Accounting for Nonprofit Organizations:

A Case Study of British Red Cross

by

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Abstract

Accounting for Nonprofit organizations (NPOs) has become an interesting and promising topic, which is different from commercial accounting in many ways: The objective of NPOs is to provide services for public benefits, not to generate profits for partners or shareholders. Since their expenditures must be covered by revenues, which are financed by grants or donations, not market transactions, NPOs is money focused, while commercial organizations are profit focused. A case study of British Red Cross (BRC) is undertaken by analyzing its bookkeeping and financial statements, the problems and suggestions could be helpful to improve the financial reports of the other NPOs.

Key words: NPOs, BRC, money focus, profit focus, bookkeeping, financial reports, fund accounting.

Foreword

This thesis aims at improving the accounting for NPOs, which is a comparatively neglected area, while nowadays NPOs play important roles all over the world, and they have unique objectives thus accounting requirements. A case study of British Red Cross is undertaken, the problems and suggestions could be helpful for the other NPOs to provide more informative financial reports.

I should express my sincere thanks to my supervisor Norvald Monsen. He inspired me to research this interesting and promising topic, and his generous help kept pushing and improving this thesis during the past year. I am also grateful to all the encouragements from my parents and friends.

Jin Zi

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Chapter 1 Introduction

1.1 Problem

Nonprofit organizations (NPOs) are playing more and more influential and powerful roles all over the world nowadays. From small, local to large, national and international organizations, they cover different aspects of social activities, such as religion, politics, education, health, environment, charity, etc.

Accounting for NPOs has become an interesting and important topic. NPOs incur expenditures when providing services to help people, while they are financed by grants or donations, not by market transactions from selling products or services, which makes their accounting requirements and treatments different from commercial accounting in many ways. Instead of taking interest in the profit effect of revenues and expenditures, NPOs focus on the money effect. In many cases, the incoming resources have their unique usages, which demand separate accounting records.

1.2 Purpose

The purpose of the thesis is to improve the financial reports of NPOs. A case study of British Red Cross (BRC) is undertaken, focusing on its bookkeeping and annual financial statements. Specifically, new and more informative financial statements will be developed for BRC, which could be a starting point to improve the accounting for the other NPOs.

1.3 Further Structure

The thesis will start with the research methodology applied and the accounting framework related; then follow a general introduction and literature review of accounting for NPOs; after that, there is a case study of BRC, including background of the International Red Cross and Red Crescent Movement, accounting information of BRC, deduced double-entry bookkeeping, further analysis and improvements;

finally, the accounting problems and our solutions in the case will be concluded and generalized analytically to other NPOs; in addition, a prediction of the development of accounting for NPOs and suggestions for further practice and research are made.

Chapter 2 Methodology

2.1 Case Study Approach

This thesis applies case study as the research strategy. According to Yin (1985), a case study is an empirical inquiry that investigates a contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used. Case studies rely on analytical generalization, whereas statistical generalization is for survey research. In analytical generalization, the investigator is striving to generalize a particular set of results to some broader theory. Here a case study of BRC is undertaken, and its analysis is generalized analytically to other NPOs.

2.2 Different Perspectives

According to Monsen (1987), there are three methods in the research, and the choice of them will affect the conclusions.

(a) Analytical Perspective

According to the analytical perspective, the reality is considered to be composed of various components in an objective manner; the whole is equal to the sum of its parts; the knowledge developed is explained by observed phenomena and independent of individual character, which means that different individuals will perceive the same phenomenon.

(b) System Perspective

According to the system perspective, the reality is assumed to be composed in such a way that the whole differs from the sum of its parts, which means that there are positive or negative effects in their relationships.

(c) Individual Perspective

According to the individual perspective, reality is assumed to consist of various processes; the purpose is to identify the significance of different individuals in the specific environment; the knowledge developed is dependent of individuals.

(d) Perspective Chosen

Here the analytical perspective is chosen. Financial statements are prepared with the help of merchant’s double-entry bookkeeping, which always follows the rule of the same amounts in two accounts and two entries (debits = credits) (Appendix 11). BRC’s accounting regulations and figures are explored to give the whole financial picture.

Chapter 3 Accounting Literature Review

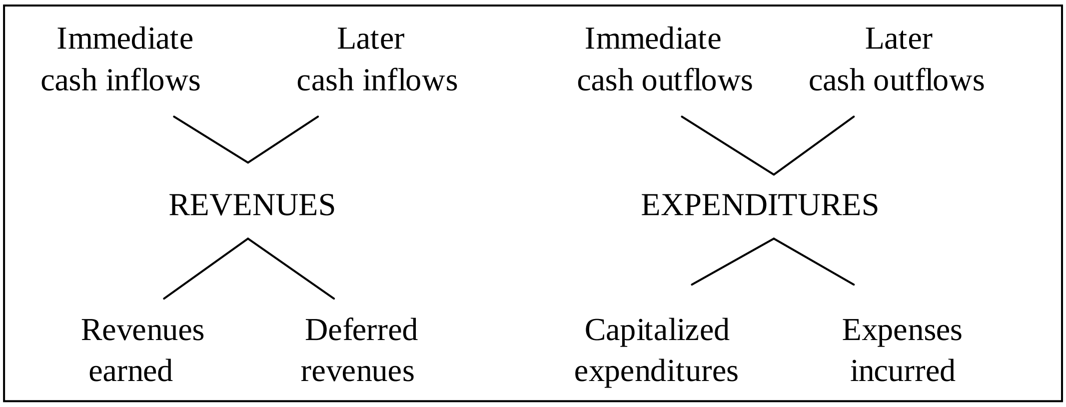
3.1 Introduction

There are two types of accounts: money accounts and profitability accounts; two basic bookkeeping methods: single-entry bookkeeping and double-entry bookkeeping; different accounting models: including commercial accounting, cameral accounting and fund accounting.

3.2 Money Accounts versus Profitability Accounts

The main concepts in financial accounting are revenues and expenditures. (See Figure 3.1) Revenues represent claims on cash receipts, while expenditures represent obligations for cash payments. Their immediate or later cash flows show the money effect, which influences the organization's working capital (Here we use a broad definition of "money"), as well as the profitability effect, which influences the organization's equity.

Figure 3.1 Revenues and expenditures



(Source: Műlhaupt, 1987, Abbildung 5, p. 75;
translated from German by Monsen (2008))

An accounting model focusing on the money effect of the revenues and expenditures, in the form of immediate or later cash flows, is referred to as money accounts. On the other hand, an accounting model focusing on the profitability effect of the revenues and expenditures, in the form of revenues earned and expenses incurred, is referred to as profitability accounts. (Monsen, 2009)

3.3 Single-entry vs. Double-entry Bookkeeping

Financial statements can be prepared with the help of either single-entry or double-entry bookkeeping. While single-entry bookkeeping refers to a system where every transaction is registered only once in one account, double-entry bookkeeping refers to a system which always involves two accounts and two entries of the same amounts (debits = credits). However, within systematic single-entry bookkeeping, a transaction may be entered more than once to provide a performance result. (Monsen, 2001)

3.4 Commercial Accounting

According to Monsen (2002), commercial accounting, or accrual accounting, used by business organizations with a profit objective, focuses on performance result, not money effect. Meanwhile, it seems to have an increasingly stronger influence on accounting for NPOs as well.

Today, the double-entry bookkeeping, more precisely referred to as the merchant's double-entry bookkeeping method (Walb, 1926), is applied to show the performance result, which is the difference between revenues earned and the expenses incurred during the period, which is also the change in the balance account during the same period. (Monsen, 2008) (Figure 3.2)

Figure 3.2 Commercial accounting and bookkeeping method

Double-entry bookkeeping

↓

Commercial Accounting

The merchant's double-entry bookkeeping method

↓

Profitability accounts

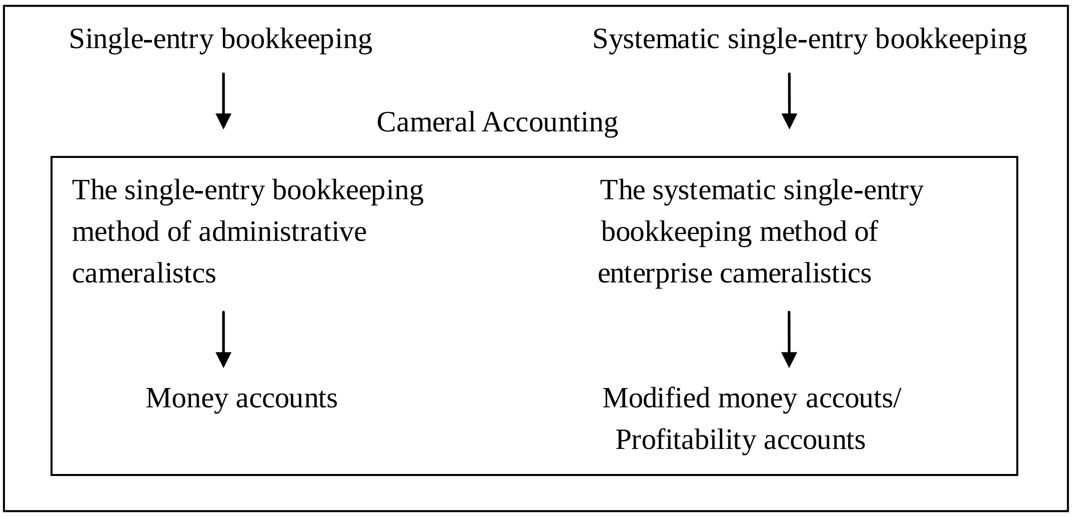
(Source: Adapted from Monsen (2008), p. 108)

Walb (1926) points out that the merchant's double-entry bookkeeping is an important improvement compared to single-entry bookkeeping from a profitability point of view, because it allows for the presentation of the performance result for the period both as it appears via the activity side (income statement) and via the payment side (balance sheet), and their direct link explains the equity change in the balance account during the same period. (Monsen, 2008) And the present financial status is fully accounted by past event. (Ijiri, 1982) However, in Monsen (2001)'s view, it can be questioned if the development of single-entry to the merchant's double-entry bookkeeping is also an advantage from a cash flow point of view. Since the merchant's double-entry bookkeeping compares revenues earned and expenses incurred for the period, independent of when the corresponding cash inflows and cash outflows occur.

