Charity accountability in the UK: through the eyes of the donor

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Abstract

Purpose – The purpose of this paper is to explore accountability from the perspective of charity donors.

Design/methodology/approach – The research utilises semi-structured interviews with a range of donors. In addition, it summarises the main findings from key related research (that uses document content analysis and questionnaire surveys) as a basis for better appreciating donor engagement.

Findings – This research offers evidence that while donors are viewed as the key stakeholder to whom a charity should be accountable, the relevance of the information commonly disclosed in formal charity communications is questionable. This is viewed as significant in terms of small dependent donors, although less critical in the case of non-dependent large donors who have power to demand individualised information. However, although all donors do not particularly engage with these formal communications, they are viewed by them as having significance and their production and publication serves as an important legitimising tool in the sector (enhancing trust and reputation).

Research limitations/implications – This research is based on semi-structured interviews with individual small donors and large institutional donors to large UK charities and therefore any generalising of the conclusions beyond large charities, and beyond the UK, should be undertaken with care. In addition, it focuses solely on the perceptions of donors, and other stakeholder groups are also important in this process.

Originality/value – Despite the widespread acceptance that charities have a duty to discharge accountability to their stakeholders, there is limited knowledge of their information needs and whether the performance information currently being disclosed fulfils them. This study provides a unique insight into the perspective of a key stakeholder group (donors) with respect to accountability.

Keywords Accounting, Charities, Reporting, Stakeholders, United Kingdom

Paper type Research paper

1. Introduction

The charity sector in the UK[1] comprises a vast and growing segment of economic activity with substantial assets at its disposal. By 2012 there were over 200,000 registered charities with an estimated total annual income well in excess of £60 billion (for example, there are 180,000 charities in England and Wales alone with an estimated total annual income of more than £59 billion – Charity Commission, 2012). The growth in the size and influence of the sector, combined with a number of highly publicised scandals, has led to increased sector visibility and public scrutiny (Katz, 2005) and the need for the sector to operate transparently and discharge accountability has been widely articulated. Indeed, under the 2006 Charities Act, the Charity Commission in England and Wales has been charged with responsibility for: enhancing charitable accountability; increasing public trust and confidence; and promoting the effective use of charitable funds. In Scotland and

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Northern Ireland, major changes in the regulatory environment have emphasised similar themes. While the conceptual framework for charity and other not-for-profit (NFP) reporting has been guided by the accountability paradigm (Accounting Standards Board, 2007), the focus has principally been on financial reporting. Recent discussion has however emphasised the significance of narrative and non-financial quantitative disclosures in the discharge of NFP accountability, and has principally focused on the need to explain performance. Indeed, the summary information return (SIR)[2] which applies to large charities centres on meeting this need, as does the most recent statement of recommended practice (SORP)[3] for charities (Charity Commission, 2005).

The user-needs (or stakeholder-needs) model is now well established as a useful basis for a conceptual framework for charity reporting, and the view that accounting should provide information to satisfy the information needs of stakeholders is inextricably linked with the concept of accountability. While accountability, in its widest sense, is more than accounting, no matter how widely accounting is defined, accounting is clearly linked to the concept of accountability. Appropriate accounting and reporting (i.e. the provision of information that meets the needs of stakeholders) are necessary to maintain and build confidence in the charity sector as a basis for promoting both charitable giving and charitable activity.

In considering accountability, two key questions emerge: to whom is a charity accountable; and what form should that account take? While there is a range of different stakeholders who can be served by accounting and reporting, including beneficiaries, government, regulators and the public, this paper focus on donors. While charities receive the overwhelming majority of their resources from such stakeholders, donors receive no direct economic benefit from their donations. In addition, it has been argued in previous studies that it is donors to whom a charity is primarily accountable (Connolly *et al.*, 2009; Hyndman, 1990). Donors have information needs, yet because they are not involved in the management of the charity they normally have to rely on external communications through formal channels to meet those information needs.

In addition, and relating to the "form of the account", it has been argued that while financial accountability (through, for example, audited financial statements) is important, such accounts are likely only to be of secondary importance. Other wider information, particularly relating to performance (for example, information relating to goals, service provision, outputs, impact and efficiency), is likely to be paramount in discharging accountability to donors. With respect to charities, the provision of information through formal information channels is a major part of the process of discharging accountability to those outside its immediate management, as the information is important for making decisions and judgements relating to involvement with, and support of, the organisation. The conceptual framework for charity and other NFP reporting has been guided principally by the accountability paradigm, with financial information contained in traditional financial statements dominating discussions (Accounting Standards Board, 2007). By contrast, the Charity Commission has also highlighted the role of the trustees' report, which contains substantial performance information, as a vehicle with which to discharge accountability to external stakeholders. It could be argued that the accountability discharged in the form of traditional financial statements largely provides evidence that funds have not been misappropriated. In contrast, accountability in relation to one's actions, outcomes and responsibilities cannot be captured in such reports.

