

Invitation to comment

Research exercise on charities SORP (FRS 102)

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Key facts

Subject of consultation:	A research exercise intended to identify necessary changes for the next Statement of Recommended Practice: Accounting Reporting by Charities (the Charities SORP (FRS102)).
Scope of this research exercise:	The invitation to comment sets out five areas of research where views are sought on how the next SORP could be improved. The aim is to identify any necessary changes in good time to prepare the next Charities SORP (FRS 102) with an Exposure Draft of the next SORP anticipated for 2018. The need for an Exposure Draft is likely to result from the planned triennial review of the accounting framework introduced by Financial Reporting Standard (FRS 102) applicable in the UK and the Republic of Ireland by the Financial Reporting Council (FRC). It is anticipated that the FRC's triennial review will be completed by 2018 with the exposure Draft SORP published shortly afterwards. It is expected that the next SORP would take effect from 2019.
Who should read this consultation:	Donors, funders, financial supporters, preparers, auditors and examiners of charity accounts, trustees, employees and beneficiaries of charities and others who may use charity accounts.
Period of consultation:	The consultation runs for 31 weeks from 4 May to 11 December 2016.
Secretariat:	Alison Scott, CIPFA.
How to respond to consultation:	<p>By email charities.sorp@cipfa.org</p> <p>By post Charities SORP, Attn. Matthew Allen, CIPFA, 77 Mansell Street, London, E1 8AN</p>
Additional ways to be involved:	SORP Consultation events will be held by sector and professional bodies as well as a number of free events held by accountancy firms. Events will be advertised on the SORP micro-site at www.charitySORP.org

<p>Getting to this stage and previous engagement:</p>	<p>The research proposals contained in this Invitation to Comment have been developed by the SORP-making body with advice received from a sector-based expert SORP Committee as a research exercise to be held through 2016. The SORP-making body last carried out a research exercise undertaken in 2008/9 which resulted in the publication: 'Charity Reporting and Accounting: Taking Stock and Future Reform'.</p>
<p>After the consultation:</p>	<p>A summary of the research consultation responses will be published in the second quarter of 2017. The responses and the feedback from consultation events will help us prepare the next Exposure Draft SORP. The Exposure Draft SORP is anticipated for 2018. An FRC consultation on changes to FRS 102 is anticipated in 2017 with any new standard likely to take effect for financial years beginning 1 January 2019.</p>

Foreword by the Joint Chairs

Why we are seeking your views now

The updating of UK-Irish Financial Reporting Standards (FRSs) is now on a three yearly cycle and so to be ready for a new FRS in 2019 we believe it is important to make an early start and listen to the views of the users of charity reports and accounts, practitioners, commentators and the accountancy profession based on their first year's use of the new Charities SORP (FRS 102).

If unfamiliar with the SORP framework or interested in the roles the SORP performs please refer to the Annex: Background to the SORP research exercise, for more information.

There are five areas identified for this research exercise on the Charities SORP (FRS 102). The aim is to reflect on the SORP as it now is and look ahead to how it needs to develop.

The five areas where your comments are sought

The joint SORP-making body and SORP Committee seek your views on five specific areas for potential SORP development:

- The SORP's structure, format and accessibility
- Implementation issues that require improvements to the SORP
- SORP Committee member suggestions for changes to the SORP
- Charity regulator themes for making changes to the SORP
- Your ideas for items to remove, change or add to improve the SORP

Responses are welcome on one or more of the areas identified. If responding to two or more areas, you may wish to submit your comments either as a single response or instead choose to submit a separate response for each section. All responses must be received by the closing date of 11 December 2016 if they are to be considered.

To help you identify those questions of interest to you, within each section we have attempted to group the questions by theme with those of more general interest first and those of more technical interest later. When responding, it is helpful to us if you say a little bit about your background so that we understand your perspective and please give your reasons for your views.

Your comments will be invaluable in helping us develop the next Exposure Draft SORP. The SORP Committee will be meeting in early 2017 to reflect on the consultation responses and will consider what changes to make when drafting the Exposure Draft of the next SORP in light of the consultation feedback. The next Exposure Draft SORP is likely to be issued in 2018.

Signed



A handwritten signature in black ink, appearing to read 'Nigel Davies'.

Nigel Davies
Chair



A handwritten signature in black ink, appearing to read 'Laura Anderson'.

