

Discussion Paper

To: Charities SORP Committee

From: Alison Bonathan, CIPFA Secretariat

Date: 2 March 2022

Subject: Tiered Reporting in the Charities SORP

Purpose

The purpose of this discussion paper is to summarise discussions to date on the number of, and thresholds for, tiers in the Charities SORP to facilitate decision-making on tiers.

Report

1. Introduction

- 1.1 Following its discussions of the approach to the drafting phase for the next Charities SORP, at its meeting on 26 January 2022 the Charities SORP Committee decided to:
- hold an initial conversation about tiered reporting at the first meeting of the drafting stage (subject to the FRC's response to the SORP-making body's submission to the FRC Periodic Review), then
 - discuss the specifics of tiered reporting for each of the 15 topics selected for review at later meetings in the drafting stage as the topic groups are considered.
- 1.2 The Charities SORP Committee debated the number of tiers and thresholds for the tiers at its meeting on 27 May 2021. These discussions were informed by a summary of the Engagement Strands' reports.
- 1.3 This Discussion Paper summarises work to date to facilitate debate on the number of tiers and the thresholds for those tiers to feed into the Charities SORP drafting process.

2. Current Position

- 2.1 Per paragraph 1.9 of the Charities SORP there are currently two tiers - 'all charities' and 'larger charities' (income over £500,000 (UK) or €500,000 (ROI)) with more reporting requirements applying to 'larger charities'.
- 2.2 The following set out the main simplifications for the reporting differences between 'all' and 'larger' charities in respect of:

- the trustees' annual report, there are significant simplifications with less detail required (see module 1)
- the accounts, there is an option for a 'natural' SoFA (module 4), the Statement of Cash flows is optional (module 14)
- the notes to the accounts, there are only a few: analysis of staff costs if using natural categories (module 9), group accounting (module 24) and related treatment of associates (module 28) and joint ventures (module 29).

2.3 There is currently uncertainty over how far, if at all, the changes requested in the SORP-making body's two submissions to the periodic review will be accepted and, if accepted, the changes that will be made to FRS102. This has significant implications for the scope for simplification and having tiered reporting requirements. The changes requested were in respect of:

- a request for the joint SORP-making body have more latitude in the application of Section 1A
- greater flexibility in formatting primary performance statements (SoFA)
- latitude in requiring comparatives for SORP specific items
- flexibility to frame disclosures in a manner that the reader is expected to understand
- simplification to defined benefit pension disclosures.

To date, Engagement Strands and Committee Members have been asked to assume the FRC will grant flexibility to accommodate tiered reporting within the Charities SORP.

3. Engagement Strand Feedback

- 3.1 All the engagement strands appeared to favour some form of tiered reporting to ensure that reporting is proportionate. However, there did not appear to be a consensus on either the number of tiers or the thresholds for the tiers.
- 3.2 Of the many options considered by the Engagement Strands, the feedback seemingly indicated a tendency towards three tiers. Two engagement strands (of the five who submitted a report) appeared to be supporting this approach with a majority view. However, there does not appear to be an overwhelming consensus on this approach.
- 3.3 Some commentaries from the Engagement Strands also considered that there were substantial benefits to a modification of a 2-tiered approach currently in the Charities SORP (known as a modified 2-tier approach) but setting the income threshold at £/€1million. This view was the preferred solution of the Smaller Charities and Independent Examiners Engagement Strand. Using the modified 2-tier approach also had the advantage of using the current structure of the Charities SORP so improving understandability and limiting confusion and complexity.
- 3.4 It was noted that more choice risks making compliance with the tiered reporting structure more complicated.
- 3.5 There was no explicit agreement for the thresholds at which the tiers should be set (though there were frequent references to specific amounts). Several of the strands indicated that £1m would be a useful level. Support was also given for more concessions to be given to smaller charities and therefore tiers should be introduced at below £250k and between £250k and £1m.
- 3.6 Several strands referred to using the Companies Act 2006 tiers based on size, though it was recognised that the Companies Act 2006 thresholds would include criteria other than income levels. Annex A outlines the Companies Act 2006 requirements to qualify as a small company.

- 3.7 The Larger Charities Engagement Strand questioned whether tiers should be based on different types of income, for example cash donations. Professional and Technical Engagement Strand (A) suggested that a pragmatic solution based on income should be used but with a possible override for complexity.
- 3.8 Professional and Technical Engagement Strand (B)'s report included a comment about ensuring that charities do not move in and out of thresholds on a regular basis and that stability should be built into the framework.