The main objective of the paper is to explore accountability from the perspective of the donor. In doing this, it presents and discusses the results of a series of semi-structured interviews with donors regarding accountability and their own information needs. As such, it gives a unique insight into donors' perspectives on accountability. Given that charities are economically dependent on donors for their survival and growth, deficiencies in accountability to donors have the potential to undermine confidence in the sector and, as a consequence, impact negatively on both charitable giving and charitable activity. In terms of the format of the paper, the next section examines accounting, accountability, stakeholder theory (and the importance of donors as a key stakeholder group) and donors' motivations for giving. This provides a theoretical backdrop for the reported empirical research that is the focus of this paper. This is followed by a summary of related, recently-published empirical work utilising document analysis and surveys (Connolly and Hyndman, 2013) which is subsequently used as an input to the analysis of the results from the interviews. The methodology is then described, findings presented and, finally, conclusions are drawn.

2. Accountability, donors and motivations for giving

2.1 Accounting

The conventional view of accounting is that it is a purposive activity, directed towards a specified end, which is the meeting of users' information needs (Accounting Standards Board, 1999; Macve, 1981). Discussions relating to this often focus on issues such as the objectives of accounting and reporting and the information rights and needs of stakeholders. Such deliberations have been prevalent with respect to NFP organisations (NFPOs), including those in the public and third sectors (Bird and Morgan-Jones, 1981; Financial Accounting Standards Board, 1980). Summarising some of the key themes, Mayston (1992, p. 228) argues that as:

> [...] a normative objective for financial reporting, the meeting of users' needs has now been widely accepted as the central objective by a long series of reports on the objectives of financial reporting.

The annual report and financial statements (referred to hereafter merely as the annual report) are generally recognised as key accounting documents that support the discharge of accountability to external users. As statutory requirements in most Western economies, annual reports attract a degree of authenticity (the extent often being associated with the mechanisms used to ensure reliability), not associated with other reporting formats and are often the principal means through which management fulfils its reporting responsibilities (Gray *et al.*, 2006). In the UK, the SORP for charities (Charity Commission, 2005) states that the purpose of preparing a charity's annual report is to discharge the trustees' duty of public accountability and stewardship. It is suggested that, among other things, the annual report should enable the reader: to understand the charity's structure and performance, that is, its activities and achievements; and gain a full and proper appreciation of the charity's financial transactions and financial position. In addition to the annual report, many charities also voluntarily prepare an annual review as a means of communicating their performance with external stakeholders. This is normally a shorter, pithier publication that includes some of the information in the annual report (but often in a more condensed form), frequently written in less formal language and including a higher proportion of stories, photographs and diagrams.

In the charity sector, the importance of high-quality accounting and reporting is argued by many (Bird and Morgan-Jones, 1981; Connolly and Dhanani, 2009). A key theme is that poor accounting and reporting (and, as a consequence, the possibility of scandals) could severely undermine confidence in the sector and reduce both charitable giving and activity. Furthermore, it is advocated that the widespread adoption of appropriate accounting and reporting practices has the potential to provide a basis for greater faith in the control processes within charities and result in a more accountable and more legitimate sector; thereby enhancing public confidence.

2.2 Accountability

Calls for greater accountability have been widespread in recent years. However, what constitutes accountability remains unclear and the concept has been variously referred to as being elusive, chameleon-like and abstract (Ebrahim, 2003; Geer *et al.*, 2008). Crofts and Bisman (2010), while broadly agreeing with this thrust, argue that, in order to understand accountability better, any discussions need to be related to the context to which it pertains. They particularly encourage the investigation of accountability in specific settings (as is the focus of the later empirical work presented in this paper). While there are clear links between accounting and accountability, Hyndman (2010) has posited that accountability is more than accounting. Various writers have focused on aspects such as the giving of an account or the being held to account (Laughlin, 1990; Lawry, 1995). These views imply a principal-agent relationship in which the agent, who is entrusted to perform the delegated function, gives an account to, or is held to account by, the principal. In such a scheme, the principal transfers to an agent resources and expectations regarding the transfer. These expectations form the basis of the accountability relationship. As Laughlin (1990) highlights, these expectations are complex and may be written and explicit or unwritten and implicit. Here, it is suggested that while information transmission is critical, the mere transfer of information is not sufficient, and that the actions taken by the principal based on their interpretation of the account also constitutes accountability. Implicit in this model is that the principal should have the power of authority to take appropriate action, including continuing with the relationship if so desired, amending the relationship or severing the relationship.

Three broad states of affairs for which an agent may be held accountable have been identified by Goodin (2003): their intentions (what their motives were); their actions (what they did); and their results (what the outcomes of their actions were). In the charity sector this can translate into providing an account with respect to: the mission, vision and objectives; the actual activities and programmes; and the extent to which mission and objectives have been achieved. In addition, Brody (2001) and Taylor and Rosair (2000) add that NFPOs, including charities, also need to report on whether appropriate systems and measures are in place to ensure financial probity. They classified accountability into two types: fiduciary accountability, to emphasise probity, compliance, control and good governance practices; and managerial accountability, to reflect organisational effectiveness and impact on society. Similarly, Ebrahim (2003) distinguished between internal and external accountability, in which the former is concerned with accounting to constituents internal to the organisation, and the latter to audiences external to the organisation. Necessarily, mechanisms to account vary depending upon the form that the accountability takes. For example, mechanisms for internal accountability often entail operational adjustments and compliance with procedures and processes, while external accountability often involves formal report writing.