Laura Anderson
Chair

Consultation questions

Section 3.1: The SORP's structure, format and accessibility

The Charities SORP (FRS 102) was a departure from previous SORPs. It was designed with individual modules (or chapters) for each topic. The modules were divided between 'core modules' that all users of the SORP must read and modules that need only be selected where they apply to the specific situation of the charity according to their constitution, structure and activities.

Each module has an introduction which explains what the module is about and details, in bullet points, the contents of a particular module. Charities are able to customise the SORP by answering a series of questions which then produce a tailored selection of modules. The new SORP was made available in hard copy and as a pdf download.

The design of the Charities SORP (FRS 102) was based on the conclusions of the earlier research conducted in 2008-09. The key findings of the research included:

- it was important for the SORP to be retained;
- the SORP should be written in an accessible style to assist smaller charities and to help them to more readily identify those requirements that are relevant to their circumstances; and
- the additional reporting requirements applicable to larger charities should be separately identified.

Q.1 Do you agree that the new format of the SORP meets the needs of all those preparing accounts using the SORP, including smaller charities? If not, what improvements should be made and why?

Q.2 Is more assistance required to help smaller charities? If so, please explain what is needed and why.

The 2008-09 research also indicated a need for the SORP to be clear about when a recommendation was a requirement and when the text of the SORP was offering advice on good practice or simply suggesting an approach to making a particular disclosure.

Each module deals with a particular accounting issue and sets out the applicable recommendations, distinguishing those that must be followed in order to comply with the SORP from those that should be followed as a matter of good practice or may be followed in order to provide relevant information.

Q3. Is the use of the terms ‘must’, ‘should’ and ‘may’ successful in distinguishing between those requirements that have to be followed to comply with the relevant accounting standard and the SORP from those recommendations which are good practice and those that simply offer advice on how a particular disclosure or other requirement might be met? If not, what alternative format should be adopted and why?

The FRC Policy on Developing Statements of Recommended Practice (SORPs) requires that the SORP-making body keep the need for a SORP under review. Both the SORP-making body and the FRC are keen not to over burden the charity sector and so it is important to confirm that the SORP is still required following the transition to the new GAAP standard FRS 102.

Q.4 Given the requirements for financial reporting that are now explained in FRS 102, is the retention of a SORP still necessary for the charity sector? Please give reasons for your answer.

Section 3.2: Implementation issues that require improvements to the SORP

The SORP-making body and the advisory Charities SORP Committee were keen to balance the competing requirements for a comprehensive SORP that provides sufficient guidance to users and additional help and support to smaller charities against the growing length of the SORP.

The SORP provides application guidance to FRS 102 and signposts to the relevant sections of FRS 102 throughout. In some areas the SORP repeats the requirements of FRS 102 but in others it simply refers the user to FRS 102 for example with respect to defined benefit pension scheme accounting, leases and complex financial instruments.

In writing the SORP there is always the risk of unintended ambiguity in the text. Also when applying the SORP practitioners may identify gaps where guidance is needed or requirements or recommendations of the SORP that prove problematic to follow in practice.

With the experience of using the Charities SORP (FRS 102) fresh in the minds of preparers of charity reports and accounts, we are keen to understand what the problem areas are.

Q.5 Do you have any suggestions as to the changes needed to address issues on implementation or in meeting the SORPs requirements? If so, please explain what they are and where possible please give examples.

Section 3.3: SORP Committee member suggestions for changes to the SORP

The SORP Committee members have considered the new SORP afresh and identified a number of issues that they believe merit reconsideration when the next Exposure Draft SORP is developed. Their comments cover both the report and the accounts.

A balance needs to be struck between adding new requirements, removing existing requirements and ensuring that the trustees' annual report and accounts do not become overlong. Section 3.5 asks you to consider what can simply be dropped or changed.

Reporting by the largest charities

- **An extra layer of reporting only for the very largest charities.** The responses to the 2015 consultation on the SORP Update Bulletin broadly supported a UK wide definition of larger charities at £500,000 (€500,000 Republic of Ireland). These larger charities have to provide the same level of information but it could be possible to identify additional reporting requirements that only apply to the largest charities.

The SORP Committee noted that the current SORP definition of larger charities draws a large number of charities into this greater level of reporting. The Companies Act reporting framework offers an alternative solution with three levels of reporting: small, medium and large (the option of reporting as a micro-entity is not available to charities in the UK.) Under this model the information supplied differs between small, medium and large with the highest level of disclosure restricted to the largest companies.

