

## **SORP Committee**

### **Minutes of the SORP Committee Meeting of October 19 2007 (Approved at the November 23 2007 SORP Committee Meeting)**

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Present:

Andrew Hind, Chair of the SORP Committee  
Kirsty Gray, Deputy Chair of the SORP Committee  
Debra Allcock Tyler  
Tidi Diyan  
Pesh Framjee  
Peter Gotham  
John Graham  
Chris Harris  
Noel Hyndman  
Ray Jones  
Tristan Lumley  
Carol Rudge  
Kate Sayer  
Catriona Scrimgeour  
Paul Spokes

In attendance:

Ken Brew, Principal Accountant, Charity Commission  
Nigel Davies, Secretary to the SORP Committee  
Alan O'Connor, Accounting Standards Board

Apologies:

Keith Hickey

#### **Item 1: Chairman's opening remarks and matters arising**

1.1 The Chair opened the meeting by advising that Claire Newton had stood down from the SORP Committee following her taking up a post outside the charity sector. The committee unanimously expressed to Claire their good wishes. The Chair advised that Lynne Robb, Executive Director of Finance, IS, and Property at Cancer Research UK, who was the reserve candidate in last year's SORP Committee recruitment exercise, had agreed to join the Committee. Formal clearance for the appointment would be sought from the Accounting Standards Board (ASB).

## **Item 2: Approval of the minutes and matters arising**

2.1 The minutes of the meeting of the 12 April 2007 were considered and approved with two minor corrections. The word 'of' was added to paragraph 3.6 so that the final sentence included the phrase 'date of acquisition'. The word 'a' was deleted in paragraph 4.2 second bullet point so that the sentence now included the phrase 'for those charities'.

2.2 There were no matters arising not covered by the agenda.

## **Item 3: 'Update on heritage assets'**

3.1 Alan O'Connor provided a verbal update on the progress of the draft accounting standard on heritage assets. Since the April SORP Committee meeting the ASB Board had met twice to consider the responses to the Financial Reporting Exposure Draft (FRED40) consultation and would be returning to this issue in their November meeting.

3.2 The ASB Board was concerned that the consultation responses indicated that the definition of a collection might lead to Institutions classifying their entire holdings as a single collection. The Board also wished to avoid a return to the "all or nothing" approach to recognition and valuation proposed in the Discussion Paper and emphasised the importance of the enhanced disclosures proposed in both the Discussion Paper and FRED40.

3.3 The ASB has considered a paper identifying a number of alternative approaches to the recognition of heritage assets, ranging from a requirement to recognise and value all assets through to a total prohibition on recognition and valuation. The Board has asked for further consideration of an approach that requires recognition but retains a test of practicality applied to determine whether valuation is possible. A reworked Exposure Draft will be prepared for the Board's November meeting with the proposals likely to be subject to further consultation.

3.4 The ASB noted the research project being taken forward by Kingston University, in partnership with HM Treasury and the Royal Institute for Chartered Surveyors, and the Discussion Paper entitled "Valuing our Heritage" that was published in August 2007.

#### **Item 4: Statement of Principles**

4.1 Ray Jones introduced a paper considering the implications of the ASB Interpretation for Public Benefit Entities of the Statement of Principles for Financial Reporting (the Interpretation) published in June 2007. The Interpretation, whilst not over-riding the SORP or accounting standards, does provide a framework for considering any issues not at present addressed by the SORP and any significant inconsistency between the two documents would need to be considered in the context of a future revision of the SORP.

4.2 The SORP and the Interpretation were compared in the following key areas:

- The Interpretation's treatment of multi-year grants was consistent with the SORP and distinguishes between performance related grants and grants arising from constructive obligations that are recognised as liabilities at the time the commitment is made.
- Differing residual interests such as restricted funds are disclosed under SORP by differentiating the separate funds of a charity within the balance sheet. This approach is fully consistent with the Interpretation.
- The Interpretation's treatment of designations whilst not inconsistent with the SORP has a difference in emphasis. Both the Interpretation and the SORP do not consider designations to represent a separate class of residual interest but a component of unrestricted funds. However whilst the SORP is not prescriptive about disclosure, the Interpretation considers designations should be reported within the annual report or notes to the accounts. In discussion the Committee agreed designations provided useful information to the reader of the accounts and disclosure on the face of the balance sheet was valuable. Also the relationship between designations and reserves might usefully be considered again when writing the next SORP.
- The Interpretation requires specific disclosure of any particular distribution requirements in the event of a charity's winding up. Currently the SORP only requires aggregate disclosure of the categories of funds (residual interests) on the face of the balance sheet with more detailed disclosure of the components and nature of material funds in the notes to the accounts.
- At a principle level the Interpretation's approach to the recognition of donated services is consistent with the SORP. Both documents recognise that reliability of measurement may be a difficulty. Where this can be overcome the Interpretation proposes the economic test of whether the service would be purchased if not provided by volunteers whilst the SORP focuses on whether the service is provided as part of a trade or profession. In discussion it