3.5 Cameral Accounting

According to Monsen (2001, 2008, 2009), cameral accounting (CAM) is developed in the continental German-speaking countries for use in governmental organizations, including administrative cameralistics (ACAM) and enterprise cameralistics (ECAM), both based on single-entry bookkeeping, namely "the single-entry bookkeeping method of administrative cameralistics" and "the systematic single-entry bookkeeping method of enterprise cameralistic", respectively. The former method is used for preparing money accounts, while the latter method is used for preparing "modified money accounts/profitability accounts ". (Figure 3.3) The main objectives of ACAM are money management, budgetary control and payment control. The objective of ECAM, however, is to prepare similar profitability information as what is prepared by using the merchant's double-entry bookkeeping method.

Figure 3.3 Cameral accounting and bookkeeping methods.



(Source: Adapted from Monsen (2008), p. 108)

3.6 Fund Accounting

A fund is defined as a separate pool of monetary and other resources established to support specified activities and operated and accounted for independently of other accounting entities, which is established when restrictions have been placed on the purposes for which particular resources may be used.

“Fund accounting was developed to present fairly the financial transactions unique to nonprofit organizations” (Herzlinger and Sherman, 1980), reflecting the accountability or stewardship concept.

Fund accounting is a system of accounting used when public sectors received restricted contributions. Separate records are kept for:

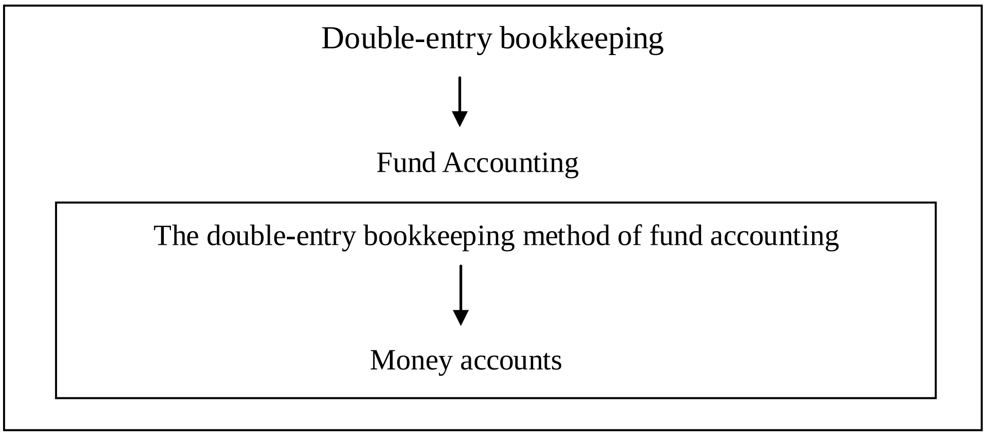
> Resources donated to an organization, which are restricted by donors or other outside parties to certain specified purposes or use;

> Portions of an organization’s unrestricted resources which the board has set aside for some specified future use;

> All other unrestricted amounts.

A special version of double-entry bookkeeping is used within fund accounting. The double-entry bookkeeping method of fund accounting is used for money accounts and prepared for specific funds, focusing on revenues and expenditures. (Figure 3.4)

Figure 3.4 Fund accounting and bookkeeping method



(Source: Adapted from Monsen (2008), p. 108)

Chapter 4 Accounting for Nonprofit Organizations

4.1 Introduction

In this chapter, we will discuss which accounting model should be used by NPOs. First, there is an overview of accounting for NPOs, and why it is different from commercial accounting. Second, the debate within Anglo-Saxon countries about using commercial accounting and fund accounting as the framework will be summarized. Third, the debate will be broadened by using cameral accounting as the framework.

4.2 Accounting for Nonprofit Organization

(a) NPOs Defined

A nonprofit organization (abbreviated NPO, also not-for-profit) is an organization that provides assistance to individuals, groups or causes, rather than generating profits for itself. There are a wide range of NPOs: Charities, churches, hospitals, schools, as well as associations with purposes of science, literature, arts, sports, wildlife protection, etc. In most countries, governments and government agencies are considered a separate type of organization and not counted as NPOs.

(b) Principal Differences between Commercial Organizations and NPOs

There are a number of features which distinguish NPOs from commercial organizations. These are summarized in Table 1.1.

One of the principal differences between commercial organizations and NPOs is that they have different reasons for their existence. While commercial organizations pursue business profits in market transactions and distribute earnings to shareholders, the NPOs pursue public benefits and provide programs and services which are often not provided otherwise. As for NPOs, which are not market oriented, assets are contributed by voluntary funds or governmental grants, which usually have restrictions on the usage, but without expectation of repayment or economic return. In most cases, NPOs are exempted from taxes due to their contributions to social needs.

Table 1.1 Differences between commercial organizations and NPOs

Characteristic	Commercial Organizations	NPOs
Motivation:	Profit earning.	Provide programs and services that are of public benefits.
Ownership:	Partners; shareholders.	Members (no financial benefit).
Management Control:	Partners; Board of Directors.	Trustees (unpaid).
Capital Structure:	Fixed-interest loans; Equity shares.	Voluntary funds.
Sources of Income:	Sales; Provision of services; Investments.	Voluntary funds; Grants (statutory and non statutory); Fees/charges; Investments.
Performance Measurement:	Profitability; Dividend growth; Capital growth.	Quality; Economy of service; Outcomes.
Planning decisions based on:	Technological improvements; Expansion of activity; Quality enhancement; Diversification.	Expansion/contraction of activities; Funding changes; Impact of statutory changes; Research findings.

Source: Adapted from Paul Palmer (1996), p. 254

(c) Accounting Distinctions between Commercial Organizations and NPOs

There are accounting distinctions in five significant areas between commercial organizations and NPOs, which partly stem from their different objectives. In commercial organizations, the objective is to match revenue and costs to measure profitability, while in NPOs, accountability for program activities and stewardship is the objective.

As Henke (1983) says, 'Financial reports for nonprofit organizations should reflect the service story of the entity, rather than net income or net loss realized by the entity. In sharp contrast, accounting reports for profit enterprises must emphasize the extent of achievement of the profit objective and the ability of the entity to support itself.'

The five areas are discussed next:

(1) Cash versus Accrual Accounting

In commercial organizations, the record keeping is always accrual basis, which means 'that all income and charges relating to a financial year shall be taken into account, without regard to date of receipt or payment' (Parker, 1984). Since in addition to recording transactions resulting from the receipt and disbursement of cash, but also the amounts supposed to pay or receive due to the realized activities should be recorded, the accounts thus reflect a true and fair view of the state of the entity at the time they are drawn up.

In NPOs, the cash basis of accounting is often used instead, which means only transactions with cash payments are recorded, as for the unpaid bills and amounts due, they are just ignored. Cash based accounting violates the realization and matching concepts, but it is easier to apply in record keeping. Most small NPOs use the cash basis, although many of the medium and larger organizations are now using the accrual basis. Furthermore, the cash basis is often used when the nature of the organization is such that material amounts are only cash involved, so there is little difference between the cash and accrual basis. Some NPOs follow a modified form of accounting, which is a combination of accrual basis and cash basis, which makes the picture even more complicated and confusing for readers. Some other NPOs keep their records during the year on a cash basis, but at the end of the year convert to the accrual basis by recording obligations and receivables.

No matter what kind of accounting basis different organizations are using, the important thing is that the records kept are appropriate to their nature and fulfill their needs.

(2) Fund Accounting

Fund accounting is a method of segregating resources into categories, (i.e. funds) to identify both the source of funds and the use of funds, which was developed to present fairly the financial transactions unique to nonprofit organizations. (Herzlinger and Sherman, 1980)

NPOs have to account for funds received, including certain specific fund that have been given for use in a particular project, as well as general obligation to employ the organization's resources effectively. The requirement for separated accounting for restricted resources to demonstrate accountability and stewardship is solved by presenting separate financial statements for each "fund". That is the major reason fund accounting is widely used by NPOs.

Furthermore, by tracing different funds, fund accounting is also helpful to provide clearer picture of financial condition, it even improves planning and budgeting, as well as the evaluation of managerial performance.

(3) Interfund Transfers and Appropriations

Interfund transfers and appropriations are also unique to NPOs by using fund accounting: One relates to the use of "transfers" to allocate resources between funds, and the other relates to the use of appropriations to authorize future expenditure of resources for specific purposes. Both add to the complexity of financial statements.

(4) Treatment of Fixed Assets

In commercial organizations, fixed assets are always recorded as assets on the balance sheet, and are depreciated over their expected useful lives.

