objects.
Value in use	is the present value of the future cash flows obtainable as a result of an asset's continued use, including those resulting from the ultimate disposal of the asset.
Vested rights	are, under FRS 17, defined as: (a) for active members, benefits to which they would unconditionally be entitled on leaving the scheme; (b) for deferred pensioners, their preserved benefits; (c) for pensioners, pensions to which they are entitled. Vested rights include where appropriate related benefits for spouses and other dependents.

Appendix 2 – Primary statements

Consolidated income and expenditure account

	Notes	Year ended 31 July 200X £000	Year ended 31 July 200Y £000
Continuing operations[1]			
Income			
Funding body grants	X	X	X
Tuition fees and education contracts	X	X	X
Research grants and contracts	X	X	X
Other income	X	X	X
Endowment and investment income	X	X	X
Total Income	**X**	**X**	**X**
Expenditure			
Staff costs	X	X	X
Other operating expenses	X	X	X
Depreciation	X	X	X
Interest and other finance costs	X	X	X
Total Expenditure	**X**	**X**	**X**
Surplus/(deficit) after depreciation of tangible fixed assets at valuation and before tax	**X**	**X**	**X**
Taxation	X	X	X
Surplus/(deficit) after depreciation of assets at valuation and tax	**X**	**X**	**X**
Minority interest	X	X	X
Surplus/(deficit) before exceptional items	**X**	**X**	**X**
Exceptional items: continuing operations	X	X	X
Disposals of fixed assets	X	X	X
Sale and termination of operations	X	X	X
Surplus/(deficit) on continuing operations after depreciation of assets at valuation and disposal of assets and tax	**X**	**X**	**X**
Surplus/(deficit) for the year transferred to accumulated income in endowment funds	X	X	X
Surplus/(deficit) for the year retained within general reserves	**X**	**X**	**X**

Statement of group historical cost surpluses and deficits

	Notes	Year ended 31 July 200X £000	Year ended 31 July 200Y £000
Surplus/(deficit) on continuing operations before taxation		X	X
Difference between historical cost depreciation and the actual charge for the period calculated on the re-valued amount	X	X	X
Realisation of property revaluation gains of previous years	X	X	X
Historical cost surplus/(deficit) for the year before taxation		**X**	**X**
Historical cost surplus/(deficit) for the year after taxation		**X**	**X**

Statement of group total recognised gains and losses

	Notes	Year ended 31 July 200X £000	Year ended 31 July 200Y £000
Surplus/(deficit) on continuing operations after depreciation of assets at valuation and disposal of assets and tax		X	X
Unrealised gains on investments	X	X	X
Unrealised surplus on revaluation of fixed assets	X	X	X
Endowment income retained in the year	X	X	X
Total return on permanent endowments not applied in the current financial period	X	X	X
Appreciation of endowment asset investments	X	X	X
Actuarial gain/(loss) in respect of pension schemes	X	X	X
Total recognised gains/(losses) relating to the year		**X**	**X**
Reconciliation			
Opening reserves and endowments		X	
Total recognised gains/(losses) for the year		X	
Closing reserves and endowments		**X**	

Balance Sheets

	Notes	Consolidated 200X £000	Institution 200X £000	Consolidated 200Y £000	Institution 200Y £000
Fixed assets					
Intangible assets	x	X	X	X	X
Tangible assets	x	X	X	X	X
Investments	x	X	X	X	X
	x	**X**	**X**	**X**	**X**
Endowment Assets	**x**	**X**	**X**	**X**	**X**
Current assets	**x**	**X**	**X**	**X**	**X**
Stock		X	X	X	X
Debtors	x	X	X	X	X
Investments		X	X	X	X
Cash at bank and in hand		X	X	X	X
		X	X	X	X
Less: Creditors - amounts falling due within one year	x	(X)	(X)	(X)	(X)
Net current assets		**X**	**X**	**X**	**X**
Total assets less current liabilities		**X**	**X**	**X**	**X**
Less: Creditors - amounts falling due after more than one year	x	(X)	(X)	(X)	(X)
Less: Provisions for liabilities	x	(X)	(X)	(X)	(X)
Net assets excluding pension asset/(liability)		**X**	**X**	**X**	**X**
Net pension asset/(liability)	x	(X)	(X)	(X)	(X)
Net assets including pension asset/liability		**X**	**X**	**X**	**X**
Deferred capital grants	x	X	X	X	X
Endowment funds					
Expendable	x	X	X	X	X
Permanent	x	X	X	X	X
		X	X	X	X
Reserves					
Income and expenditure account excluding pension reserve		X	X	X	X
Pension reserve	x	X	X	X	X
Income and expenditure account including pension reserve	x	X	X	X	X
Revaluation reserve	x	X	X	X	X
		X	X	X	X
Total funds		**X**	**X**	**X**	**X**