This would translate to charities with three tiers of reporting depending upon the income of the charity, for example this could be defined as: small up to £500,000, larger up to £10.2 million and largest above that. This approach could offer some simplifications for the intermediate sized charities currently included in the definition of larger charities.

- Q.6 Do you agree that there needs to be a third tier of reporting by only the largest charities and if so at what level of income should that reporting requirement apply?
- Q.7 If you agree that there should be a third tier of largest charities, what items in the existing SORP that apply to larger charities should be restricted to just these largest charities?

Trustees report / Narrative reporting

The 2008-09 research indicated support for the retention of the 'story' approach to the trustees' annual report and as a response to that feedback the new SORP emphasises the telling of the charity's story.

It is important that the SORP facilitates and encourages charities to explain their performance and report on their achievements. The SORP retained the approach taken previously by SORP 2005 and recommended that both qualitative and quantitative information on performance is provided as

good practice. The SORP was revised to take into account the principles of good impact reporting developed in collaboration by six sector-based organisations (New Philanthropy Capital, Association of Chief Executives of Voluntary Organisations, Charity Finance Group, the Institute of Fundraising, The SROI Network, National Council for Voluntary Organisations) in their report 'The Principles of Good Impact Reporting'

- **Better integration of the report with the accounts** – the report should be better linked to the accounts, drawing on material themes and demonstrating the difference the charity has made. Better reporting of operating results in the report should show the actual operating position for the charity. More guidance is needed to help preparers to tell their story, perhaps by providing them with guidance notes, prompts and best practice examples.
- **Detail of reporting** – given that there is plenty of detail which is required as part of the Trustees' Annual Report, a key area of concern is how to encourage preparers of accounts and professional advisors to cover these areas in sufficient detail to be helpful to the readers of the report and accounts, including funders.
- **Key facts summary** – given that the general public are interested in the annual report and accounts of a charity, it might be helpful to include a simple summary containing key information as an annex to the report. The content for this summary could be either charity specific items or a mix of mandated items (see section 3.4 for the charity regulators' ideas for what the mandated items could include) and charity specific items.
- **Reserves definition and guidance** – the new SORP states that larger charities should describe their reserves and approach to reserves more fully. This could now be revisited in light of themes arising out of the implementation of the new SORPs. Suggested additional guidance on reserves could cover the following areas: why reserves are held, possible reasons for using reserves, basis of calculation, and how reserves are expressed (thereby avoiding just a monetary amount being stated in the report).

Q.8 Do you agree with one or more of the four suggested areas for review of the trustees' annual report recommended by the SORP Committee? If so, which ones do you support and if you do not support any of these suggestions, please give your reasons as to why not?

The accounts (financial statements)

The Statement of Financial Activities (SoFA) is a single accounting statement that includes all income, gains, expenditure and losses recognised for the reporting period. It provides the user of the accounts with an analysis of the income and endowment funds received and the expenditure by the charity on its activities and presents a reconciliation of the movements in a charity's funds for the reporting period.

The 2008-09 research indicated wide support for the retention of the SoFA but in response to feedback and to improve the accessibility of the SoFA, the descriptors of income and expenditure were changed and governance costs were included as a separate component of support costs and disclosed in the notes to the accounts. A consequence of these changes was that it may not always be possible to match the expenditure of a particular activity with the related income from the information provided on the face of the SoFA.

- **SoFA – more specific definitions of support costs and fundraising costs.** There is scepticism about the purpose of separating “support” costs – especially as doing so encourages unhelpful comparisons and given that sector practice is inconsistent even though this category has been required since SORP 2005. Dropping this category altogether would be a simplification and thereby increase consistency across the sector. An alternative approach would be greater specification and guidance.
- **The mixture in the SoFA between ‘revenue’ and ‘capital’ items needs to be considered.** Capital funding is being recorded as income in the year of receipt and the depreciation on the relevant assets being charged as normal, resulting in huge fluctuations in reported results. From a funder’s perspective, it is often difficult to understand the ongoing surplus/deficit of a charity. Including an additional column in the SoFA for capital items e.g. fixed assets restricted/unrestricted column might offer better disclosure in this area but at the price of complexity. Some charities create a designated fund equal to the net book value of unrestricted assets to highlight how much is tied up in capital items. However, this information is only detailed in the notes to the accounts and perhaps should be more obvious on the face of the SoFA. Alternatively a combination of this and additional guidance on reserves may help to address the reporting issues of mixing revenue and capital items in the SoFA.

