Jenny Carter
Director of UK Accounting Standards
Financial Reporting Council
8th Floor
125 London Wall
London
EC2Y 5AS

Sent electronically to ukfrs@frc.org.uk

77 Mansell Street
London
E1 8AN

29 March 2019

Dear Jenny,

FRED 71: Draft amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*

The Charity Commission for England and Wales, the Charity Commission for Northern Ireland, and the Office of the Scottish Charity Regulator act together as the joint SORP-making body for UK charities and are advised by the Charities SORP Committee.

The FRC's proposal of how an entity shall transition from defined contribution accounting to defined benefit accounting was considered by our SORP Committee at its last meeting. Our comments incorporate the views and advice we have received from this committee.

Historically, it has been common for entities in the charity sector to participate in multi-employer defined benefit pension plans. We are aware of a number of such plans where the administrator is unable to provide participating employers with sufficient information to use defined benefit accounting, resulting in charities currently accounting for the plan as if it were a defined contribution plan.

The invitation to comment acknowledges that some multi-employer defined benefit plans are now carrying out exercises in order to provide sufficient information to participating employers that will facilitate the use of defined benefit accounting. We understand this development is currently restricted to plans with participating employers in the social housing sector. However, there is a potential that the development will be reflected in other multi-employer defined benefit plans with participating employers in the charity sector. We therefore welcome this opportunity to offer feedback on amendments to FRS 102 that address a transition which will potentially impact a significant number of charities in the future. We also welcome the work undertaken by the FRC to address the transition by setting clear and unambiguous requirements, and acknowledge their attempts to reach pragmatic solution.

However, we are concerned that the suggested solution to the change in accounting presented in the Exposure Draft works less well for the charity sector. Our comments to the consultation questions report these concerns and explain the potential unintended consequences of the proposed treatment that are specific to the charity sector. We support a requirement for public benefit entities to adopt an alternative solution that we believe is more appropriate to the sector and the information needs of users of charities reports and accounts, but which still fits with the requirements of FRS 102 and promotes consistency amongst PBEs.

Yours sincerely,

Laura Anderson
Joint Chair of Charities SORP Committee
Head of Professional Advice & Intelligence
Office of the Scottish Charity Regulator

Nigel Davies
Joint Chair of Charities SORP Committee
Head of Accountancy Services
Charity Commission for England and Wales

Fiona Muldoon
Joint Chair of Charities SORP Committee
Monitoring and Compliance Manager
Charity Commission for Northern Ireland

Annex to Charities SORP-making body's response to FRED 71: Draft amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*

We have limited our response to the points on which we wish to place most emphasis, as well as those most relevant to the charity sector.

Question 1

Do you agree with the proposed amendments to FRS 102? If not, why not?

We do not agree with the proposed amendments to FRS 102. We acknowledge that the proposed treatment offers a pragmatic solution, however, our concern is that it will have a number of potential unintended consequences for charities.

The Charities SORP requires charities to prepare a statement of financial activities (SoFA). The SoFA is a single accounting statement that includes all income, gains, expenditure and losses recognised for the reporting period. It is analogous to a statement of comprehensive income in FRS 102.

The requirement for the adjusting entry to be recognised in other comprehensive income means that charities will have to present the entry within the '*other recognised gains/(losses)*' heading in the SoFA. This will impact the charities' '*net movement in funds*' for the period. As this figure shown at the bottom of the statement, it is commonly used by readers of the accounts to evaluate the performance of the charity. Users of the accounts may interpret the adjustment as being associated with the charity's current period's performance, rather than a consequence of a change in accounting treatment.

This treatment therefore risks being unhelpful to users of accounts in their interpretation of the entities' performance and may influence their funding decisions. This risk is exacerbated in the context of charitable entities, where the resources and financial knowledge of users of accounts can vary. Given the potential for the adjustment to distort the charity's performance for the current reporting period, the treatment may also cause confusion when comparing a charity's performance with prior periods or other entities.

We would encourage the FRC to revisit the proposed amendments and consider a requirement for public benefit entities to adopt an alternative treatment. We would recommend an alternative that requires entities to treat the transition as a change in accounting policy, with the adjustment in opening reserves for the earliest year the information is available. This is based on the transition to defined benefit accounting representing a change in accounting policy which should be recognised retrospectively in accordance with Section 10 of FRS 102. This treatment allows the transition to be clearly presented as not part of the entity's financial performance for the current reporting period and avoids creating unnecessary utility. For the reasons noted above, we consider the treatment to offer the most suitable solution for the charity sector which more appropriately reflects how charity's accounts are read, understood and interpreted. Whilst the FRC's aim for consistency in the accounting treatment for this transition is acknowledged, we believe this must be balanced with proportionate and practical solutions based on each sector's users' information needs.

We observe that the sector includes a significant number of charities that participate in multi-employer defined benefit plans but account for these plans as if they were a defined contribution plan. Therefore, these charities may transition to defined benefit accounting in the future and be affected by this change.

Question 2

In relation to the Consultation stage impact assessment, do you have any comments on the costs and benefits identified? Please provide evidence to support your views.

We agree with the expected benefits identified in the Consultation stage impact assessment.

We note the potential future costs for entities that participate in multi-employer defined benefit plans for which sufficient information to apply defined benefit accounting has previously not been available. Whilst outwith the scope of the proposed amendments to FRS 102, the costs associated with identifying and attributing participating employers underlying share of a plan's assets and liabilities may be significant.

The valuation of the employer's obligation under the plan is done for accounting purposes in order to meet the requirements of FRS 102. This information is calculated by the plan administrators and will represent a cost to employers. Whilst this represents an ongoing cost of compliance with FRS 102, it is expected that there will be additional charges incurred by the plan administrator in order to develop the methodology and obtain the necessary information to provide sufficient information in the first year of implementation. It is expected the administrator's set-up costs will also be passed onto employers and will represent a one-off cost associated with the transition.

We note that it has been common for small charities to participate in multi-employer defined benefits plan. These plans were previously popular amongst smaller entities due to the perceived financial benefits of sharing risks and controlling costs. Therefore smaller charities may be potentially impacted by the one-off and ongoing costs associated with this accounting change.