In considering users to whom accountability should be discharged, Hyndman and McMahon (2010) argue that many external stakeholders (particularly small donors) of a charity have information needs, yet because they are not involved in the management of the charity they often must rely on formal communications from a charity to meet those needs. Furthermore, it is argued that although financial accountability has some importance (to indicate, for instance: that the money raised has been used for the appropriate purposes; that the charity has "lived within its means"; and the level of resources available to the charity for future service provision), accounts focusing solely on financial matters are likely to be inadequate in terms of discharging accountability. Indeed, research has shown that donors are likely to have only limited interest in such communications (Hyndman, 1991; Kilcullen *et al.*, 2007). Of much more importance to these stakeholders is information relating to performance, and this will require the telling of "the story" of the charity in a way that is truthful, consequential and engages with donors (Connolly *et al.*, 2009; Gray, 1984; Hyndman, 1991; Khumawala and Gordon, 1997).

2.3 Stakeholder theory and donors

Ideas from stakeholder theory can be linked to themes in the accounting and accountability literatures. Stakeholder theory originated from studies by Freeman (1984). The central argument advanced was that if organisations engaged with stakeholders on a basis of mutual trust and cooperation, those organisations would build legitimacy and reputation that would give a competitive advantage over rivals. Stakeholder theory is concerned with the long-term survival and success of organisations and proposes that these organisations require the support of their constituents, and that to gain this support and approval, management need to legitimise their activities to these groups (Lindblom, 1994; Roberts, 1991). Management can obtain legitimacy by deploying different accountability mechanisms with which to demonstrate that the values, beliefs and successes of the organisation are commensurate with stakeholder expectations and demands (Gray *et al.*, 1995). Stakeholder theory has become an increasingly popular way in which to understand accountability, with the Charity Commission highlighting the importance of stakeholders in its discussion of accountability and defining accountability in terms of meeting the legitimate information needs of these constituents.

With respect to stakeholder theory, critical concerns relate to the identification and prioritisation of stakeholder groups in terms of discharging accountability. A number of charity-focused studies have identified a range of stakeholders to whom a charity should account. These include: funders and donors; the accounting profession and other regulators; beneficiary groups and clients; government; the general public; employees; and partner organisations (Hyndman and McDonnell, 2009; Le Roux, 2009). With respect to the prioritisation of these stakeholders, Mitchell *et al.* (1997), in exploring how organisations determine "who or what really counts" with respect to competing stakeholder claims, introduced the concept of stakeholder saliency. They argued that the salience of stakeholders (or the degree to which they and their arguments were perceived to count) depended upon the stakeholder possessing three attributes: power, legitimacy and urgency. It was suggested that the most salient to the organisation are stakeholders who are perceived to have power, legitimacy and urgency; and the claims of these "definitive stakeholders" (Mitchell *et al.*, 1997, p. 878) are likely to be prioritised. The salience of stakeholder groups, that is the degree to which their influence(s) will impinge on organisational activities, will determine the hierarchical structure.

Donors to charities have been singled out as the most significant group of stakeholders for fundraising charities (Hyndman, 1990) because they ensure the long-term survival of these organisations through regular funding. Indeed, much of the focus of guidelines for accounting in NFPOs has been targeted at donors and funders[4]. For example, the Accounting Standards Board (2007, p. 10) drew attention to the claims of this stakeholder group (referred to as "funders and financial supporters").

2.4 Motivations for giving

Given the importance (or salience) of donors as a stakeholder group, an understanding of the reasons for giving would seem to provide a useful input to discussions on appropriate accountability mechanisms. Prior research on this area is both large and extremely broad and encompasses work from economic, sociological and psychological perspectives. While comprehensive coverage of this is beyond the scope of this paper, some key themes (which inevitably overlap) are considered which help to provide context to the subsequent empirical work.

Religious belief is viewed as being one major determinant of giving; with the extent of commitment to religious beliefs being positively correlated with charitable giving (Edmondson, 1986; Graham and Haidt, 2009). A link between social interacting and religious charitable giving has been identified as being important. Graham and Haidt (2009) found that religious individuals tend to involve themselves more directly in helping their communities, and, as a consequence of such involvement, increased their donations. Several studies of charitable giving have explored behavioural aspects, often focusing on the concept of altruism. Occasionally linking with ideas connected to religious beliefs, altruism is viewed as a completely selfless form of behaviour whereby the individual's motivation comes purely from the concern and well-being of others with no self-satisfaction. This concept however lacks empirical backing, mainly for the reason of difficulties in specifying donors' reasons for giving. Andreoni (1990) suggested that pure altruism does not exist because it is human nature for a person to feel happy (or gain utility) from doing good. He argued that contributions to charities increased because of the self-satisfaction that individuals got from donating, supporting a notion of impure altruism (the theory of "warm glow giving").

Some researchers have suggested that the main (or only) reason that people give to charity is related to pure self-interest. Various economic studies have explored who is most likely to give, often relating "giving" to variables such as income, age and education. These may provide some clues as to the types of people who are likely to be receptive to charitable messages (and who are liable to gain utility by responding to such messages) and may be particularly useful to charities in targeting potential donors. However, it has been argued that the identification of these variables alone is not enough and such variables are "descriptive at best" (Smith and McSweeney, 2007, p. 4). Literature from a sociological and psychological perspective has explored motivational trends related to giving. Empirical studies have shown that individuals are moved to support charities seen to be fighting causes that have personally impacted on their lives, possibly linked to them through the illness or the death of a family member

(Bekkers and Wiepking, 2007). Similarly, studies have shown that people who can be classified as "animal lovers" give much more to charities relating to animal welfare rather than charities relating to social welfare (Bennett, 2003). Moreover, individuals with a sense of the importance of being involved within a community or social organisation are more likely to give (Aaker *et al.*, 2009). Perhaps, unsurprisingly, the highlighting of particular causes (or particular individuals) by the media can have a powerful influence on giving by individuals. Small *et al.* (2007) found that people were more likely to give if they could perceive an "identifiable victim" rather than a "statistical victim". Such findings would encourage the highlighting of vignettes and stories by charities as a means of engaging with donors and potential donors. In addition, research from New Zealand (Huang and Hooper, 2011) focusing on how major funding organisations allocate resources, has suggested that financial information is of limited importance in such decisions. Of more importance are outcome (performance) information and the character of the key people in the organisation requesting funds.