Q.9 Do you agree with either of the two suggested areas for the review of the accounts recommended by the SORP Committee? If so, which ones do you support and if you do not support any of these suggestions, please give your reasons as to why not?

Section 3.4: Charity regulator suggested themes for making changes to the SORP

The SORP-making body is made up of the Charity Commission for England Wales (CCEW) and the Office of the Scottish Charity Regulator (OSCR). The SORP-making body is responsible for developing each SORP in accordance with the Policy on Developing Statements of Recommended Practice (SORPs) published by the Financial Reporting Council (FRC).

The charity regulators consider the main purpose of the SORP is to meet the needs of the general purpose user of the report and accounts who is not in the position to demand additional information of the charity. The charity regulators acknowledge that they have the capability to collect additional information via annual returns or similar statutory reporting. Similarly large funders often include additional reporting requirements in their funding agreements, grant requirements, and/or contracts. In identifying their themes, the regulators believe that improving the reporting requirements of the SORP would better serve user needs and help raise public confidence and trust in charities.

The CCEW and OSCR consider, and where appropriate investigate, concerns about charities as well as issuing alerts and publishing guidance for charities on regulatory matters including charity governance and the duties of trustees.

The regulators’ themes cover both the report and the accounts. Respondents are invited to consider both the theme and the issues when making their response to the questions at the end of the section. A balance needs to be struck between adding new requirements, removing existing requirements and ensuring that the trustees’ annual report and accounts do not become overlong. Section 3.5 asks you to consider what can simply be dropped or changed.

Theme: making a difference for the public benefit

Statutory reporting requirements differ between jurisdictions as to the form and content of public benefit statements in the report. The SORP could offer a common approach. Knowing the difference a charity makes to its beneficiaries is arguably central to understanding a charity's effectiveness.

If you agree this theme deserves further consideration in the next SORP, the specific issues within this theme that you are asked to consider are:

- A greater emphasis on reporting public benefit reflected in a requirement that the report explains who the charity helps. All charities could be explicitly asked to explain who the beneficiaries are that the charity seeks to serve.
- Whether the beneficiaries are involved in service design. Charities could explain how the charity's beneficiaries were involved in identifying the significant activities to be undertaken and the nature of those activities.

Theme: risk management

The Charities SORP (FRS 102) already requires larger charities to describe the principal risks and uncertainties facing the charity and its subsidiary undertakings that have been identified by the charity trustees, together with a summary of their plans and strategies for managing those risks (paragraph 1.46). The new governance code published by the FRC for UK listed companies is similar, it includes a provision that the annual report should describe the principal risks and explain how they are being managed or mitigated. The code also specifically asks directors to report on how they reviewed the effectiveness of internal financial controls.

If you agree this theme deserves further consideration in the next SORP, the specific issues within this theme that you are asked to consider are:

- Whether all charities be required to advise if the reserves are sufficient to avoid service disruption to the charity's beneficiaries.
- Whether all charities be required to explain what assurance they have that the charity's internal financial controls are operating effectively and state when they last carried out a review of the effectiveness of internal financial controls.
- Larger charities be required to explain how the charity manages the risk of fraud and whether fraud is an item on the corporate risk register.
- Larger charities be required to explain how the charity ensures effective governance arrangements are in place to identify and manage conflicts of interest, ensure sound decision-making, and ensure adequate oversight of decisions delegated to staff.

Theme: going concern

The Charities SORP (FRS 102) already requires disclosure in the notes to the accounts where there are material uncertainties about the charity's ability to continue as a going concern (paragraph 3.38). The new governance code published by the FRC for UK listed companies goes further and requires a 'viability statement' over a longer term timeframe than 12 months. With defined benefit pensions representing potentially very significant long term liabilities, greater transparency for charities could be helpful with specific reference to these liabilities.

If you agree this theme deserves further consideration in the next SORP because charity financial viability is a key issue, the specific issues within this theme that you are asked to consider are:

- All charities could be required to explain why the charity is a going concern.
- Where there are material uncertainties as to going concern, a requirement on all charities explain their plans for addressing these uncertainties.
- Pensions remain a matter of concern - all charities could be required to provide more discussion of the implications of pension liabilities as part of their going concern disclosures.
- Where there are uncertainties about going concern all charities could be required to provide disclosure in the report as a 'must' not a 'should' (paragraph 1.23).