In NPOs, fixed assets are difficult to record, and there is no single generally accepted principle or practice to follow. Some organizations record and report fixed assets, some do not. Some record and report depreciation, some do not. The different treatments of fixed assets cause a lot of confusion.

(5) Contributions

In commercial organizations, contribution is not a usual source of income. If the amount is legally owned, it is recorded as accounts receivable.

In NPOs, contributions are the principal resource to depend on, and there could be a wide range of restrictions attached to them. Furthermore, contributions to NPOs are not legally enforceable, which makes the case even more complicated. So the contributions should be recorded in the right fund, at the right time with the right restrictions. Some contributions are made in the form of pledges that will be paid off over a period of time or in the future, the accounting problem is when to record them as assets and income. Some contributions are noncash, such as buildings, equipments, services of volunteers, which also trigger controversies.

(d) Accounting Standards for NPOs

There are few specific accounting standards for NPOs, and the legal requirements vary by country. However, regulations and guidelines which have a strong impact on accounting for NPOs are being developed by official bodies and other organizations. In addition, many books and papers have released guidance and become valuable tools for obtaining a complete and unified picture of accounting standards for NPOs.

4.3 Anglo-Saxon Debate

"Anglo-Saxon accounting" is an approach to financial accounting and reporting that is common to the UK and Ireland, the USA and other English-speaking countries including Canada, Australia, and New Zealand. (David, Simon, 2000)

In the US, there has been interesting controversies about the NPO accounting, represented by Anthony (1980 and 1989) and Herzlinger and Sherman (1980). Later, in the UK, Johns (1982) has continued the debate.

(a) Anthony’s Argumentation (1980)

Anthony points out that there are two worlds of accounting in the US after 1920s: one accounting world for business organizations and another accounting world for NPOs. Before that, “nonbusiness accounting was approximately the same as business accounting”. (Anthony, 1980, p.84) The reasons for the emergence of the accounting world for NPOs are as follows:

“First, NPOs, by definition, do not exist to earn a profit and it is therefore argued that they should not use business accounting principles, which are focused on the measurement of profitability. Second, managers of NPOs must adhere to restrictions on spending – either legal, such as those set forth in the approved budget of a governmental unit, or other limitations specified by donors or grantors – and it is argued that the purpose of accounting should therefore be to ensure compliance with these restrictions.” (Anthony, 1980, p.86)

In his view, the basic purpose of NPOs is to provide services, so their success should be measured by how much services they provide with the resources available, which is impractical in most NPOs. However, Anthony does not agree that the reasons are sufficient for the differences in the two accounting worlds:

“Expenses in a NPOs are essentially the same as those in a business; in both cases, they represent the resources used in an accounting period, that is the material, labor, and other services consumed in that period. Thus the difference in the meaning of the operating statement relates solely to revenues.”

“Thus a business and a nonbusiness operating statement can convey the same message: the extent to which the organization has maintained its capital through operations. Maintenance of capital is the most important single peace of information about nonbusiness operations. It is also important for business, but in a business the bottom line conveys an additional message – how well the organization attained its objective of earning profits.”(Anthony, 1980, p.87-88)

According to Anthony, the special accounting problem for NPOs is contributed capital, the essential nature of such funds is that the principal must be maintained intact, leaving only the earnings on the principal available for operating purposes. The contributed capital that is intended to benefit future periods must be separated from revenues which relates to current period.

In summary, Anthony concludes:

"NPOs differ from business organizations in that their objective is something other than earning a profit. Both, however, must maintain their capital through operations if they are to continue as sound organizations. An operating statement, prepared according to a common set of standards, reports how well any organization has maintained its capital through operations…

Nonbusiness capital contributions must be excluded from revenues on the operating statement and must be separately disclosed on the balance sheet and funds flow statement…With the exception of the capital contributions, nonbusiness accounting should be essentially the same as business accounting." (Anthony, 1980, p.92-93)

(b) Herzlinger and Sherman's Argumentation (1980)

Herzlinger and Sherman(1980) disagree with Anthony(1980), arguing that NPOs and business organizations are two different accounting worlds.

"1. Nonprofit enterprises have financial structures that are different from those of business.

2. Nonprofit's objectives differ from those of for-profit organizations to such a degree that similar formats would be misleading and would misdirect those evaluating the financial management of nonprofits.

3. Weakness in accounting controls, rather than in nonprofit accounting principles, have contributed to the difficulties that have plagued these nonprofit institutions.

4. Those who manage and deal with nonprofit institutions should have greater

familiarity with the unique requirements of nonprofit financial structures and accounting practices. They should not rely on familiarity with business financial accounting and administration.” (Herzlinger and Sherman, 1980, p.95)

In their view, fund accounting should be applied for NPOs:

“Fund accounting systems were devised to help trustees fulfill their legal obligation to use each of the institution’s various funds according to its guidelines. While business, of course, earn most of their operating revenues from the sale of their goods or services, nonprofits must rely on nonrevenue sources, such as gift, endowment income, and donated services and goods. Moreover … revenue sources frequently have constraints placed on them.” (Herzlinger and Sherman, 1980, p.97)

Furthermore, Herzlinger and Sherman(1980) recommend strongly to include budgetary accounting in NPOs:

“For nonprofit organizations, therefore, traditional corporate reporting is almost meaningless. How, then, should their performance be measured? By comparing actual performance with that intended in the budget… The funds represent external restrictions on the use of resources, while the budget represents legislatively mandated restrictions on the distribution of monies.”

“Nonprofit enterprises have a more basic need for this kind of budgetary information.

Profit is an inappropriate measure for these organizations. Existing to benefit society as whole or particular groups in it, they are by definition not for profit. The appropriate measure of their performance is the level of the benefits achieved, not revenues. But the ability to measure that level is obviously quite limited.” (Herzlinger and Sherman, 1980, p.102-103)

In summary, Herzlinger and Sherman coclude:

“Fund accounting was developed to present fairly the financial transactions unique to nonprofit organizations. The problem of the complexity of their accounting statements should be resolved not by simplification but by better education of users about the meaning and purpose of the components of fund accounting statement and by greater accessibility to these statements.

The weakness of nonprofit accounting would be more fruitfully addressed by resolving the problems in nomenclature and quality of accounting information than by converting fund accounting to simpler (but increasingly complex) for-profit standards." (Herzlinger and Sherman, 1980, p.104)

(c) Jones' Argumentation (1982)

Jones (1982) tries to suggest a way of thinking about financial reporting models which can be applied to NPOs. Following current opinion within Anglo – Saxon literature, double entry bookkeeping is used without any discussion:

"If we adopt the axiom that double-entry bookkeeping is the foundation for financial reporting, in the context of an organization with a single, self-contained set of accounts, the financial reporting problem is to decide which debits and credits should be reported in the balance sheet and which in the operating statement. There are several reasons for financial reporting taking this form, ranging from the trivial, because we conventionally report in this way, to the seemingly unattainable to produce an objective measure of performance." (Jones, 1982, p.287)

According to Jones, most discussion about business and nonbusiness accounting has focused on their different objectives: business organizations pursue profits, while NPOs are not profit oriented.

In order to examine the performance at the organizational level, the boundaries for the financial report should be defined precisely. Jones suggests that the use of fund accounting would be of interest for all types of organizations, business as well as nonbusiness.

"(A fund is defined as an) independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves and equities which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations." (Jones, 1982, p.289-290)

In summary, Jones suggests a way of thinking about financial reporting models which can potentially be applied to all organizations, business and nonbusiness, which is to use 'fund' as the reporting entity, and even for NPOs, they should also specify the unit of measurement, the valuation model and the concept of capital maintenance.

4.4 Broadening the Debate

In the Anglo-Saxon literature, there has been a debate over commercial accounting and fund accounting, and which of them should be used for NPOs. In Monsen (2008)'s view, cameral accounting is advantageous to any of them.

Cameral accounting was developed in the sixteenth century in some continental European German-speaking countries to increase control of public money, including administrative cameralistics and enterprise cameralistics.

Monsen points out, cameral accounting has some advantages over commercial accounting and fund accounting for use in NPOs.

First, cameral accounting uses single-entry bookkeeping, while commercial accounting and fund accounting use double-entry bookkeeping, and single–entry bookkeeping is more flexible than double-entry bookkeeping, because when using single-entry bookkeeping, the number of entries varies depending on the accounting information; when using double-entry bookkeeping, there is always debit and credit with the same amount in two accounts. As a result, cameral accounting is easier to adapt to new reporting requirements and changing environment.

Second, cameral accounting has been specially developed for money management, budgetary control and payment control, which are the most important objectives of NPOs.

4.5 Summary

This chapter started by an overview of accounting for NPOs; then followed a review of the Anglo-Saxon debate about which accounting model should be used for NPOs, the focus has been on commercial accounting and fund accounting; finally, the advantages of cameral accounting were illustrated to broaden the debate, which offered another option for NPOs.

Chapter 5 Empirical Study: A Case of British Red Cross

5.1 International Red Cross and Red Crescent Movement

The International Red Cross and Red Crescent Movement is an international humanitarian movement with approximately 97 million volunteers and 12,000 full time staff members worldwide. The purpose of the Movement is to protect human life and health, to ensure respect for the human being, without any discrimination based on nationality, race, religious beliefs, class or political opinions.

(a) Principles

In the official statutes of the Movement, there are seven basic principles:

> Humanity

The International Red Cross and Red Crescent Movement, born of a desire to bring assistance without discrimination to the wounded on the battlefield, endeavors, in its international and national capacity, to prevent and alleviate human suffering wherever it may be found. It promotes mutual understanding, friendship, co-operation and lasting peace amongst all peoples.