Research has also indicated that giving to charity can be used as a signalling device by both individuals and businesses, with those who are successful financially having a desire to demonstrate (or signal) that success through philanthropy (Glazer and Konrad, 1996). Philanthropic activity has become common in recent years among wealthy individuals and big corporations; not only signalling how wealthy they are but also potentially rewarding them with popularity (which may be useful in driving future success). With companies, giving to charities may indicate a wider corporate social responsibility. Additionally, by providing large donations, it may also demonstrate liquidity to the market, and consequently encourage investors to acquire shares of the company.

3. Towards charity accountability: narrowing the gap between provision and needs

Based upon a content analysis of the (statutory) annual reports (voluntary), annual reviews and SIRs of the top 100 UK fundraising charities and an online questionnaire survey of their stakeholders, Connolly and Hyndman (2013) sought to:

- establish the accountability information disclosed by charities through formal channels of communication;
- identify the key charity stakeholders with respect to the discharge of accountability;
- determine the relative importance of established channels of communication in the discharge of accountability to key charity stakeholders;
- ascertain the information needs of donors; and
- identify any gaps between the information disclosed and information needs.

To allow comparisons to be made over time, Hyndman's (1990) checklist of 14 information types, which contains a mixture of the information types identified as being important to charity donors (argued by Hyndman as the group to which the annual report was primarily addressed) and those most frequently disclosed by charities in their annual report, was utilised by Connolly and Hyndman (2013) as a framework for analysing information disclosure. In broad terms, Hyndman (1990, 1991) compared the perceptions of donors' information needs by the providers of information (charity officials and auditors) with identified information needs, and found that while audited financial statements dominated charity reporting, donors viewed other information, particularly that relating to performance, as more important. Moreover, providers of information were largely aware of donors' information needs.

In summary, Connolly and Hyndman (2013) reported that:

- Donors are viewed by all respondent groups (auditors, charity officials and donors themselves) as the key stakeholder to whom a charity should be accountable.
- When donors' information needs are compared to the information disclosed in annual reports and annual reviews, a gap is apparent.
- Extant charity annual reports are dominated by audited financial information (operating statement/statement of financial activities, balance sheet and funds flow/cash flow statement). However, this information is perceived by donors as being relatively less important than performance-related information (for example, measures of output and measures of efficiency) that is much less disclosed.
- Annual reviews include a greater proportion (although, overall, similar levels of disclosure) of performance-related information (disclosures viewed by donors as of greatest importance) compared with annual reports, but a much lesser proportion (and much lower levels of disclosure) of traditional audited financial statement information (information viewed by donors as much less important).
- Annual reviews are perhaps a more meaningful communication with donors, as they are considered by all respondent groups as being a more engaged with (defined as meaning "read, understand and consider"), although less important, communication channel compared with the annual report.
- Given the lack of alignment between the contents of the annual report and the information needs of donors, annual reviews may be the main means of discharging accountability to such stakeholders, with annual reports, documents that have greater regulatory oversight, assuming a more formalised role relating to the legitimation of the charity.
- With respect to the perceived limited engagement with the annual report, it may be that some groups (for example, small donors) may not be especially interested in, or capable of understanding, detailed accounting and reporting.
- While there remains a gap between donors' information needs and the information disclosed in annual reports and annual reviews, it has closed over time, with much greater information disclosure in annual reports through time, particularly with respect to performance information (the most important information sought by donors).
- An area where performance disclosure has not increased substantially over time, although one considered very important by donors, is with respect to administration cost percentage information.

4. Research method

To obtain a more in-depth understanding of the research by Connolly and Hyndman (2013), semi-structured interviews were conducted with charity donors. Given the difficulties of gaining access to interviewees, the potential sensitivities of the matters being discussed and the desire for the interviewees to be as candid as possible, each potential interviewee was informed (prior to agreeing to be interviewed) that the interviews would be reported in a manner where specific statements could not be attributed to particular individuals. It was considered that such assurances were necessary to increase the quality of participation.

A semi-structured interview guide, informed by the theoretical and contextual issues explored in the literature review presented above and the Connolly and Hyndman (2013) findings, was developed and the interviews, which ranged from one to two hours in length, were conducted by two researchers. All interviewees allowed their interviews to be recorded and notes were taken during the interview. The recordings were transcribed immediately to ensure accuracy and comprehension of the interview data. In total six interviews were conducted with charity donors, three with individual small donors (CD1, CD2 and CD3), and three with large donors (two grant makers, CD4 and CD5, and one with a corporate donor CD6)[5]. This allows distinctions to be made between individual small donors and large donors (where relevant) in the analysis (as well as enabling the reader to identify comments from the same interviewee). The three individual donors claimed to have contributed between £3,000 and £6,000 per annum to a small number of charities (between three and five) each, and had done for a number of years. The two grant maker interviewees were senior executives of relatively large charitable trusts which had each made grants exceeding £5 million per year to a large number of charities. The corporate donor contributed gifts in excess of £10 million per annum, again across a significant number of charities. By giving each interviewee a unique reference, this allows the reader to identify comments from the same interviewee, while maintaining the confidentiality of the interviewee.