was agreed the recognition and valuation of volunteers might usefully be reviewed again in the writing of the next SORP.

- The Interpretation's treatment of capital grants is consistent with the SORP and both result in grants being recognised as gains unless there are conditions to be met with no presumption of deferring recognition.
- On business combinations, the Interpretation recognises that merger or acquisition accounting can apply and offers a useful clarification that where acquisition accounting is used, where there is an excess value upon acquisition (the overall net difference between fair value on acquisition of assets and liabilities and the consideration paid) it is treated as a gain.

#### **4.3 The Committee agreed:**

- **That there are no fundamental issues which require addressing by a revision to the current SORP ; and**
- **the paper might usefully be reissued in the form of an Information Sheet.**

#### **Item 5: Analysis and review of SORP Compliance**

5.1 The Chair invited Ken Brew to address the meeting. He recapped on the approach taken in the study which involved an initial checklist based review of the annual report and accounts of selected charities. The paper also captured issues most commonly identified from the escalated calls to a Commission Accountant from callers to the Charity Commission Direct help line.

5.2 Kirsty Gray, deputy chair, provided a perspective from the Office of the Scottish Charity (Regulator). OSCR already carries out a basic completeness check on all charities to ensure receipt of a trustees' report and primary financial statements and an external scrutiny report. Experience in the first year revealed an overall non-compliance rate (an incomplete submission) by 63% of charities. Charities under £25,000 had a non-compliance rate of 75% compared to only 25% for those charities with a gross income over £25,000. OSCR would consider the Charity Commission's approach to SORP compliance when planning their next regulatory study programme.

5.3 OSCR are carrying out three further regulatory studies: a detailed review of a sample of 300 smaller charities, the impact of Financial Reporting Standard 17 on pension disclosures, and a SORP compliance study similar to that carried out by the Commission and OSCR would consider the Commission's approach to SORP compliance when planning their study.

5.4 Ken Brew identified the main findings from the review of 647 reports and accounts inspections carried out in the Commission study:

- On a positive note, the study and anecdotal experience suggests an improving trend in annual reporting and the quality of charity accounts
- However the quality of annual reporting still needs to be improved. Over 60% of annual reports submitted by smaller charities (gross income of £100,000 and under, the receipts and payments threshold) were poor. Regrettably 8% of annual reports for larger charities (gross income exceeding £5m) were also poor.
- Inadequate or non-disclosure of reserves and reserves policies was the most common issue identified with over 25% of annual reports making incorrect or insufficient disclosures.
- The study suggested evidence of “template” annual reporting where the reporting narrative often changed little between reporting years. Some 14% of annual reports were disturbingly similar to the previous year.
- In many cases where the annual reports appeared little changed between years the style of reporting appeared to be modelled on small company reports, which suggested the use of a standardised text with trustees not writing their own report and perhaps simply following formats provided by their auditors.
- Governance costs were surprisingly high in a number of cases (exceeding 20% of gross income or £5m) which suggests inappropriate classification of costs.
- The study identified a number of common technical errors which could usefully be addressed in an Information Sheet.

5.5 The Chair proposed to the meeting that the recurring technical issues should be identified and clarified within a future Information Sheet. Also the issues arising from the study could usefully be explored through engagement with professional accountancy bodies, accountancy firms and sector partners, for example the Charity Finance Director’s Group.

5.6 In discussion it was noted that feedback to accountancy firms was valuable. Also it was noted that the Commission had written to the largest registered charities several years ago asking them to set a lead in improving the quality of reporting.

5.7 Debra Allcock Tyler on behalf of Directory of Social Change offered to publish the key findings in their e-newsletter. Also it was noted the definition of governance costs might usefully be reviewed in the writing of the next SORP.