> Impartiality

It makes no discrimination as to nationality, race, religious beliefs, class or political opinions. It endeavors to relieve the suffering of individuals, being guided solely by their needs, and to give priority to the most urgent cases of distress.

> Neutrality

In order to continue to enjoy the confidence of all, the Movement may not take sides in hostilities or engage at any time in controversies of a political, racial, religious or ideological nature.

> Independence

The Movement is independent. The National Societies, whilst auxiliaries in the humanitarian services of their governments and subject to laws of their respective countries, must always maintain their autonomy so that they may be able at all times to act in accordance with the principles of the Movement.

> Voluntary service

It is the voluntary relief movement not prompted in any manner by desire for gain.

> Unity

There can only be one Red Cross or Red Crescent Society in any one country. It must be open to all. It must carry on its humanitarian work throughout its territory.

> University

The International Red Cross and Red Crescent Movement, in which all Societies have equal status and share equal responsibilities and duties in helping each other, is worldwide.

(b) Organizations

The International Committee of the Red Cross (ICRC) together with The International Federation of Red Cross and Red Crescent Societies (IFRC) and National Red Cross and Red Crescent Societies make up the International Red Cross and Red Crescent Movement. They are legally independent from each other, but are united within the Movement through common basic principles, objectives, symbols, statutes and governing organs.

The International Committee of the Red Cross (ICRC) is a private humanitarian institution founded in 1863 in Geneva, Switzerland by Henry Dunant. Its 25-member committee has a unique authority under international humanitarian law to protect the life and dignity of the victims of international and internal armed conflicts.

The International Federation of Red Cross and Red Crescent Societies (IFRC), founded in 1919 and based in Geneva, Switzerland, closely coordinates activities between the 186 National Red Cross and Red Crescent Societies within the Movement. On an international level, the Federation leads and organizes the National Societies in large-scale emergencies.

National Red Cross and Red Crescent Societies exist in nearly every country in the world. Currently 186 National Societies are recognized by the ICRC and admitted as full members of the Federation. Each entity works in its home country according to the principles of international humanitarian law and the statues of the International Movement. Depending on their specific circumstances and capacities, National Societies can take on additional humanitarian tasks, and they are tightly linked to the respective national health care system by providing emergency medical services in many countries.

(c) Funding and Financial Matters

ICRC

The main parts of the budget of ICRC come from Switzerland and in its capacity as the depository state of the Geneva Conventions, from national Red Cross Societies, the signatory states of the Geneva Conventions, and from international organizations like the European Union. All payments to the ICRC are voluntary and are received as donations based on two types of appeals issued by the committee: an annual Headquarter Appeal to cover its internal costs and Emergency Appeals for its individual missions.

IFRC

The main parts of the budget of the Federation are funded by contributions from the national societies which are members of the Federation and through revenues from its investments. The exact amount of contributions from each member society is established by the Finance Commission and approved by the General Assembly. Any additional funding, especially for unforeseen expenses for relief assistance mission, is raised by appeals published by the Federation and comes from voluntary donations by national societies, governments, other organization, corporations, and individuals.

(d) Statement of Compliance

> ICRC and IFRC

The consolidated financial statements have been prepared in accordance with and comply with International Financial Reporting Standards (IFRS) as adopted by the International Accounting Standards Board (IASB) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) of the IASB and are presented in accordance with their Financial Regulations.

Currently, IFRS do not contain specific guidance for NPOs concerning the accounting treatment and the presentation of financial statements. Where IFRS is silent or does not give guidance on how to treat transactions specific to the NPOs, accounting policies have been based on the general principles of IFRS, as detailed in the IASB Framework for the Preparation and Presentation of Financial Statements.

> National Societies

Most of the National Societies apply their own accounting standards, some examples are showed in Table 2.1.

Table 2.1 Accounting Standards for National Red Cross and Red Crescent Societies

Country	Accounting Standards
USA	USA GAAP
Canada	Canadian GAAP
Australia	Australian Equivalents to IFRS
UK	UK General Accepted Accounting Practice
Norway	Norwegian Accounting ACT
Singapore	Singapore Financial Reporting Standards
Hong Kong	HK Financial Reporting Standards

5.2 National Red Cross and Red Crescent Societies

(a) Official Recognition of a National Society

National Red Cross and Red Crescent Societies exist in 186 countries in the world. After official recognition by the ICRC according to the statutes of the Movement, a national society is admitted as a member to the International Federation of Red Cross and Red Crescent societies. (Appendix 1)

(b) Activities of National Societies on a National and International Stage

Despite formal independence regarding its organizational structure and work, each national society is still bound by the laws of its home country. In many countries, national Red Cross and Red Crescent societies enjoy exceptional privileges due to agreements with their governments or specific "Red Cross Laws" granting full independence as required by the International Movement. The duties and responsibilities of a national society as defined by International Humanitarian Law and the statutes of the Movement include humanitarian aid in armed conflicts and emergency crises such as natural disasters. Depending on their respective human, technical, financial, and organizational resources, many national societies take on additional humanitarian tasks within their home countries such as Blood donation services or acting as civilian Emergency Medical Service (EMS) providers. The ICRC and the International Federation cooperate with the national societies in their international missions, especially with human, material, and financial resources and organizing on-site logistics.

5.3 British Red Cross

(a) Objectives

The legal objectives of the British Red Cross, as laid out in its revised Royal Charter, are to provide assistance to victim of armed conflicts and to work for the improvement of health, the prevention of disease and the prevention and alleviation of human suffering in the UK and throughout the world. The British Red Cross is required at all times to act in accordance with the fundamental principles of the International Red Cross and Red Crescent Movement.

(b) Status

The British Red Cross was founded in 1870 and incorporated by Royal Charter in 1908, and its governing instruments compromise the revised charter, the standing orders and other policies agreed from time to time by its governing body, the board of trustees.

The British Red Cross is a prominent member in the International Red Cross and Red Crescent Movement, with volunteers and staff contributing to a number of initiatives in the IFRC, ICRC, and other National Societies.

(c) Volunteers' Contributions

During 2008, the average number of British Red Cross volunteers was 27,349 and the average number of staff was 2,755. Volunteers provide services in emergency response and short-term crisis. They also work with refugees and asylum seekers.

The financial statements do not incorporate any value attributable to the number of voluntary hours devoted to the service of the British Red Cross by its membership. Based on national average hourly earnings rates, duly weighted to reflect the membership, the work undertaken was about ￡42.5 million for the year ended 31 December 2008.

(d) Trustees' Responsibilities

The trustees prepare consolidated financial statements for each financial year. These give a true and fair view of the state of the British Red Cross and of the annual results. In preparing the financial statements, the trustees have:

> selected suitable accounting policies and applied them consistently

> made judgments and estimates that are reasonable and prudent

> followed applicable accounting standards without any material departures

> prepared the accounts on a going concern basis.

Financial statements are published on the organization's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The trustees' responsibilities also extend to the ongoing integrity of the financial statements contained therein.

In addition, the board of trustees has given regard to the legislative and regulatory requirements for disclosing how its charitable objectives have provided benefit to the public.

5.4 Accounting for British Red Cross

(a) Fund Accounting

Fund accounting is applied (Appendix 6: Notes 1, 1(b)):

General unrestricted funds are available for use at the discretion of the trustees in furtherance of the general charitable objectives. A pension reserve is included within unrestricted funds to meet the pension deficit.

Designated funds are those unrestricted funds transferred from the general fund for particular purposes or projects at the discretion of trustees. The creation of designated funds is approved by the trustees before the year end to meet specific future plans. Amendments to estimates used in calculating the level of designated funds are made up to the date of approval of the accounts.

Restricted funds are donated for either a particular area or purpose, the use of which is restricted to that area or purpose. Such donations are principally for international purposes.

(b) Regulations

Scope and basis of the financial statements are as follows:

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of investments at market value, and are in accordance with the Accounting and Reporting by Charities: Statement of Recommended Practice (Revised 2005) ("the SORP", Appendix 2) and applicable accounting standards in the United Kingdom. (Appendix 6: Notes 1, 1(a))

(c) Annual Reports

The annual reports compromise: Consolidated statement of financial activities, consolidated balance sheet and consolidated cash flow statement. (Appendix 3, 4, 5)

Chapter 6 Analysis

6.1 Cash Basis Accounting versus Accrual Basis Accounting

(a) Theory Level

There are two bases for keeping records: the cash basis and the accrual basis. There are also combined and modified accounting bases in practice. They will be explained below.

(1) Cash Basis Accounting

Cash basis accounting is a system that records a transaction when cash has been received or expended. The principal advantage is its simpler nature, and even non-professionals can understand the financial information easily. The problem is that, in many instances, the cash basis does not present accurately enough the financial picture of the organization when there are substantial unpaid bills or uncollected income, which will materially distort the financial statements.

As for NPOs, contributions are the principal sources of income, which in most cases are not legally enforceable; and some donations are hard to evaluate until sold. As a result, cash basis accounting is considered more conservative.

(2) Accrual Basis Accounting

Accrual basis accounting is a system that records income when earned and expenses when incurred. (Richard and Ann, 2008) There are two requirements to recognize the transaction: When the amount is quantified and there is certainty to happen, which can be explained further, when the economic resources have exchanged and there is right or obligation to collect or pay money. The accrual basis accounting is finely detailed and comprehensible to professionals, and it applies the matching principle, which shows a real picture of the financial condition. However, its sophistication also adds difficulty to apply and understand.