5. Accountability through the eyes of donors

In terms of the format of this section, the analysis of the interviews with the charity donors is presented under the following sections: exploring accountability; meeting user needs and discharging accountability; and the influence of external practices and drivers of charity accountability.

5.1 Exploring accountability

In an attempt to link user needs, stakeholder theory and accountability, and perhaps give an insight into where accountability pressures come from, interviewees were asked what they understood by "accountability" in terms of charities. Most interviewees, whether small or large donors, made reference to accountability being associated with demonstrating that monies received had been spent in accordance with the aims and objectives of the charity. Consequently, views on accountability were often closely associated with how it was discharged:

> Being accountable is being able to show that the money given to the charity has been spent on providing services for us (CD4).

Some interviewees linked accountability with stewardship, including the implementation of appropriate systems and structures to record monies received and how they were spent, particularly with respect to restricted funds (in the case of large donors):

> I am most interested in making sure a charity has the right processes in place so that they can track that money is spent as it should be, spot mistakes and focus on what works (CD5).

When the donors were asked to whom charities should be primarily accountable, most began by accepting that charities are accountable to a wide range of stakeholders:

> One of the interesting things about charities is that they have multiple and overlapping levels of accountability. They're accountable to their funders, to government, to their members, to their beneficiaries (if they don't have members), and even to the community (CD4).

When pushed further, and consistent with the Connolly and Hyndman (2013) questionnaire findings, the interviewees tended to deliberate whether primacy of accountability should be towards donors or beneficiaries. Some argued that charities should be primarily accountable:

> [...] to the people who donate; the donors. Because the charity probably wouldn't exist if it wasn't for the donors (CD2).

While others highlighted the need to be answerable to beneficiaries:

> I guess that in its purest form of why charities exist, they exist to marshal funds on behalf of those in their aims, that they say they are there to benefit, and so they are legally accountable to those people [the beneficiaries] on how they spend those funds and what they achieve (CD5).

However, this apparent tension relating to the primacy of stakeholder groups in terms of accountability may however be overstated, as some interviewees acknowledged that meeting the needs of beneficiaries could not be divorced from being accountable to donors. It was suggested that the interests of these two groups may in fact be mutually supportive, particularly when it was difficult for charities to engage with their beneficiaries:

> How accountability actually manifests itself depends on who's there to hold charities to account. It might be that the regulator holds charities to account on behalf of beneficiaries because beneficiaries can't. Alternatively, funders can provide a good proxy because they act in the best interests of beneficiaries (CD5).

Nonetheless, although interviewees accepted that there could be a link between donors' and beneficiaries' interests, there was a note of caution about focusing too heavily on donors' needs. This was particularly the case where donors' perceptions of beneficiary needs were not up-to-date:

> If you have a funder, a charity, a beneficiary, a flow of money, activities and some sort of feedback of impact. If the charity reports no impact then the funder presumably will decide to give elsewhere. In theory, the funder is also measuring beneficiary needs and whether those needs are changing. But this is not a functional loop of information and so if funders are supposed to be acting as a proxy for the beneficiaries' best interests, they almost never do and the loop breaks down at every single point (CD5).

The Connolly and Hyndman (2013) questionnaire explored the issue of why people give and why they choose a specific charity, with the results indicating that most donors give primarily because of either a "commitment to the aims and objectives of the charity" or a "personal experience" with either the charity or the cause. The overwhelming impression from individual small donor interviewees was that the "cause" was their motivation and that they trusted those organisations that they gave to (possibly because of their charitable status and some previous contact). There was an inherent belief among individual donors in particular that the charities they donated to were inherently good and would spend the money given to them wisely and appropriately:

> I usually give to charities based on people I know who are associated with them in some way (CD2).

> I trust the charity to use the money that I give to them to do what they are supposed to do with it (CD3).

When interviewees were given the opportunity to suggest how charities should discharge their duty of accountability, the most common response was the inclusion of more narrative (performance) information in the formal communications of charities (annual reports and annual reviews) so as to explain the story behind the figures:

> I would like more of the personal stuff than the actual figures [. . .] I'm not analytical about it, I'm a story person. This would prompt me to continue giving if I think, "Yes, that's doing well" (CD2).

5.2 Meeting user needs and discharging accountability

It is often argued that accounting information can provide an important and regular mechanism through which major aspects of accountability are discharged, and that the annual report is a suitable reporting package through which accountability can be discharged. As an indication of whose needs charities were trying to meet, interviewees were asked to whom the annual report, annual review and SIRs were addressed and used by. If not used, the role of such communications in discharging accountability is limited.