4. Key points from Charities SORP Committee discussion from meeting held on 27 May 2021

- 4.1 The Charities SORP Committee expressed a preference for **three** tiers with a new tier for the largest charities.
- 4.2 Some support was shown for allowing receipts and payments accounts for charities under the £/€250k threshold.
- 4.3 It was agreed that the more tiers there are, the more complicated and confusing that the prospective Charities SORP might be.
- 4.4 The Charities SORP Committee commented that smaller charities would benefit from simplification of the reporting requirements of the Charities SORP. Further, larger charities are best equipped to deal with complexity and any changes in the tiers.
- 4.5 A Charities SORP Committee member noted that movement between the tiers currently relies on income in an individual year, therefore consideration could be given to changing this, so a charity meets the condition of the new tier after being at the relevant income level for two years. The Chair indicated that the point would be considered, as it needs detailed thought (for example, consideration of the requirements in the different jurisdictions).

5. Other Considerations

- 5.1 Commentaries both from the Engagement Strands and Charities SORP Committee Members touched on the potential benefits of aligning tiers with Companies Act 2006 requirements, and the potential from confusion in the absence of such alignment. As noted above, Companies Act 2006 thresholds would include criteria other than income levels. The Charities SORP thresholds are currently based solely on income level. Income level is therefore an established method of delineating accounting requirements across the jurisdictions and is therefore familiar to charities. Further, all regulators have data on income levels for all charities so they can accurately gauge the numbers of charities in various brackets for regulatory and decision-making purposes.
- 5.2 Commentaries both from the Engagement Strands and Charities SORP Committee Members referred to the BEIS consultation on *Restoring trust in audit and corporate governance*. A Government response to this consultation is still forthcoming. However, one point under consultation was the possibility of larger charities (and other third sector entities) meeting the definition of Public Interest Entities. The threshold that was under discussion associated with this proposed reform was £100m or higher.
- 5.3 Several Engagement Strands suggested that a decision tree should be included in the Charities SORP to support charities when determining which requirements to apply. Alternatively, a digital solution could be developed to facilitate decisions around tiers for charities and which would only present the modules of the Charities SORP relevant to an individual charity.

6. Numbers of charities affected

- 6.1 Feedback from both the Engagement Strands and the Charities SORP Committee frequently indicated that the threshold for smaller charities should be set at £/€250k, although support for this was not unanimous. There was less agreement on the appropriate threshold to distinguish 'medium' from 'large' charities. The debates at the Charities SORP Committee referred to thresholds set at around £1m. However, this threshold was not subject to the same amount level of debate as the 'small' charities' threshold and there was therefore less of a clear consensus.
- 6.2 To assist the Charities SORP Committee with its deliberations the following data (as at 22 February 2022) indicates the number of charities in various income brackets, split by jurisdiction.

Income band	CCEW	OSCR	CCNI	Total	% of Charities
Less than £250k	150,999	20,460	5,409	176,868	87.2%
£250k - £1m	12,032	1,756	1,052	14,840	7.3%
Over £1m	7,606	1,566	231	9,403	4.6%
on register but no income disclosed		1,666		1,666	0.8%
Total	170,637	25,448	6,692	202,777	100.0%

7. Emerging thoughts of the joint SORP-making body

- 7.1 To help facilitate discussion at the meeting of the Charities SORP Committee, the joint SORP-making body has provided its emerging thoughts for the number of tiers and the thresholds for each of those tiers. These thoughts are provided solely to assist debate.
- 7.2 The joint SORP-making body consider that:
- there could be three tiers – small, medium and large for ease of reference.
 - thresholds would be based on income, given that charities are already familiar with this approach.
 - £250k could be an appropriate threshold to distinguish small from medium charities.
 - £1m or £3m could be an appropriate threshold to distinguish medium from large charities.
 - Data on the number of charities that would be included in each tier should be considered when determining the thresholds for the tiers.

The Charities SORP Committee is invited to consider the views expressed by the various parts of the engagement process and the joint SORP-making body on the number of tiers and thresholds for the tiers. In particular, the Charities SORP Committee is invited to make decisions on the following:

- **Does the Charities SORP Committee still agree that there should be three tiers in the Charities SORP (subject to the decisions of the FRC), or do they consider that fewer tiers may be less complex?**
- **What should the thresholds for each of the tiers be?**
- **Should thresholds for each of the tiers be based solely on income, as in the current Charities SORP, or should consideration be made of other criteria, such as those used in Companies Act 2006 (See paragraph 3.6 and Annex A)?**
- **Should the Charities SORP include measures to avoid charities moving too frequently between tiers per the comments in paragraphs 3.8 and 4.5 above? What form should these measures take eg meeting thresholds for more than one year?**

Companies Qualifying as Small Under the Companies Act 2006

Section 382 of the Companies Act 2006, specifies that a company would be classified as small in a year in which it satisfies two or more of the following requirements:

- Turnover not more than £10.2m
- Balance sheet total not more than £5.1m
- Not more than 50 employees.

Additionally, in relation to a subsequent financial year, where on its balance sheet date a company meets or ceases to meet the qualifying conditions, that affects its qualification as a small company only if it occurs in two consecutive financial years.