

**FOR** LEGAL

Learning without limits

James Stebbings

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**Why do Charities ask for so much information about the gifts they receive in wills?**



# Introduction

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- › Gifts in wills contribute £3.5bn a year to UK charities and this is expected to exceed £5bn a year by 2030. This income already represents over 25% of charities' fundraised income but it is becoming an increasingly larger share year by year.
- › Gifts in wills are an incredible way to give to charity. Many people in the UK are asset rich but cash poor and legacy giving allows them to give that capital away when they no longer need it. This allows ordinary people to leave extraordinary gifts to charity.
- › Administering an estate with charitable beneficiaries introduces different challenges for executors with different tax considerations and often greater demands in terms of clear accounting and documentation.
- › The Institute of Legacy Management (ILM) is working in partnership with For Legal to help people administering estates understand what charities need and why they need it. James Stebbings is Chair of the ILM.



# What is the role of the charity legacy professional?

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Charity Legacy Professionals are responsible for ensuring that supporter's final wishes are fulfilled and that each gift is administered in accordance with the legal requirements placed on charities.

- > The key role of a legacy officer is to ensure that supporters' wishes are fulfilled which usually means ensuring the gift is received and used to further their charity's objectives.
- > The financial importance of legacies to charities means that it is vital that they are accounted for properly, with income being recognised accurately and at an appropriate time.
- > Legacy professionals play a vital role in forecasting income from legacies so that plans can be made to use the funds.
- > It is vital that charities communicate their appreciation for the incredibly generous gifts supporters leave in their will to executors, family and friends.
- > Please contact the ILM if you think that our members are falling short. We want legacy giving to be a great experience as we want as many people to leave gifts as possible, we want estates administered to high standards and our members to be helpful and be positive.

# FRS 102 and SORP 2015 – The Accounting Principles

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Legacy Professionals must adhere to SORP 2015 when accounting for Legacies.

- › Charities accounting principles are set out by FRS102 – The Financial Reporting Standard applicable in the UK and Republic of Ireland
- › The Charity Commission’s Statement of Recommended Practice(SORP) 2015 is based on FRS102 and recommends how charities should prepare ‘true and fair’ accounts in accordance with UK accounting standards.
- › The purpose of the SORP is to provide consistency between charities and make life easier for the users of accounts.
- › The SORP is updated from time to time to take account of changes to accounting standards and/or charity law and the ILM are participating in the latest review.



# SORP 2015 – Key concepts

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SORP dictates that charities should account for legacies once they have:-

- > Entitlement
- > Measurement
- > Probability of Receipt

- > The section on accounting for legacies is set out at 5.29 to 5.37 of SORP 2015. The wording is open to different interpretations which means there isn't a single accounting method used by UK charities.
- > Under SORP 2015 charities should recognise income when they have confirmed their entitlement to the gift, where they can identify the value of the gift and where they have probability of receipt.
- > In the previous guidance the requirement was that charities' had to have "certainty" of receipt. The change to "probability" has seen many charities move to recognising income earlier than they had prior to 2015.
- > Whilst there is variation between charities, auditors will insist on any interpretation being applied consistently on all legacies received by the charity.



# Entitlement

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Most charities consider they have “entitlement” to a legacy when probate is granted on a will including a gift to the charity

- › The first requirement for a charity when deciding whether to recognise the income is that their entitlement to the gift has been established.
- › Most charities recognise that they have entitlement, when it is clear that there is a valid gift, in a valid will and where no potentially valid legal claims exist.
- › Most charities deem themselves to have entitlement whenever probate has been granted and there is no indication of a potential legal claim against the estate.
- › However, some charities believe the ongoing threat of a claim coming forward means entitlement is not sufficiently established until the executors are nearing distribution even where there is no indication of a claim being made.

# Entitlement – How executors can help charities?

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Information about potential claims against the estate will help charities forecasting.