Respondents to the Connolly and Hyndman (2013) questionnaire indicated that while the annual report is viewed as the most important channel of communication, the annual review is viewed as the most engaged with[6]. Interestingly, the individual small donors interviewed did not show a significant desire to engage with either of these formal communications produced by charities, and were unclear as to the names and status of the documents they received. In addition, they perceived themselves as having limited power and influence. Moreover, they appeared to rely on others to scrutinise what was going on. As one small donor expressed it, other stakeholders had to "do it on my behalf" (CD1). This donor went on to suggest:

> I might thumb through it [annual report], but I'd never look at it in an analytical way. As long as someone else looks to see that they're doing it right, I'm happy with that (CD1).

Large donor interviewees stated that although they did use annual reports and annual reviews, they would request additional information and additional direct engagement before a funding decision was made (for example, management accounts and cash flow information, together with at least one visit to the organisation's premises). In addition, specific reports (frequently to include information on outputs) relating to any project funded would often be required during the funding period. Therefore, in many cases with respect to large donors, while formal channels of communications (particularly annual reports) had limited impact on the funding decision, it was expected that they would be available as a matter of course. In other words, in the case of large donors, they were necessary but not sufficient for funding purposes:

> Mostly these things give you a warm fuzzy feeling about what a nice organisation it is. We would be looking into the organisation's finances and performance in a lot more detail than what is provided in these documents (CD4).

> Before we go out to see the client, we'll have a look at the different published reports and the web site. But you would never make a decision just on that basis (CD6).

Despite the apparent restricted interest by large donors in the annual report, some stated that it was often checked whether amounts shown in the financial statements for specific projects or purposes agreed with amounts donated/granted, and that clear acknowledgement of such donations was expected.

While the general opinion among all donors was that there was limited interest in the contents of the annual report by many, most interviewees believed that it was still a useful document. One of the main benefits for the charity was seen to be that its preparation imposed a certain amount of discipline on the charity and focused attention on how the charity was being run:

> It forces a charity to review what happened during the year, and to look at this in relation to what their plans are [...] You can't force people to learn from that reflection, but the hope is that they will (CD4).

The individual small donors interviewed largely supported this assessment, with many confirming that their funding decision was mainly based upon the "cause" and not the financial content of the various reports; although being kept informed about the charity's performance, particularly through personal stories, was widely supported.

Interviewees were asked to comment on what they perceived as the status of annual reports in terms of discharging accountability. The broad thrust of the responses was that it was a formal document that provided independent assurance (from the auditor) that the charity was complying with its responsibilities. Without exception, it was considered as essential for the proper regulation of charities and the sector. Moreover, there was agreement among the large donors that the SORP-based annual report had improved considerably in recent years (small donors were less aware of the detail of the SORP changes). However, although it was generally believed by all donors that few people actually read or understand the document (largely because of its length and the inability of most people to appreciate SORP-based financial statements), it was still considered a useful document because of what it represents and what it signals.

Interviewees were asked why it may be, as suggested by Connolly and Hyndman (2013), that despite the annual report being considered the most important channel of communication, the annual review was the one that users engage with most. While the individual donors had to have the differences between these two documents explained by the interviewer before answering this question (each being a little unclear as the title of the various documents that they received), all donors agreed with the suggestion. The reason given for this was that the annual report was perceived as dull and dry in comparison to the more narrative pictorial annual review:

> Most annual reports look a bit more boring than an annual review because the annual review will strip out a lot of the cluttering detail, will put a couple of pie charts but major on the case study and the well written pros and the nice pictures (CD5).

It is argued that performance measures are needed in the charity sector to facilitate management decision making and to allow individual charities, and the sector as a whole, to justify their existence. Unless adequate performance measures are in place, it is often difficult for the charitable sector to counter criticisms as a whole, or for individual charities to refute accusations of poor management and ineffectiveness. Performance information gives a visibility to the resources, activities and achievements of an organisation, thus enabling informed discussions and decisions. Furthermore, it has been suggested that the need to discharge accountability encourages management to concentrate on the issues that are of importance to those stakeholders who are outside the immediate management of the organisation and often provide the resources for the organisation to function. Edwards and Hulme (1995, p. 9) assert that the absence of performance information "begins to make the likelihood of ineffective or illegitimate actions by an organisation much more probable". In the context of charities, this argument suggests that where accountability is weak, management might have no incentive to manage the charity's funds efficiently.

In order to explore this further, interviewees were given the opportunity to indicate what performance information, both financial and non-financial, that currently is not provided should be included in an annual report. A main thrust of the interviewees' responses was that more narrative explanations were needed. In addition, some emphasised that these should not merely describe past events, but should also focus on future plans. While it was believed that the disclosure of more performance information would be beneficial, the overall impression gained was that this was an area that needed more thought and direction (in terms of what information should be disclosed, the basis on which it should be calculated and the channel through which it should be made available).

In addition, the importance of improving performance reporting, and (particularly with respect to individual small donors) the relative lack of interest in financial reporting was stressed in interviews:

> I am interested in, well, things like, are they building schools? Are they setting up water projects? Are they giving aid to countries with famine? All those things. Again it's specific things. I would be pleased if they showed me a person, and told me their name and told me how I had helped them, or how my small bit had contributed to helping them. One person, any project, any village (CD3).

> It's not the financial numbers; it's what they've done [. . .] I think I might be happy enough to have no financial numbers (CD2).