(3) Combination of Cash and Accrual Accounting

One practical way to avoid the complexities of accrual basis accounting, and still have meaningful financial statement annually, is to keep the records on a cash basis and make the necessary adjustments to record the accruals at the end of the year.

(4) Modified Cash Basis

Some NPOs use a modified cash basis system of accounting, which means certain transactions will be recorded on an accrual basis while others on a cash basis. Usually, on a modified cash basis, all unpaid bills will be recorded on an accrual basis, while uncollected income on a cash basis, which is also to be conservative.

(b) Rule Level

According to the SORP, which governs the economic and financial reporting of NPOs in the UK, all charities with an annual gross income of ￡100,000 and above are required to keep their accounts on an accrual basis, other charities below this figure may keep their accounts on a cash basis, and this also applies under the Company Act if they are incorporated. (David, Robert, 2003) Thus due to its large scale of financial activities, British Red Cross should apply accrual basis accounting in accordance to the regulation requirement.

(c) Practice Level

For British Red Cross, the accounting basis varies to conditions:

Incoming resources (See Appendix 6: Notes 1, 1(c))

All income is accounted for when the British Red Cross has entitlement to the funds, the amount can be quantified and there is certainty of receipt. Where income is received in advance of providing goods and/or services, it is deferred until the British Red Cross becomes entitled to that income. For legacies, entitlement is taken as the earlier of the date on which the estate is finalized, or when proceeds are received.

Entitlement for donations is deemed to be taken when the money is received. Gifts donated for resale are included as income when they are sold. Donated assets are included at the value to the British Red Cross where this can be quantified. Donated services, including work by volunteers, are not included within the financial statements.

Resources expended (See Appendix 6: Notes 1, 1(d))

All expenditure is accounted for on an accrual basis.

(d) Analysis

It seems British Red Cross adopt a modified cash basis accounting, since some categories of incoming resources are recorded on cash basis while all expenditure on accrual basis.

According to Anthony (1980), "Expenses in a nonbusiness organization are essentially the same as those in a business…Thus the difference in the meaning of the operating statement relates solely to revenues." That is the reason British Red Cross has different accounting basis for some revenues. Cash basis reduces the risk of uncollected contributions, which are voluntary and without legal guarantees. As for donated assets and gifts, they are only recorded when the value is certain.

We can understand in this way, British Red Cross still follows the requirement of SORP, which means on an accrual basis accounting. The exceptions for some revenues are because they are not quantified or there is no certainty of receipts, as soon as the two conditions are met, the revenues are recognized, which fulfills the definition of accrual basis accounting.

The additional problem here is the unrecognized donated services, which are also important invisible revenues on the financial statements, since they represent huge opportunity costs. The donated services are difficult to record, because they are various and no standard to evaluate. Furthermore, they are expensed instantly when produced, even if they show up in the statement of financial activities, the net effect is zero, and they have nothing to do with cash flows and assets. British Red Cross records the donated services by the total hours and estimated amounts in the trustees' report in an independent paragraph.

6.2 Money Accounts versus Profitability Accounts

(a) Practice Level

When we turn to the official accounts of British Red Cross, it is easy to find they are basically profitability accounts. Even with some accounts unique to charities, in essence it applies accrual basis accounting, which has no material differences from business organizations. For further analysis of its financial transactions and accounting treatments, BRC's double-entry bookkeeping is deduced (Appendix 11), which also helps prepare the alternative money accounts later.

In order to report the money development, an overview of funds is presented in the notes to the financial statements, as exhibit 6.1 shows.

Exhibit 6.1 Statement of funds for the year ended 31 December 2008
(Appendix 7: Notes 9)

￡000	Total funds
Balance 1 January 2008	150,282
Income	243,548
Expenditure	(239,755)
Investment gains	(13,770)
Actuarial gains on benefit pension schemes	(289)
Balance 31December 2008	140,016

However, this statement of funds could not fulfill the requirements of money accounts, because the "funds" here is just like "equity" in commercial accounting. The accounting items provide more information than "money": "Expenditure" includes depreciation; "Investment gains" is the net effect of loss of fixed investments and gain of current investment. Meanwhile, there is some "money" related information not mentioned here. The reason of the whole blurred picture is the misconception between "money" and "funds", "funds" and "equity", in the root, the mentally convergence of charity accounting and commercial accounting.

(b) Money Accounts

As an alternative to the official profitability accounts, "money accounts" of British Red Cross are presented below, consisting of "money status accounts" and "money result accounts". (Adapted from Monsen (2009))

(1) Money Status Accounts

The money status accounts of British Red Cross for the year ended 31 December 2008 are presented in Exhibit 6.2. The accounts are divided into the following three main groups: current assets, short-term debts and working capital, which is the difference between the first two. The change in money status is referred to as "money result" or "working capital change", which also appears in the money result accounts. In the supplementary accounts, other long-term assets and liabilities are showed to reflect the complete financial situation of British Red Cross.

Exhibit 6.2 Money Status Accounts for the year ended 31 December 2008

￡000	2008 Total
Current assets	
Stocks	2,691
Debtors	19,356
Current Investments	18,731
Cash at bank and in hand	4,668
Total current assets	45,446
Short – term debt	
Amounts falling due within one year	(20,954)
Net current assets	24,492

Working Capital at 1 January	44,932
Money result	**(20,440)**
Working capital at 31 December	24,492

Supplementary Accounts

Fixed assets	
Tangible assets	68,684
Investments	53,339
Defined benefit pension scheme deficit	(649)
Amounts falling due in more than one year	(275)
Provision for liabilities and charges	(5,575)

(2)Money Result Accounts

The money result accounts of British Red Cross are presented in Exhibit 6.3, where the development of the revenues and expenditures during the year 2008 is reported. Here is the direct method of preparing the money result accounts, the incoming sources are divided according to three types of activities: operating, investing and financing.

Exhibit 6.3 Money Result Accounts
for the year ended 31 December 2008

￡000	2008 Total
Operating activities	
Revenues:	243,347
Expenditures:	234,693
Net operating activities	*8,654*
Investment activities	
Sales of investments	22,349
Purchase of investments	(24,567)
Sales of tangible fixed assets	914
Purchase of tangible fixed assets	(13,964)
Net investment gains in the year for Current investments	505
Net charges for defined benefit pension scheme	(382)
Net investment activities	*(15,145)*
Financial activities	
Decrease provision for liabilities and charges	(13,949)
Net financial activities	*(13,949)*
Money result (A+B+C)	**(20,440)**

(c) Financial Statements

Trustees must receive necessary financial information to ensure the proper stewardship of the organizational funds, in as comprehensive yet succinct form as possible. The comparisons between money accounts and the financial statements in the trustees' report are provided as follows.

(1) Money Status Accounts (Exhibit 6.2) versus Balance Sheet (Appendix 4)

The accounts are almost the same, only differing in the structure:

Money Status Accounts includes two groups: working capital and supplementary accounts. It is money focused, while also provides the other long-term financial information. The picture and the purpose are straightforward.

Balance Sheet appears the same as the commercial organizations. "Accumulated funds" is equivalent to "equity", there is no actual adaption to NPOs. For commercial organizations, equity is the concern, since their purpose is to maximize the shareholders' wealth, while for NPOs, they are in pursuit of public benefit, the information of "Accumulated funds" here does not fulfill the trustees' purpose.

(2) Money Result Accounts (Exhibit 6.3) versus Cash Flow Statement (Appendix 5)

Money Result Accounts uses the direct method, specifying incoming sources from operating, investing and financing activities. Just like Money Status Account, the picture and purpose are clear; in addition, "money result" is the linkage between the two statements.

Cash Flow Statement used the indirect method, which is technical and hard to follow for non-professionals, not as informative as Money Result Accounts. And the final item "Net short-term funds less borrowing" is weird, which equals "Cash at bank and in hand" plus "Current asset investments" minus Loan due after one year. The term only appears here and hard to make sense.

6.3 Fund Accounting

(a) Theory Level

Fund accounting is used for NPOs to record restricted funds separately. The double-entry bookkeeping method of fund accounting is applied to prepare money accounts and financial statements.

(b) Rule Level

Fund accounting is applied by British Red Cross, and there are three funds kept separately: general unrestricted funds, designated funds, and restricted funds. (Appendix 6: Notes 1, 1(b))

(c) Practice Level

In the Consolidated Statement of Financial Activities (Appendix 3) and Consolidated Balance Sheet (Appendix 4), detailed information for the subdivisions of "unrestricted" and "restricted" funds is disclosed, which combines the "general funds" and "designated funds" into "unrestricted" group. In the Consolidated Cash Flow Statement (Appendix 5), only total amount is showed. In additional Statement of Funds (Appendix 7, Notes 9), there is further information of the developments of the three funds. With all the above signs of fund accounting, it is still impossible to deduce its special double-entry bookkeeping method due to incomplete information in the trustees' report. We can only analyze the transactions by the merchant's double –entry bookkeeping. (Appendix 11) British Red Cross probably keeps detailed internal bookkeeping records on a fund accounting basis to comply with donor-imposed restrictions. Rather, for reporting purposes, the organization combines all the activity for the year in a meaningful manner, intending to improve the reader's understanding of the overall financial picture.

Another reason to add the complexity is that as mentioned before, here the "fund" is used for profitability accounts, not money accounts, which is a misconception of fund accounting.