Theme: enhanced analysis of expenditure

Research conducted by IPSOS-MORI in 2012 for the Charity Commission identified considerable public interest in staff and administrative costs incurred by charities. IPSOS-MORI also found that the overwhelming majority of people surveyed believed that charities should provide the public with information on how they spend their money and how they benefit the public.

The research indicated that the public may see these costs as a proxy measure of a charity's impact. The traditional focus of the SORP has been on encouraging the reporting of the difference the activities of a charity make to its beneficiaries in order to demonstrate the impact of their work rather than focussing on particular types of spending that prove hard to define in a uniform way. The consistent interest of press and public is in distinguishing how the money was spent in charitable terms and other types of spending.

If you agree this theme deserves further consideration in the next SORP, the specific issues within this theme you are asked to consider are:

- the SORP might be more explicit in defining administrative and fundraising costs
- Identifying charitable expenditure outside of jurisdiction of main registration. There are issues around (i) which countries charities operate in and (ii) how much they spend in these countries. The public, regulators and stakeholders have an interest in understanding how much money charities are spending overseas each year and in which countries charities operate.
- Executive pay disclosures – increasing the requirements with consideration given to implementing the NCVO proposals for larger charities (England and Wales) to disclose the post and pay level of all senior employees.
- Staff pay disclosures – tightening definitions to cover the cost of interim staff or agency or similar staff covering specific senior management roles in the charity. The SORP does not currently cover these arrangements (see module 9 paragraph 9.26 to 9.28).

Theme: disclosure of who funds a charity

Information about who funds the charity was identified as of interest to funders in the SORP research carried out in 2008-09 and in responses from the Republic of Ireland to the consultation on the Exposure Draft of the SORP in 2013 regarding government funding of charities.

If you agree this theme deserves further consideration in the next SORP, the specific issues within this theme that you are asked to consider are:

- All charities could identify by name and amount any material individual/ corporate/ government/ organisation donations and/or contracts.
- Disclosing for whom is the charity acting. The report/accounts must disclose if the charity has been a party to any agency or consortia arrangements in the year (see module 19, paragraph 19.12 for current disclosures) but in addition a requirement could be added to explain how these arrangements supported the key objectives of the charity and who each party is.

Theme: disclosure of key facts

The charity regulators support the SORP Committee's proposal that a key facts section be included in the report. In terms of what might be included, if you agree with this theme, the specific issues within this theme that you are asked to consider are:

- Charitable expenditure. All charities could be required to include a prominent statement of total charitable expenditure in the year;
- All charities could include the figure for total gross income in the year received/receivable to the charity/parent charity in their key facts;
- Fundraising materials often quote pence in the pound making it to the end beneficiary/charity so should charitable expenditure as a proportion of total income be expressed as a percentage and the equivalent pence in the pound. To be meaningful the calculation would need to reconcile to the accounts.

Q.10 Do you agree with one or more of the six themes for review of the SORP suggested by the charity regulators? If so, which themes do you support, or if you do not support any of these suggested themes, please give your reasons as to why not?

Q.11 If you do support one or more of the suggested themes, which, if any, of the specific issues identified within each theme do you agree needs attention in the next SORP? Alternatively, if you do not support any of these suggested issues, please identify the issues that need to be addressed and explain your reasons why?

Section 3.5: Your ideas for items to remove, change or add to improve the SORP

The SORP requires certain disclosures in charity accounts that are additional to the requirements in accounting standards. These additional disclosures are aimed at providing additional information to donors, funders, financial supporters and other stakeholders about a charity's activities and expenditure.

The SORP research exercise is an opportunity to stand back and consider which elements of the existing report and accounts might be dropped or amended to improve information to users of the report and accounts.

- Whilst it is important for the SORP to be comprehensive, it would be possible to identify details of disclosure requirements in different ways, for example by making use of cross references to standards or to a separate appendix providing a listing of disclosure requirements.
- You have seen the ideas of the SORP Committee and the charity regulators have for changes or additions to reporting so now we are seeking your views:

Q.12 Are there any items in the report or accounts which could be removed. If so, what are they and what are your reasons for removing them?

Q.13 Are there any items in the report or accounts which could be changed to improve the information provided to the user? If so, which items would you change, what would the change be, and how would it improve the information to users of the report and accounts?