Looking at it more widely, one of the large donors, focusing on the importance of output and impact performance, argued that charities were often good at specifying the social need that they were dealing with, but poor at explaining how they help the situation:

> I think most charities do quite a good job of saying what the problem is; actually they often assume that someone reading it [the annual report] already knows what the problem is. But they do a terrible job of [saying] what they are achieving. They should be giving a sense of both a big picture level (where you are trying to get to, how you think that is going to happen and how you are doing) and also, at the more detailed level, how the work that you do actually translates into changing peoples' lives (CD5).

5.3 Influence of external practices and drivers of charity accountability

The interviewees were asked to consider the extent to which initiatives such as the SORP, SIRs and recent changes in charity legislation have influenced charity accountability. Albeit that small individual donors had only a sketchy understanding of what changes had occurred (and had these broadly explained to them by the interviewer), generally, among donors, there was support for the various initiatives within the sector, especially because they were perceived as raising the profile of the sector and enhancing professionalism. Moreover, it was believed by large donors that the SORP had increased confidence in the sector, even if most people did not actually read the annual report. The Charity Commission was recognised as being extremely influential in driving improvements in the sector and in facilitating charities in doing this. The larger donors suggested that the various initiatives tended to impact most initially on larger charities, with the improved practices then permeating down gradually to medium-sized and smaller charities, which might actually initially see these changes as threats:

> I think there are some steps in the right direction [. . .] the SIR asks some of the right questions [. . .] I think these sorts of things, for those who are already thinking about accountability and taking it seriously, you see them as helpful kind of steps along the way (CD5).

> I think the SORP has improved accountability to the larger charity that can make sense of the documents. To the smaller charity it probably worries the daylights out of them I guess (CD6).

Interviewees were asked about the increase in the disclosure of performance information. Particularly (but not solely), the large donors recognised the increased disclosure, and attributed it to the growing maturity of charities and the sector, and that the changing reporting habits simply reflected the fact that charities now had the systems and the personnel to provide such information (i.e. a reflection of the improving professionalism within the sector). In addition, there was a belief that improvements in reporting by some charities encouraged or "forced" others to follow suit. However, it was accepted that the disclosure of some performance-related items remains relatively low in both annual reports and annual reviews.

6. Conclusions

The UK charity sector is significant numerically, socially and economically. It is a sector in which the fact and perception of accountability is particularly important, one in which good accountability is viewed as a basis both for reducing the potential for scandal and for breeding confidence which, it is argued, promotes increased giving and increased charitable activity. Many external stakeholders, including small individual donors, have information needs yet, because they normally have limited powers of interrogation, must primarily rely on communication channels such as annual reports, annual reviews and SIRs to meet those needs. The production of such documents is seen as a major part of the process of discharging accountability by charities to those outside its immediate management, particularly to stakeholders such as small donors. The provision of financial information, such as that contained in traditional financial statements, and of non-financial information, particularly performance information, is important to such external stakeholders. Drawing upon the findings of recently-published related empirical work (Connolly and Hyndman, 2013) and semi-structured interviews, this paper explored accountability from the perspective of donors.

This research offers evidence that while donors are viewed as the key stakeholder to whom a charity should be accountable (or, in the words of stakeholder theory, a salient stakeholder), the relevance of the information commonly disclosed in charity annual reports to their needs is questionable. These mandated reports, which are viewed by both small individual donors and large donors as having some, but possibly limited, relevance, are dominated by audited financial information. This however is perceived as being relatively less important and more difficult to understand (particularly by individual small donors) than performance-related information that is much less disclosed. As is seen from the interviews, large donors possess particular power and, as a result, can demand customised information, often relating to the projects that they fund. Their reliance on the annual report as a channel through which accountability is discharged is therefore more limited. It has been suggested that small donors, who do not possess the same power and often have no easily exercised right to demand information (and are therefore possibly less salient than large donors), must have their interests focused on in formal communications such as the annual report given that they normally have no easily exercisable right to receive information through other channels of communication. This reflects an argument to the fore in *The Corporate Report* (Accounting Standards Committee, 1975) and is echoed by both the Australian Accounting Research Foundation (1990) and the New Zealand Institute of Chartered Accountants (1993) when referring to dependent users. This research brings into question the relevance to all donors of charity annual reports and suggests a charity sector where accountability is not discharged in the most effective manner. This may be critical to dependent users (such as individual small donors), although less critical to non-dependent users (for example, large donors who possess and, as seen in this research, exercise powers of interrogation).

Notwithstanding the above, it was clear from the interviews that although the annual report is considered the most important channel of communication between a charity and its donors, it was rarely read in detail by donors (particularly small donors). Without entering the debate regarding the distinction between "interest of stakeholders", possibly as evidenced by widespread readership of annual reports by donors, and "stakeholder interest", perhaps facilitated by transparency and potential scrutiny by a few interested members, it is clear that the Charity Commission, in particular, considers the publication of annual reports as an important matter of accountability. It argues that such reports should have at their core the provision of "adequate information to allow stakeholders to assess the overall performance of the charity" (Charity Commission, 2004, p. 2). The research clearly shows that while both individual small donors and large donors do not particularly engage with the annual report, they view it as having significant importance. This suggests that the production and publication of the annual report, and its review by auditors and others, while possibly falling short of its accountability goal, serves as an important legitimising tool in the sector (enhancing trust and reputation).