Consolidated Cash Flow Statement

	Notes	Year ended 31 July 200X £000	Year ended 31 July 200Y £000
Net cash inflow/(outflow) from operating activities	x	X	X
Return on investments and servicing of finance			
Income from endowments	x	X	X
Interest received		X	X
Interest paid		(X)	(X)
Net cash inflow/(outflow) from returns on investments and servicing of finance		**X**	**X**
Taxation	x	(X)	(X)
Capital expenditure			
Endowment assets acquired and received	x	X	X
Receipts from the sale of endowment assets	x	X	X
Payments to acquire tangible assets	x	X	X
Deferred capital grants received		X	X
Net cash outflow from capital expenditure		X	X
Cash inflow/(outflow) before management of liquid resources		X	X
Management of liquid resources			
Cash transferred from/(to) term deposits		X	X
Financing			
Bank loan drawn down in year		X	X
Loan repayment in the year		(X)	(X)
Increase/(decrease) in cash in the year	x	X	X

Reconciliation of net cash flow to movement in net funds/(debt)*

Increase/(decrease) in cash in the year	X	X
Cash inflow/(outflow) from new bank loan	X	X
Cash inflow/(outflow) from liquid resources	X	X
Loan repayment in year	X	X
	X	X
Change in net funds	X	X
Net funds at 1 August	X	X
Net funds at 31 July	**X**	**X**

*For the purposes of this SORP this is not a primary statement and can be shown in the notes to the accounts

Appendix 3 – Notes to the Financial Statements

This Appendix provides a list of notes which may be required to accompany an institution's accounts. This provides a list where institutions may reasonably be expected to disclose further information in the notes to the accounts and is not intended to be exhaustive.

Funding body grants

Tuition fees and education contracts
Research grants and contracts
Other income
Endowment and investment income
Staff costs (and staff numbers)
Emoluments of the Principal/Vice-Chancellor and other higher paid staff
Other operating expenses (analysed by activity)
Interest and other finance costs
Taxation
Surplus/(deficit) for the year analysed between the institution and the group
Exceptional items (e.g. disposals of fixed assets, or sale or termination of operations)
Intangible assets
Tangible assets
Investments
Investments in joint ventures
Endowment Assets
Debtors
Current asset investments
Creditors: amounts falling due within one year

Creditors: amounts falling due after more than one year
Provisions
Deferred Capital Grants
Endowment Funds
Revaluation reserve
Income and expenditure reserve
Reconciliation of Surplus Before Tax To Net Cash (Outflow)/Inflow From Operating Activities
*Returns on Investment and Servicing of Finance
*Capital Expenditure and Financial Investment
*Management of Liquid Resources
*Financing

Contingent liabilities

Prior Period Adjustments
Post Balance Sheet Events
Analysis of Changes In Net Funds
Cash flow relating to exceptional items
Capital and other commitments
Subsidiary Undertakings
Agency arrangements (memo note)
*Principal accounting policies and estimation techniques

* unless detail provided on face of the cash flow statement

Appendix 4 – Membership of the HE/FE Board for the SORP

Generic List of Organisations Represented

Chair (Universities UK)	Treasurer of Universities UK: this is always a member of Universties UK (i.e. a Vice-Chancellor of a UK university) who has been selected for the Treasurer role because of his/her respected status within the sector and experience in higher education resource management.
Other Sector Representative Organisations	Association of Colleges (FE sector) GuildHE (previously called SCOP: represents HE colleges and some universities) Association of Scottish Colleges (FE in Scotland)
Funding Councils	Higher Education Funding Council for England (HE England) Learning and Skills Council (FE England) Scottish Funding Council (HE and FE) Welsh Assembly Government (HE and FE) Department of Education and Learning Northern Ireland
Finance Directors	British Universities Finance Directors Group (BUFDG) FE Colleges Finance Directors Group (FECFDG) Chair of the BUFDG Accounting Standards Group (ASG) (technical group for the SORP Board) Representative of Colleges in Northern Ireland
Auditors' Representatives	PricewaterhouseCoopers LLP KPMG LLP
In Attendance	UUK and GuildHE secretariat BUFDG technical secretariat SORP technical author (Matthew Hodge from PricewaterhouseCoopers) Accounting Standards Board

List of Members, July 2007

Chair	Professor Rick Trainor, Principal of King's College London
Association of Colleges	Mr Julian Gravatt, Director of Funding and Development
GuildHE	(member to be confirmed)
Association of Scottish Colleges	Mr Alan Williamson, Director of Finance, Jewel and Esk Valley College
HEFCE	Mr Ian Lewis, Head of Finance
Learning and Skills Council	Mr Richard Healey, Director of Finance
Scottish Funding Council	Mr Andrew Millar, Senior Financial Analyst
Welsh Assembly Government	Mr Rob Rogers, Head of Standards, Quality and Governance Division, Department of Education, Lifelong Learning and Skills
DELNI	Mr Paul Liddy, FE Accountant
BUFDG	Mr Phil Harding, Director of Finance, University of Westminster and Chair of BUFDG
FECFDG	Mr Martin Smith, Director of Finance and Corporate Services, Runshaw College
BUFDG ASG	Mr Miles Hedges, Finance Director, The Open University
Northern Ireland Colleges	Ms Josephine Kelly, Director of Finance & Corporate Services, Lisburn Institute of Further and Higher Education
Auditors' Representatives	Mr Ian Looker, PricewaterhouseCoopers LLP Mr Mike Rowley, KPMG LLP

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