In summary, British Red Cross applied fund accounting in its own way, which does not follow strictly with the theory and misses some detailed information, thus makes the readers confused. In all the participants of The International Red Cross and Red Crescent Movement, British Red Cross is the only one to specify itself as an adopter of fund accounting, which is a pioneer, even though not successful.

6.4 Treatment of Tangible Assets

(a) Theory Level

Tangible assets and their depreciations may present accounting problems for NPOs. There are different practices depending on whether to record and report tangible assets and depreciation. The two basic alternative approaches are as follows:

> Immediate write-off approach, where assets are written off as purchased, in the statement of financial activities. This is simple and popular among small organizations.

> Capitalization approach, where the full cost of the asst is capitalized and recorded in the Balance Sheet to depreciate. This is probably appropriate for larger organizations if they choose accrual accounting basis and want to match revenues and costs to determine cost of services being rendered.

(b) Rule Level

Tangible fixed assets and depreciation (See Appendix 6: Notes 1, 1(e)))

All tangible fixed assets costing more than ￡1,000 are capitalized and included at cost, including any incidental expenses of acquisition and irrecoverable VAT. Depreciation is provided on a straight-line basis over their useful economic lives.

(c) Practice Level

The presentation of tangible assets is clear in the Balance Sheet of British Red Cross for the year ended 31 December 2008, while the presentation of depreciation in the financial statements is vague. In Cash Flow Statement, which is prepared by indirect way, there is an adjustment of “depreciation charge”, which demonstrates that “Net income resources” is “depreciation” included. When refer to Statement of Financial Activities, we could not find “depreciation”, the only explanation is that depreciation has been allocated to different costs already. Then more problems come: What are the exact costs of different activities? How is depreciation allocated to different activities? For financial accounting, accurate numbers are expected, while for management accounting, technical methods are applied to get more related costs information. To apply the management accounting thinking in financial reporting is confusing. Here the depreciation is invisible in the Statement of Financial Activities and there is no further information to explain how it disappears and what its real effects are, which distorts the overall financial picture and makes the further analysis difficult. Without a professional background and thorough understanding, the readers would probably ignore the depreciation.

6.5 Cash Flow Thinking

(a) Theory Level

Cash flow thinking is important for all the organizations, especially for NPOs. Here are several reasons why things are different:

First, while businesses are created by markets, NPOs are often created by market failure. (Richard, Ann, 2008) When there is no incentive for markets to provide some services, a third party is needed.

Second, NPOs are exempted from most of the taxes due to their contribution to public benefits. While commercial organizations have to apply accrual accounting partly for tax requirement, NPOs do not have this consideration.

Third, NPOs raise money mostly from contributions, and use money with restrictions for social purpose, while commercial organizations sell equity to investors in the form of stocks, bonds, partnerships, and venture arrangements, they have a great deal of flexibility to use the money to make profits and distribute earnings to investors.

As a result, the fiscal cycle for NPOs is only about cash flow, which makes cash flow thinking uniquely emphasized for NPOs.

(b) Practice Level

For British Red Cross, the accrual basis and profitability accounts are applied, which are not appropriate for cash flow thinking. Instead, cash basis and money accounts are advisable.

6.6 Budgetary Control

(a) Theory Level

Budget is a forward financial plan for a prescribed period, usually expressed in financial terms, against which actual performance may be monitored, and it plays a particular important role in NPOs. One reason is that NPOs has to plan and control their financial activities carefully to survive and to provide more efficient services. Another reason is that some contributors request a general operating budget, as well as special project budget when there are restrictions on the funds. NPOs have the incentive to show the funders how the projects will be implemented and managed. Good budgets reflect carefully planned projects.

There are some steps to prepare budgets for charities:

> All proposed projects should follow their objectives, especially when funds with restrictions are being used.
> Priorities of the projects should be reevaluated constantly due to the updated information.
> The costs of continuing and new projects should be estimated carefully.
> All sources and levels of expected income should be predicted realistically, with economic and other factors into consideration.
> The total expected income should be compared to the estimated costs achieving the objectives. The process to reconcile income and costs is a series of adjustments to plans with priorities as reference. .
> The final proposed budget should be approved by the trustees.

(b) Practice Level

In the trustees' report of British Red Cross, there is no budgetary information, which seems only for internal use. In order to attract funders, we strongly recommend including budget in the report. Budget is based on cash flow thinking, since it is a process to translate plans into monetary terms. Budgetary control is to monitor actual performance by comparing it with the plan and responding appropriately to differences between them. To make budget more comparable with accounting figures, cash basis and money accounts are also more suitable. Furthermore, budget is built up by different funds, which requires fund accounting as well.

Chapter 7 Closing

7.1 Conclusion

A case study of British Red Cross is undertaken by analyzing its bookkeeping and financial statements. Fund accounting is claimed to be used, while actually profitability accounts are applied. The self-contradiction has blurred the financial picture. As a NPO, BRC is smart to choose fund accounting to specify the usage of restricted funds, which should be accompanied with money accounts since BRC is not profit-oriented. Then money status accounts and money result accounts are prepared as alternatives to official accounts, and they are clearer and simpler for readers to acquire an overview of the actual development of the revenues and expenditures. What is more, fund accounting and money accounts could well realize cash flow thinking and budgetary control, which are important for NPOs.

BRC is a good model of NPOs, it is chosen for the reasons as follows:

> Charity accounting is an important part of NPO accounting.

> UK has a long history of accounting development for NPOs.

> BRC is the only one to specify itself as an adopter of fund accounting in the financial report.

As a result, the analysis and conclusions in the case study of BRC could be helpful to improve the financial reports of the other NPOs.

7.2 Trends in Accounting for NPOs

(a) The Whole Organization as a Reporting Entity

The most important trend is to report the financial information of the organization as a whole, because readers are willing to see a big picture which is concise and easy to understand, for more details, they could always refer to notes. As a result, there will be a requirement to combine the financial reports of affiliated organizations into the parent organizations. What is more, the individual funds making up the entity will not be separately shown in each financial statement in case of confusion. (Malvern, et al., 1995) Fund accounting is still advisable for NPOs, but it will only be used for bookkeeping, not for public reporting purposes.

(b) Convergence of Accounting Regulations for All NPOs

There has been unprecedented convergence of accounting regulations all over the world during the past years, because accounting tends to be a standard language to measure financial performance for all organizations in order to provide a better comparison and understanding. As for NPOs, they are expected to apply only a single set of basic underlying accounting principles and reporting practices, which means there will be great uniformity in the basic financial information disclosed in the statements, however, the reporting formats could vary from organization to organization.

(c) Divergence from Commercial Accounting

On the other hand, NPOs are different from commercial organizations in many ways, and the essence is that they are not profit-oriented, so they should have their own accounting regulations.

7.3 Further Practice

(a) Historic Accounting Figures

Accounting figures for the past three years should be provided in favor of a dynamic analysis of the financial information. The current data makes more sense as compared to historic data. The development of NPOs presents a vivid picture then.

(b) Budgetary Figures

Budgetary Figures could also be an important part of the financial report. The actual differences to original budget need reasonable explanations, which increases the inner control of NPOs. The future budget reveals the next plan, which becomes a benchmark for funds raising and expenditures spending.

(c) Verbal Comments

Verbal comments should be given to disclose more financial related information, for example, to explain about the historic, current and budgeting accounting figures.

(d) Key Ratios

Key ratios could be helpful to give readers a general impression of the financial conditions of NPOs, while graphic illustrations are advisable.

7.4 Further Research

In this thesis, accounting for NPOs is illustrated with a case study of British Red Cross. Due to the limitation of the uniqueness of the sample, the analysis and conclusions could be improved by comparing it with other Red Cross organizations, and even with other types of NPOs.

As for the research methodology, only the analytical perspective is applied to explore the accounting figures in this thesis, while the budgeting figures could also be added into analysis from the system perspective, what is more, interviews of financial staff, auditors and users could be made from the individual perspective. The case study has a lot of room to be continued and generalized analytically further.

In addition, among the three accounting models mentioned, commercial accounting and fund accounting have become the research focus, while cameral accounting is not applied in the analysis part. Actually, cameral accounting was developed for government, which has many advantages over the other two and could be an interesting and promising topic in the further research.

Appendix 1 Official Recognition of a National Society

In order to be recognized by the ICRC as a member to the International Federation of Red Cross and Red Crescent societies, in terms of Article 5, paragraph 2 b) according to statutes of the Movement, the National Society shall meet the following conditions:

1. Be constituted on the territory of an independent State where the Geneva Convention for the Amelioration of the Condition of the Wounded and Sick in Armed Forces in the Field is in force.
2. Be the only National Red Cross or Red Crescent Society of the said State and be directed by a central body which shall alone be competent to represent it in its dealings with other components of the Movement.
3. Be duly recognized by the legal government of its country on the basis of the Geneva Conventions and of the national legislation as a voluntary aid society, auxiliary to the public authorities in the humanitarian field.
4. Have an autonomous status which allows it to operate in conformity with the Fundamental Principles of the Movement.
5. Use the name and emblem of the Red Cross or Red Crescent in conformity with the Geneva Conventions.
6. Be so organized as to be able to fulfill the tasks defined in its own statutes, including the preparation in peace time for its statutory tasks in case of armed conflict.
7. Extend its activities to the entire territory of the State.
8. Recruit its voluntary members and its staff without consideration of race, sex, class, religion or political opinions.
9. Adhere to the present Statutes, share in the fellowship which unites the components of the Movement and co-operate with them.
10. Respect the Fundamental Principles of the Movement and be guided in its work by the principles of international humanitarian law.