This research, and the related Connolly and Hyndman (2013) work, also demonstrates that annual reviews (voluntary and less-formal publications than annual reports) are more aligned with donors' information needs. They contain a greater proportion of performance-related information (which is likely to be of considerable interest to small donors, who are dependent on formal channels of communications) compared with annual reports, and a much lesser proportion of traditional audited financial statement information (which is of very limited interest to many donors, particularly small donors). As a consequence, annual reviews have become the main means of discharging accountability to dependent small donors. Given this, perhaps there should be more direction and oversight in relation to the content provided in such documents. Such has the potential to curtail possible misrepresentation and gaming, and hence support the building of trust in the messages contained in annual reviews. With respect to this, a number of parties could have a part to play, including: the regulatory bodies (such as the Charity Commission) in steering and encouraging the development of a framework and providing some assurance indicators; the professional accountancy bodies by suggesting strategies to communicate potentially complex financial information in a summarised and meaningful way to financially-unsophisticated users; and organisations with a particular interest and focus on outcomes and impacts (such as New Philanthropy Capital – NPC) with respect to the provision and auditing of performance information. In particular, the research also suggests that much more could be done in providing meaningful communications through all channels on the "stories", outputs and impacts which are so central to donors' interests and which have the potential to connect them with the work.

While there remains a gap between donors' information needs and the information disclosed in annual reports and annual reviews of UK charities, research has shown that this relevance gap has closed over time (Connolly and Hyndman, 2013). This is an issue explored in the interviews. A possible explanation for this narrowing gap is the growing commitment of the UK Government to charity accountability, driven in part by a desire to see the donors' interests reflected in charity accounting requirements. This is shown in recent legislative changes, including making the SORP mandatory for many large UK charities. At the same time, it is likely that the growth of organisations (such as GuideStar, Intelligent Giving and NPC) which aim to raise public interest in charitable giving and help donors make informed giving decisions has focused charity attention on the importance of disclosing relevant information, particularly relating to performance.

If charities are to meet the information needs of donors, it would seem appropriate that more focused guidance and pressure relating to the production and disclosure of performance information should be provided by those concerned with the administration, control and support of the charity sector. For example, from organisations such as the Charity Commission, the National Council for Voluntary Organisations, the Charities Aid Foundation and the Charity Finance Group. This might include detailed recommendations, guidance and examples relating to the performance-related requirements of the Trustees' Annual Report (part of the SORP), and the pilot testing of common performance indicators in specific sub-sectors of the sector. To expect individual charities to develop meaningful and extensive performance reporting systems is perhaps optimistic. Some aspects of a framework for such guidance might be "read-across" from that existing in the UK public sector (where performance measurement and performance reporting issues have been to the fore for a number of years). However, as this research indicates, and particularly with respect to small donors, there is a need to link numbers (possibly as captured in key performance indicators) to "stories" in order to meet information needs adequately and engage appropriately with a key stakeholder group. As Hedley *et al.* (2010, p. 9) have emphasised in their NPC published analysis of performance, there should be "no numbers without stories" and "no stories without numbers".

The widespread adoption of appropriate accounting and reporting practices, and the ongoing renewal of such, has the potential to provide a basis for greater confidence in the control processes within charities and result in a more accountable and more legitimate sector. This is recognised by government, the charity regulators and those championing the sector's cause. Key in this process is an understanding of the information needs of donors, stakeholders who receive no direct economic benefit and, without whose support, charities could not function. This research illustrates that their prime interest is often in the cause which they fund and, at present, they have limited engagement with formal charity reporting channels. Nevertheless, donors stress the significance of trust relations and connect this to adherence to good accounting and reporting (with small donors frequently assuming, or hoping, that other interested parties play a scrutiny role).

The research reported in this paper is based on a small UK sample and is obviously not generalisable to all donors in all settings. However, while it seeks to open up a much-neglected area to investigation, further work is needed to build upon this study (possibly using larger numbers of interviews, surveys informed by initial interviews, case studies and different country settings). However, this paper offers initial critical insights into donors' motivations, information needs and abilities to understand formal reporting formats. As such, on an individual charity level, it can help to improve donor communication and donor trust. At a charity-wide level, it can provide a useful input to discussions by policy makers, standard setters and wider interested parties on future accounting and reporting formats for charities. Consequently, it supports the quest for a more legitimate, better managed, more accountable and healthier charity sector in the UK.

Notes

1. The UK consists of four separate countries (England, Northern Ireland, Scotland and Wales) within one main political unit.
2. The SIR now forms part C of the annual return that charities in England and Wales with an income over £1 million have to complete and submit to the Charity Commission. The public can view a charity's SIR from a link on its register entry. The SIR is designed for charities to provide an easily accessible summary of their key aims, activities and achievements.
3. SORPs are recommendations on accounting practice for specialised industries or sectors, and they supplement other legal and regulatory requirements. The first charity SORP was issued in 1988, with subsequent revisions in 1995, 2000 and 2005.
4. Although, as Kilcullen *et al.* (2007) highlight, other users, who often are not prioritised in such discussions, may be more likely to engage with aspects of charity reporting (particularly financial accounts).
5. These were selected using contacts provided by members of the joint SORP Committee of the Charity Commission (the regulator in England and Wales) and the Office of the Scottish Charity Regulator (one of the authors being a member of this committee).
6. It is of note that, in the interviews that are the focus of this paper, large donors displayed awareness of the SIR and had accessed it on occasions for information on particular charities; although it did not provide a major source of information for them. However, the small donors were not aware of its existence.

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