- › Charities greatly benefit from early notification of a gift in a will because it enables them to estimate a pipeline of future income.
- › Whilst most charities subscribe to the legacy notification service provided by Smee & Ford which will confirm probate, this is often delayed, it is therefore always helpful when executors advise charities when probate is granted.
- › The more information on the value of the gift the executor can provide, the more accurate an estimation of future income can be made. Charities will always value an estimated value for their legacy or alternatively an estimate of the net estate.
- › If the executor is aware of any disgruntled beneficiaries who are contemplating or are in the process of making a claim against the estate they should advise charities so that suitable adjustments can be made to the pipeline

# Measurement – Identifying the value of the gift

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SORP 5.35 states it must be possible to produce a reasonably accurate estimate in order to recognise income .

- › The central premise of FRS 102 is that the accounts should show a “true and fair” reflection the organisation’s financial health. This usually involves some element of estimation and forward accounting e.g solicitors accounting for WIP.
- › For legacies to be recognised early, a degree of estimation is required especially for residuary gifts which are subject to the estate administration costs.
- › SORP indicates that charities with sufficient historical data can use this to make a reasonable deduction for probable costs. Many charities take this approach but there is not a standard percentage deduction and some choose not recognise income until the executors identify the costs.
- › The formula for identifying the probable amount received is simply
  - Latest known value of Assets
  - Less Liabilities
  - Less Estate Administration Costs (estimated)
  - Less Specific and Pecuniary Gifts (usually from executor)
  - % of Estate to beneficiary



# Measurement – How executors can help charities?

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Charities need to monitor their valuations to ensure they remain true and fair estimates for the legacy.

- › The issue for charities is that the value of the assets may change during the administration of the estate. Where that happens charities should be updating their estimate of that legacy.
- › Executors can assist charities with their accounting by updating them when there is a material change in asset values from probate or from an interim account.
- › It also greatly assists charities to know when a distribution is likely as they should start discounting their valuation where funds won't be received within 12 months.
- › Charities often make an estimate for administration costs. Where executors have an indication of the estate administration costs it is helpful if the charities are informed so they can check their estimate is appropriate.

# Probability of Receipt

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SORP states that charities should not account for legacies unless there is probability of receipt

- › This concept reflects the fact that legal entitlement to money does not necessarily result in payment.
- › Charities need to monitor each gift to make a judgement whether the funds due to them will be paid and ensure that they do not account for gifts where there is not “probability of receipt”.
- › The drafting of SORP muddles this concept with entitlement and references claims against the estate in this context. The ILM’s view is that a claim threatens entitlement but many charities would exclude income subject to a claim on the basis that there is not probability of receipt.
- › If claims are about entitlement then probability of receipt is about fraud or non payment by the executor. Thankfully, this is extremely rare, in part because charities subscribe to notification services and because they employ legacy officers but mainly because executors are usually honest and reliable

# When should charities recognise income?

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The ILM believes early recognition is the way to give a true and fair reflection of a charities financial position.

- > There is currently a huge variation of approach with some charities waiting until receipt, some until final accounts, some until assets and liabilities or interim, some from the net estate at probate and other pre probate.
- > Many, including executors and legacy officers believe that legacies are inherently uncertain and recognising income before receipt is both presumptive and fraught with risk.
- > However, an increasing majority of charities and accountants take the view that early recognition is the only way to give a true and fair reflection of the charities financial position.
- > The ILM believes a more consistent approach would benefit of members, for users of accounts and for executors. We think the most true and fair approach is to recognise income when probate has been granted so long as there is no claim or other matter that threatens entitlement or receipt.
- > We do however acknowledge the risks of including unpaid legacies on the balance sheet and we would be willing to support an approach where legacies were accounted for as contingent assets prior to receipt.

# Working together

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- › We would love anyone involved with will writing and estate planning to help us normalise the inclusion of charities in wills.
- › Please come to us if you have concerns about the way charities are approaching things.
- › We appreciate your contribution and would love your continued support.
- › For more information on charities requirements and information about the ILM please visit our website <https://legacymanagement.org.uk/> or email [support@legacymanagement.org.uk](mailto:support@legacymanagement.org.uk)