Q.14 Are there any items you would like to add in to the report or accounts? If so, what are these items and how would their inclusion help the user of the report and accounts?

The accountability to donors and funders for the funds held and used by charities is the major reason for greater disclosure in charity accounts compared to similarly-sized private commercial companies. However, it is also important that the information that the SORP requires charities to provide in their accounts is helpful to the user of the accounts and for unnecessary requirements to be avoided.

Although the SORP-making body cannot remove any requirements that are set by FRS 102 because it cannot over-ride the specific accounting requirements or disclosures of accounting standards, your responses will provide evidence to assist the SORP-making body respond to the FRC's triennial review of FRS 102.

Q.15 Are there any disclosures in the notes to the accounts that you believe can simply be removed altogether? If so please state the disclosure, the relevant SORP paragraph(s) and give your reasons as to why this disclosure is not useful to the user of the report and accounts?

SECTION 4

Summary of the consultation questions

- Q.1 Do you agree that the new format of the SORP meets the needs of all those preparing accounts using the SORP, including smaller charities? If not, what improvements should be made and why?
- Q.2 Is more assistance required to help smaller charities? If so, please explain what is needed and why.
- Q.3 Is the use of the terms 'must', 'should' and 'may' successful in distinguishing between those requirements that have to be followed to comply with the relevant accounting standard and the SORP from those recommendations which are good practice and those that simply offer advice on how a particular disclosure or other requirement might be met? If not, what alternative format should be adopted and why?
- Q.4 Given the requirements for financial reporting that are now explained in FRS 102, is the retention of a SORP still necessary in the charity sector? Please give reasons for your answer.
- Q.5 Do you have any suggestions as to the changes needed to address issues on implementation or in meeting the SORPs requirements? If so, please explain what are they are and where possible please give examples.
- Q.6 Do you agree that there needs to be a third tier of reporting by only the largest charities and if so at what level of income should that reporting requirement apply?
- Q.7 If you agree that there should be a third tier of largest charities, what items in the existing SORP that apply to larger charities should be restricted to just these largest charities?
- Q.8 Do you agree with one or more of the four suggested areas for review of the trustees' annual report recommended by the SORP Committee? If so, which ones do you support and if you do not support any of these suggestions, please give your reasons as to why not?
- Q.9 Do you agree with either of the two suggested areas for the review of the accounts recommended by the SORP Committee? If so, which ones do you support and if you do not support any of these suggestions, please give your reasons as to why not?
- Q.10 Do you agree with one or more of the six themes for review of the SORP suggested by the charity regulators? If so, which themes do you support, and if you do not support any of these suggested themes, please give your reasons as to why not?

- Q.11 If you do support one or more of the suggested themes, which, if any, of the specific issues identified within each theme do you agree needs attention in the next SORP? Alternatively, if you support none of these suggested issues, please identify the issues that need to be addressed and explain your reasons why?
- Q.12 Are there any items in the report or accounts which could be removed. If so, what are they and what are your reasons for removing them?
- Q.13 Are there any items in the report or accounts which could be changed to improve the information provided to the user? If so, which items would you change, what would the change be, and how would it improve the information to users of the report and accounts?
- Q.14 Are there any items you would like to add in to the report or accounts? If so, what are these items and how would their inclusion help the user of the report and accounts?
- Q.15 Are there any disclosures in the notes to the accounts that you believe can simply be removed altogether? If so please state the disclosure, the relevant SORP paragraph(s) and give your reasons as to why this disclosure is not useful to the user of the report and accounts?

SECTION 5

The consultation process and how to respond

How the SORP is developed

The issues and themes raised in the invitation to comment on Charities SORP (FRS 102) have been drafted by the Charity Commission and the Office of the Scottish Charity Regulator as the joint SORP-making body for charities with advice received from its sector-based expert SORP Committee.

The responses received to this consultation and the feedback provided at consultation events will be analysed and carefully reviewed by the joint SORP-making body and the SORP Committee. The feedback received will be used to inform the development of a future Exposure Draft Charities SORP (FRS 102).

The research exercise will also inform the annual review of the SORP to assess how it is being applied and to ensure its continued consistency with accounting standards.

How to respond to this consultation

A summary of the questions in this consultation is set out in section 4 of this invitation to comment.