Appendix 2 SORP

Today, the economic and financial reporting of NPOs in the UK is governed by Accounting and Reporting by Charities: Statement of Recommended Practice" (SORP), which has been updated continuously since 1988 by adjusting to adapt the model of reporting to the real needs of NPOs and to bring it into line with all the different accounting standards and financial institutions present in the UK, which is also a result of profound dialogue between the members of the Charity Commission and the Accounting Standards Board.

The purpose of the adoption of SORP is to give a clear and transparent representation of the activities and financial position of NPOs which have an annual income exceeding ￡100,000, and to have the possibility to compare the results and activities with the national territory. (Claudio, 2008)

The SORP Annual Report must include:

> Reference and administrative details of the charity, its trustees and advisors: A series of specific information needed to identify not only the NPOs but also its directors and any other independent or dependent auditors.
> Structure, governance and management: The NPOs must not only be clear in its internal organization but also motivate the choice of legal form and the internal rules on decisions and voting.
> Objectives and activities: The institution must highlight its objectives, role and by what methods it pursues its activities.
> Achievements and performance: The activities must also be illustrated through performance indicator or sectoral comparisons, to highlight the reader of the role and the importance of being a NPO. The entity must also expose in this section the fundraising activities undertaken and the results obtained from these campaigns.

> Financial review: The financial position of the entity should be presented and the reserves and the changes that occurred over the previous period should be explained, giving appropriate reasons for such variation.
> Plans for future periods: The objectives and plans for the next accounting year shall be presented.
> Statement of financial activities: This document, purely accounting, seeks to highlight how the company has used its resources in relation to the stated objectives.
> Balance sheet: This document allows the entity to disclose its assts and liabilities, highlighting the consistency of the assets, with intangible assets as part of the equity.
> Cash flow statement: This document supplements the statement of financial activities, giving an appropriate representation of cash flows and highlighting the origin and use.
> Notes on the accounts: The rules followed in the preparation of the accounts, the accounting standards used and how they were interpreted should be highlighted.

The document is then drawn up under the supervision of auditors

Appendix 3 Consolidated statement of financial activities

for the year ended 31 December 2008

	Unrestricted £000	**Restricted** £000	2008 Total £000	2007 Total £000
Incoming resources				
Incoming resources from generated funds				
Voluntary income	65,966	21,389	**87,355**	101,463
Trading activities	22,997	842	**23,839**	22,286
Investment income	1,964	1,384	**3,348**	3,125
Total incoming resources from generated funds	90,927	23,615	**114,542**	126,874
Incoming resource relating to charitable activities				
Emergency response	16,639	56,608	**73,247**	46,085
Short-term crisis care	28,143	531	**28,674**	28,153
Humanitarian action	329	262	**591**	502
Supporting and strengthening the Red Cross Movement	-	25,518	**25,518**	35,736
Total incoming resources from charitable activities	45,111	82,919	**128,030**	110,476
Other incoming resources				
Miscellaneous income	637	138	**775**	829
Net gains/(loss) on disposal of fixed assets	243	(42)	**201**	3,446
Total incoming resources	136,918	106,630	**243,548**	241,625

Consolidated statement of financial activities

for the year ended 31 December 2008

	Unrestricted £000	Restricted £000	2008 Total £000	2007 Total £000
Resources expended				
Costs of generating funds				
Voluntary income	31,010	1,917	**32,927**	22,831
Trading activities	21,954	-	**21,954**	20,842
Investment management costs	25	-	**25**	96
Total resources expended on generating funds	52,989	1,917	**54,906**	43,769
Costs of charitable activities				
Emergency response	30,142	67,959	**98,101**	95,583
Short-term crisis care	43,132	4,591	**47,723**	49,119
Humanitarian action	6,481	939	**7,420**	5,681
Supporting and strengthening the Red Cross Movement	2,962	26,088	**29,050**	37,955
Total resources expended on charitable activities	82,717	99,577	**182,294**	188,338
Governance costs	2,553	2	**2,555**	2,182
Total resources expended	138,259	101,496	**239,755**	234,289
Net incoming resources before transfers	(1,341)	5,134	**3,793**	7,336
Transfers between funds	(332)	332	**-**	-
Net incoming resources before recognized gains and losses	(1,673)	5,466	**3,793**	7,336
(Loss)/gains on investments	(14,103)	333	**(13,770)**	2,553
Actuarial losses on defined benefit pension schemes	(289)	-	**(289)**	(761)
Net movement in funds	(16,065)	5,799	**(10,266)**	9,128
Total funds – 1 January	109,496	40,786	**150,282**	141,154
Total funds – 31 December	93,431	46,585	**140,016**	150,282

All activities related to continuing operations.

Appendix 4 Consolidated balance sheet
for the year ended 31 December 2008

	Unrestricted £000	Restricted £000	2008 Total £000	2007 Total £000
Fixed assets				
Tangible assets	59,954	8,730	**68,684**	60,495
Investments	20,337	33,002	**53,339**	65,396
	80,291	41,732	**122,023**	125,891
Current assets				
Stocks	1,878	813	**2,691**	2,080
Debtors	15,316	4,040	**19,356**	17,247
Investments	12,898	5,833	**18,731**	34,847
Cash at bank and in hand	1,183	3,485	**4,668**	10,382
	31,275	14,171	**45,446**	64,556
Creditors:				
Amounts falling due within one year	(15,859)	(5,095)	**(20,954)**	(19,624)
Net current assets	15,416	9,076	**24,492**	44,932
Total assets less current liabilities	95,707	50,808	**146,515**	170,823
Creditors:				
Amounts falling due in more than one year	-	(275)	**(275)**	(275)
Provision for liabilities and charges	(1,627)	(3,948)	**(5,575)**	(19,524)
Net assets before pension scheme deficit	94,080	46,585	**140,665**	151,024
Defined benefit pension scheme deficit	(649)	-	**(649)**	(742)
Net assets	93,431	46,585	**140,016**	150,282
Represented by:				
Funds excluding pension scheme deficit	94,080	46,585	**140,665**	151,024
Defined benefit pension scheme deficit	(649)	-	**(649)**	(742)
Accumulated funds	93,431	46,585	**140,016**	150,282

Appendix 5 Consolidated cash flow statement

for the year ended 31 December 2008

	2008 Total £000	2007 Total £000
Net cash (outflow) / inflow from operating activities (see below)	**(8,255)**	14,521
Capital expenditure and financial investment	**(14,080)**	(11,355)
	(22,355)	3,186
Decrease in Loans due within one year	**-**	(50)
Cash withdrawn from current asset investments	**16,621**	198
(Decrease)/increase in cash	**(5,714)**	3,334
Reconciliation of net incoming resources to net cash outflow from operating activities		
Net incoming resources	**3,793**	7,336
Depreciation charge	**5,062**	5,358
Surplus on sale of tangible fixed assets	**(201)**	(3,446)
Decrease/(increase) in stocks	**(611)**	2,742
(Increase)/decrease in debtors	**(2,109)**	5,410
Increase in creditors	**142**	7,261
(Decrease) in provisions for liabilities and charges	**(13,949)**	(9,637)
Net charges for defined benefit pension scheme	**(382)**	(503)
Net cash (outflow) / inflow from operating activities	**(8,255)**	14,521
Reconciliation of net funds to movement in short-term funds less borrowing		
(Decrease)/increase in cash in the period	**(5,714)**	3,334
Decrease in loans due within one year	**-**	50
(Decrease) in current asset investments	**(16,621)**	(198)
Changes in net funds resulting from cashflows	**(22,335)**	3,186
Unrealized gains on current asset investments	**505**	1,242
	(21,830)	4,428
Net short-term funds less borrowing at 1 January	**44,954**	40,526
Net short-term funds less borrowing at 31 December	**23,124**	44,954

Appendix 6

Notes 1: Accounting policies

The principal accounting policies, all of which have been applied consistently throughout the year, are set out below:

(a) Scope and basis of the financial statements

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of investments at market value, and are in accordance with the Accounting and Reporting by Charities: Statement of Recommended Practice (Revised 2005) ("the SORP") and applicable accounting standards in the United Kingdom.

(b) Fund accounting

General unrestricted funds are available for use at the discretion of the trustees in furtherance of the general charitable objectives. A pension reserve is included within unrestricted funds to meet the pension deficit.

Designated funds are those unrestricted funds transferred from the general fund for particular purposes or projects at the discretion of trustees. The creation of designated funds is approved by the trustees before the year end to meet specific future plans. Amendments to estimates used in calculating the level of designated funds are made up to the date of approval of the accounts.

Restricted funds are donated for either a particular area or purpose, the use of which is restricted to that area or purpose. Such donations are principally for international purposes.

(c) Incoming resources

All income is accounted for when the British Red Cross has entitlement to the funds, the amount can be quantified and there is certainty of receipt. Where income is received in advance of providing goods and/or services, it is deferred until the British Red Cross becomes entitled to that income. For legacies, entitlement is taken as the earlier of the date on which the estate is finalized, or when proceeds are received. Entitlement for donations is deemed to be taken when the money is received.

Gifts donated for resale are included as income when they are sold. Donated assets are included at the value to the British Red Cross where this can be quantified. Donated services, including work by volunteers, are not included within the financial statements.

(d) Resources expended and basis of allocation of cost

All expenditure is accounted for on an accruals basis.

Direct costs are those specifically related to producing the output of an activity, for example the costs incurred in direct contact with beneficiaries.