The closing date for responses is **11 December 2016**. You can respond by:

Email to charities.sorp@cipfa.org or

Post to Charities SORP,
Attn. Matthew Allen
CIPFA
77 Mansell Street
London, E1 8AN

Please tell us in what capacity you are replying, for example as a charity trustee, volunteer treasurer, member of a charity's staff, charity auditor, independent examiner, umbrella body or representative group, user of charity services, funder or simply as a member of the public. All responses will be acknowledged although it will not be possible to give substantive replies to each response we receive.

Confidentiality

In accordance with the code of practice on open government and the FRC's Policy on Developing Statements of Recommended Practice comments submitted will be made publicly available. If you want your response to be treated as confidential, it would be helpful to us if you could briefly explain why you regard the information you have provided as confidential. If you are replying by e-mail, please make it clear in the body of your response if you wish your comments to be treated as confidential and why.

We will take full account of your explanation but we cannot give an assurance that confidentiality can be maintained in all circumstances.

ANNEX:

Background to the SORP research exercise

The Charity Commission for England and Wales (CCEW) and the Office of the Scottish Charity Regulator (OSCR) are the joint SORP – making body for charities and publish the Statement of Recommended Practice: Accounting and Reporting by Charities (the SORP). The SORP applies to charities preparing accounts under UK-Irish Generally Accepted Accounting Practice (GAAP) to present a ‘true and fair view’. For financial years beginning on or after 1 January 2016 a single SORP applies: ‘Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland’ also known as the Charities SORP (FRS 102).

Reporting by charities is different to the for-profit and government sectors. This difference is partly due to charity law requirements regarding fund accounting but is mainly because the users of the trustees’ annual report (the report) and accounts have particular needs. The SORP provides a standard framework for charities to tell their story well which is transparent and accountable and informative to the users of the report and accounts.

Since the development of the SORP was entrusted to the charity regulator(s), the SORP has developed to meet the requirements of UK Generally Accepted Accounting Practice (GAAP) and the requirements of the user of the accounts. In the past the SORP has been issued periodically in 1988, 1995, 2000, and 2005 with the latest SORP taking effect from 2015. The planned triennial review of the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102) by the Financial Reporting Council (FRC) is likely to conclude by 2018 and any changes to GAAP necessitate changes to a SORP that applies GAAP. It is therefore timely to run a SORP research exercise to co-ordinate changes required to meet user needs for stewardship information with any changes required by GAAP.

The demands for stewardship information are shaped by the context in which charities operate, the range of activities charities undertake and the changing expectations of funders, financial supporters, donors and other stakeholders. This research exercise is a further step in the continuing evolution of the SORP to meet the financial reporting needs of the charity sector.

The joint SORP-making body last undertook major research in 2008-09 to obtain the views of users of the current SORP. Over 1,000 people took part representing of charities, charity funders, auditors and independent examiners. The 2008-09 research was only conducted within the UK but with the establishment of the Charity Regulatory Authority in the Republic of Ireland this latest exercise will cover the UK and the Republic of Ireland.

In framing the research exercise it is important to consider:

- Who are the users of charity reports and accounts?
- Purposes served by the SORP
- The SORP framework
- The coverage of the SORP

Who are the users of charity reports and accounts?

The 2008-09 SORP exercise concluded that although funders were a significant user group, they were not the only group interested in financial reporting by charities. The Charities SORP (FRS 102) recognises this and states, in paragraph 12:

‘Although past, current and potential funders, donors and financial supporters of a charity are the primary audience for the financial information contained in a charity’s report and accounts, the preparer should also be aware that interest in this information may also extend to a charity’s service users and other beneficiaries’.

The research is therefore conducted in this spirit so that respondents are asked to consider the users of the report and accounts when framing their responses and to justify changes with their users in mind. In the web era charity reports and accounts are readily accessible and some charity regulators post them free to view on their register pages. This means that charities may be unaware of the true extent to which their reports and accounts are read and used.

The FRC anticipates the financial statements (accounts) are there to serve the general purpose user who lacks the capability to require/impose specific additional reporting. The SORP-making body extends this approach to the report and accounts. This means that regulators and expert donors making material grants can be expected to obtain extra information, where required, in addition to the information provided by the report and accounts.

The SORP framework

The SORP supplements accounting standards and other legal and regulatory requirements to reflect the special factors prevailing or transactions undertaken in the charity sector. The SORP is developed in line with the FRC’s Policy on Developing Statements of Recommended Practice (SORPs). Prior to the SORP being issued, it is subject to review by the FRC and when issued carries a statement confirming, as appropriate, that the SORP does not appear to contain any fundamental points of principle that are unacceptable in the context of current accounting practice or in conflict with an accounting standard or undermine the FRC’s wider objectives.

Before a new SORP is issued, an Exposure Draft must be subject to a wide consultation which should include organisations and individuals in the sector concerned and the accountancy professional bodies, auditors and advisers actively involved in the sector.

The proposals contained in each Exposure Draft of the SORP are developed with advice received from a sector-based expert SORP Committee. The SORP Committee’s membership is drawn from charity finance directors, charity auditors, academics and charity advisers. The Committee is also structured to reflect the different jurisdictions covered by UK-Irish Generally Accepted Accounting Practice (GAAP) which have an established independent charity regulator. All the charity regulators participate in the SORP-making process.

Charities that prepare their accounts on an accruals basis to give a true and fair view must follow the accounting standards that constitute UK-Irish GAAP.

In particular, FRS 102 which is issued by the FRC addresses a number of issues specific to public benefit entities in a specialised activities section.

In developing an Exposure Draft of the SORP, the joint SORP-making body and its advisory SORP Committee place significant weight on the available research concerning the views of the public and other stakeholders on the current SORP and on how it could be improved.

Purposes served by the SORP

Firstly: raising the standards of reporting and accounting is an objective of the FRC and is an expectation on SORP-making bodies in the FRC's Policy on Developing Statements of Recommended Practice (SORPs). CCEW and OSCR fully endorse this objective. The SORP differentiates the requirements that apply to all charities irrespective of size, from those additional disclosures required of 'larger charities'. Larger charities are defined as charities with an income exceeding £500,000 (UK) and €500,000 (Republic of Ireland).

Secondly: for-profit accounting standards do not cover narrative reporting or all the areas of interest to the stakeholder groups relevant to charity reporting and so the SORP does this. General purpose financial statements aim to provide information to stakeholders to inform economic decision-making.

Thirdly: the SORP provides sector specific guidance on the application of GAAP and provides additional interpretation, disclosure, illustrations and explanations specific to the sector to help preparers compile accounts compliant with GAAP. Our sector, with a predominance of comparatively small organisations, is reliant on volunteers and so has particularly high needs for this support.

Fourthly: there are omissions in GAAP due to some charity specific issues being absent from standards, the primary one being fund accounting. For-profit standards reflect company law financial statement formats and regulatory requirements. The SORP sets out the specific performance statement for charities – the Statement of Financial Activities (SoFA) and additional reporting necessary for charities. The inclusion in FRS 102 of public benefit entity specific items was a very welcome development with significant areas now included within standards for the first time.

Lastly: influencing practice to a degree overlaps with raising the standards of reporting and accounting. Influencing practice is more proactive as it involves taking in new ideas or emerging practice and making it mainstream, for example risk reporting, and it is also responsive in terms of meeting new demands for disclosure, for example executive pay. It can be pro-active if new areas of reporting are anticipated and developed.

The coverage of the SORP

- a) **Geographical:** the SORP is supported by regulations in the charity law jurisdictions of Scotland, England and Wales, and Northern Ireland. The SORP is currently followed on a voluntary basis in the Republic of Ireland.

The SORP is not the guidance of a particular charity law jurisdiction and in drafting Charities SORP (FRS 102) the SORP-making body was keen to ensure that it was jurisdiction neutral. Content that is prescribed by regulation or by charity law in a particular jurisdiction is clearly identified and separate from the SORP's recommendations that apply across all charity law jurisdictions.

In framing the research, the SORP-making body and charity regulators of all four jurisdictions are seeking to identify issues or matters which are common in some degree to all four charity

law jurisdictions. Although the degree of emphasis may differ, it is the matters which are in common which the SORP will address. Matters that affect a single jurisdiction only are useful to identify and will be referred to the relevant body that makes regulations for that jurisdiction for their consideration.

- b) **Topics:** the SORP covers the trustees' annual report (the report), the charity specific performance statement – the SoFA – and provides guidance on the balance sheet, statement of cash flows and also on the income and expenditure account required of charitable companies. The SORP sets out requirements and provides guidance on the notes to the financial statements (accounts).

Where the SORP requires more than FRS 102, this requirement is prefixed by 'this SORP requires that all charities/larger charities must'. This ensures that the user can distinguish the requirements of FRS 102 from those extra requirements made by the SORP.



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