Direct support costs are those which, whilst not directly related to producing the output of an activity, are the costs of activities in contact with and supporting the front-line output producers. These costs are likely to be geographically close to the point of delivery, and are allocated directly to the activity supported where possible.

Central support costs are those which provide indirect support to front-line output provision-examples are central finance, human resources and management information services. Support costs not attributable to a single activity have been allocated on a basis consistent with identified cost drivers for that cost category.

Governance costs related to the direct running of the charity, allowing the charity to operate and generate the information required for public accountability. They include the costs of the International Red Cross and Red Crescent Movement, as well as the costs of trustee meetings and internal and external audits.

(e) Tangible fixed assets and depreciation

All tangible fixed assets costing more than £1,000 are capitalized and included at cost, including any incidental expenses of acquisition and irrecoverable VAT. Depreciation is provided on a straight-line basis over their useful economic lives as follows:

Freehold properties	50 years
Leasehold properties	
Shop premises	the shorter of the term of the lease and five years
Other premises	the shorter of the term of the lease and 50 years
Freehold premises improvements	ten years
Leasehold premises improvements	the shorter of the term of the lease and ten years
Vehicles, equipment and furniture	between two and ten years
Fixture and fittings	five years
Computer equipment	between on and three years
Overseas fixed assets	to date of anticipated tsunami project completion
Freehold land	nil

Appendix 7
Notes 9: Statement of funds

	Balance 1 January 2008 £000	Income £000	Expenditure £000	Investment gains £000	Actuarial gains on benefit pension schemes £000	Transfers £000	Balance 31 December 2008 £000
General funds	85,666	136,918	(135,866)	(14,103)	(289)	5,441	**77,767**
Designated funds	23,830	-	(2,393)	-	-	(5,773)	**15,664**
Total unrestricted funds	109,496	136,918	(138,259)	(14,103)	(289)	(332)	**94,431**
Restricted funds							
United Kingdom							
Other UK funds	22,265	7,538	(5,570)	333	-	(621)	**23,945**
Total UK restricted funds	22,265	7,538	(5,570)	333		(621)	**23,945**
International							
Africa	5,134	33,415	(34,773)	-	-	795	**4,571**
America	1,665	2,436	(2,185)	-	-	215	**2,131**
Asia	7,472	19,125	(14,883)	-	-	(376)	**11,338**
Europe	1,161	1,059	(1,703)	-	-	5	**522**
Middle East	276	15,165	(15,383)	-	-	86	**144**
Other	2,813	27,892	(26,999)	-	-	228	**3,934**
Total international restricted funds	18,521	99,092	(95,926)	-	-	953	**22,640**
Total restricted funds	40,786	106,630	(101,496)	333	-	332	**46,585**
Total funds	150,282	243,548	(239,755)	(13,770)	(289)	-	**140,016**

Appendix 8
Notes 10: Tangible assets

Cost	Freehold property £000	Leasehold property £000	Vehicles, equipment and furniture £000	Assets in the course of construction £000	Total £000
At 1 January 2008	38,510	27,264	34,147	8,024	**107,945**
Completion	3,589	1,824	-	(5,413	**-**
Reclassification	(102)	102	-	-	**-**
Additions	1,282	2,656	4,012	6,014	**13,964**
Disposals	(941	(423)	(3,319)	-	**(4,683)**
At 31 December 2008	42,338	31,423	34,840	8,625	**117,226**
Accumulated depreciation					
At 1 January 2008	10,559	7,739	29,152	-	**47,450**
Reclassification	(72)	72	-	-	**-**
Charge for year	1,296	1,385	2,381	-	**5,062**
Disposals	(490)	(238)	(3,242)	-	**(3,970)**
At 31 December 2008	11,293	8,958	28,291	-	**48,542**
Net book value					
At 31 December 2008	31,045	22,465	6,549	8,625	**68,684**
At 31 December 2007	27,951	19,525	4,995	8,024	**60,495**

Appendix 9
Notes 11: Investments

Fixed assets investments	**Total** **£000**
Market value – 1 January	**65,396**
Additions at cost	**24,567**
Disposals at market value	**(22,349)**
Net investment losses in the year	**(14,275)**
Market value – 31 December	**53,339**
Cost – 31 December	**59,478**

Current assets investments	**2008** **£000**	**2007** **£000**
HSBC Sterling Liquidity Fund Class A plc	**4,849**	16,392
Royal Bank of Scotland Global Treasury Funds plc	**10,310**	14,930
Barclays Global Investments Sterling Liquidity Plus Fund	**3,572**	3,525
	18,731	34,847

Appendix 10
Notes 19: Gross cash flows

Capital expenditure and financial investment	**2008**	**2007**
	£000	**£000**
Sales of investments	**22,349**	15,256
Purchase of investments	**(24,567)**	(18,236)
Sale of tangible fixed assets	**914**	4,184
Purchase of tangible fixed assets	**(12,776)**	(12,539)
Net cash (outflow)	**(14,080)**	(11,335)

Appendix 11 Double-entry bookkeeping

BALANCE ACCOUNT 31.12.2007

Tangible assets	60,495	Accumulated funds	150,282
Fixed Investments	65,396	Defined benefits pension scheme deficit	742
Stocks	2,080	Provision for liabilities and charges	19,524
Debtors	17,247	Amounts falling due in more than one year	275
Current Investments	34,847	Amounts falling due within one year	19,624
Cash at bank and in hand	10,382		
	190,447		190,447

Tangible assets

OB	60,495	2b)	5,062
7)	13,964	8)	713
		EB	68,684
	74459		74459

Fixed Investments

OB	65,396	10)	22,349
9)	24,567	4)	14,275
		EB	53,339
	89,963		89,963

Stocks

OB	2,080		
11)	611	EB	2,681
	2,681		2,681

Debtors

OB	17,247		
12)	2,109	EB	19,356
	19,356		19,356

Current Investments

OB	34,847	13)	16,621
3)	505	EB	18,731
	35,351		35,352

Financial result accounts

2)	239,755		243,548
4)	14,275	3)	505
5)	289	6)	10,266
	254,319		254,319

Accumulated funds

		OB	150,282
6)	10,266		
EB	140,016		
	150,282		150,282

Defined benefits pension scheme deficit

14)	382	OB	742
EB	649	5)	289
	1,031		1,031

Provision for liabilities and charges

15)	13,949	OB	19,524
EB	5,575		
	19,524		19,524

Amounts falling due in more than one year

		OB	275
EB	275		
	275		275

Cash

OB	10,382		
	243,548	2a)	234,693
8)	713	7a)	12,776
10)	22,349	9)	24,567
13)	16,621	11)	611
16)	142	12)	2,109
		14)	382
		15)	13,949
		EB	4,668
	293,755		293,755

Amounts falling due within one year

		OB	19,624
		7b)	1,188
EB	20,954	16)	142
20,954		20,954	

BALANCE ACCOUNT 31.12.2008

Tangible assets	68,684	Accumulated funds	140,016
Fixed Investments	53,339	Defined benefits pension scheme deficit	649
Stocks	2,691	Provision for liabilities and charges	5,575
Debtors	19,356	Amounts falling due in more than one year	275
Current Investments	18,731	Amounts falling due within one year	20,954
Cash at bank and in hand	4,668		
	167,469		167,469

Explanations:

D=Debit; C=Credit; OB=Opening balance; ED=Ending balance

1) Total incoming resources (243,548)

(D-Cash(243,548) and C-Financial result accounts(243,548))

2) Total resources expended are supposed to be the sum of Cash and depreciation of Tangible assets(Notes10). (239,755)

(D- Financial result accounts(239,755), C- Cash(234,693) and C- Tangible assets (5,062))

3) Net investment gains in the year for Current investments is an adjustment of book value to market value(Notes11).(505)

(D- Current Investments (505) and C- Financial result accounts(505))

4) Net investment losses in the year for Fixed investments is an adjustment of book value to market value(Notes11).(14,275)

(D- Financial result accounts (14,275) and C- Fixed Investments (14,275))

5) Actual losses on Defined benefits pension scheme deficit (289)

(D- Financial result accounts (289) and C- Defined benefits pension scheme deficit (289))

6) Close Financial result account to Accumulated funds.(10,266)

(D- Accumulated funds(10,266) and C- Financial result accounts (10,266))

7) Additions to Tangible assets are supposed to be Cash and Amounts falling due within one year(Notes10&19).(13,964)

(D-Tangible assets(13,964), C-Cash(12,776) and C- Amounts falling due within one year(1,188))

8) Cash from sale of tangible fixed assets (Notes19): (914-201=713) (Net gains of disposal of fixed assets are included in Total incoming resources already.)

(D-Cash(713) and C- Tangible assets(713))

9) Purchase of investments (24,567)

(D-Fixed Investments(24,567) and C-Cash(24,567))

10) Sale of investments (22,349)

(D-Cash(22,349) and C-Fixed Investments(22,349))

11) Increase in stocks (611)

(D-Stocks(611) and C-Cash(611))

12) Increase in debtors (2,109)

(D-Debtors(2,109) and C-Cash(2,109))

13) Cash withdraw from current asset investments(16,621)

(D-Cash(16,621) and C-Current Investments(16,621))

14) Net charges for defined benefit pension scheme(382)

(D- Defined benefits pension scheme deficit(382) and C-Cash(382))

15) Decrease in provision for liabilities and charges(13,949)

(D- Provision for liabilities and charges(13,949) and C-Cash(13,949))

16) Increase in creditors(142)

(D-Cash(142) and C- Amounts falling due within one year(142))

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