**5.8 The Committee agreed that:**

- **The findings from the paper should be considered as part of the discussion of agenda item 6, the Information Sheet.**

**Item 6: Information Sheet**

6.1 The Chair invited Ray Jones to introduce the paper and appendices (draft Information Sheet and SORP preamble). The issue for consideration by the Committee was on the revised guidance on the classification of grants receivable between the “voluntary income” and “charitable activities” categories of the Statement of Financial Activities (SoFA).

6.2 In discussion the Committee agreed that the process of drafting, reconsideration at full Committee and redrafting has proven too protracted and that ideally Information Sheets should be issued more promptly. (The Information Sheet under discussion was the output of the 2006 SORP review.) It was agreed that the order of paragraphs in the draft text be re-ordered before publication in the Information Sheet.

**6.3 The Committee concluded that:**

- **the Information Sheet should now be issued on the web;**
- **that paper 2 on the Statement of Principles should be modified and issued as a second Information Sheet;**
- **that the findings of paper 3, Charity Commission analysis and review of SORP compliance, might usefully be incorporated into a later Information Sheet;**
- **the process for agreeing the contents of the Information Sheet should be streamlined with an initial draft considered by the Committee and then any proposed changes submitted by Committee Members to the SORP Secretariat by e-mail, with the final output then issued by the Secretariat without further review;**
- **future Information Sheets should be issued via the web sites of the Commission and OSCR; and**
- **the draft SORP preamble be considered as part of agenda item 7.**

## **Item 7: Timing of the reprint of SORP 2005**

7.1 The Committee had previously considered the amendments to the current SORP following changes in charity law in Scotland, charity law in England and Wales and Company law, and the inclusion of a preamble (Committee meeting of 12 April agenda item 6). The preamble had been revised by a sub group of the Committee led by Debra Allcock Tyler and the changes due to law had subsequently been reviewed for legal accuracy.

7.2 The timing of the reprint of SORP 2005 had not proven straightforward as many of the company law changes were not effective until April 2008 and a number of anticipated changes in charity law in England and Wales had not been implemented in October as expected but deferred until 2008 pending the relevant Order and Regulations proposed by the Office of the Third Sector obtaining Parliamentary time.

7.3 Kirsty Gray advised that further modifications to the Regulations for accounts in Scotland were planned and Ray Jones advised the Committee that all thresholds applying in England and Wales were also due for review and consultation later this year.

7.4 The Committee discussed the ease with which a web based SORP could be frequently modified and updated as compared to a printed version. It was noted that the Commission has a publication contract with CCH and any web based changes would have to be compatible with the terms of that contract.

7.5 The Chair thanked Debra Allcock-Tyler, Paul Spokes, Tidi Diyan and Tritsan Lumley for convening a sub group to refine and develop the preamble.

### **7.6 The Committee concluded that:**

- **The preamble should be published on the Commission web site pending a reprint of the SORP;**
- **the Preamble should be referred to the ASB CAPE Committee for information; and**
- **the Commission should liaise with CCH as to the most appropriate timing of a reprint of SORP 2005, once the further Order and Regulations amending charity law in England and Wales and Scotland were in effect. The reprint would incorporate the preamble and amendments due to changes in the law.**

## **Item 8: Preparing for convergence – SORP and IFRS options**

8.1 The Chair asked Nigel Davies to introduce the paper. It was noted that the Committee had previously considered developments in International Financial Reporting Standards (IFRSs) at its January and April meetings. Following the April meeting a letter was sent to the ASB expressing concern that sufficient attention was not being given to the development of IFRSs for charities and requesting the ASB press the International Accounting Standards Board (IASB) to liaise with the ASB and through the ASB with the UK SORP Committee and other interested parties.

8.2 The paper considered whether waiting for an IFRS for charities was a viable option but rejected this option due to the probability that UK Generally Accepted Accounting Practice (UK GAAP) will have converged with IFRS many years before any IFRS for charities might be available. The SORP could not exist in isolation of changes in UK GAAP.

8.3 All of the available options on which to base the next SORP were problematical. The International Public Sector Accounting Standards Board (IPSASB) had produced an interpretation of IFRS for government bodies but this was inappropriate due to its complexity and its reflecting the particular accountability relationships of the homogeneous government and public sector.

8.4 Similarly the IFRSs which are developed for commercial organisations quoted on a recognised stock exchange and publicly accountable to world capital markets, were too complex. Both IFRSs and IPSASB's standards were written for organisations considerably larger than all but the very largest registered UK charities.

8.5 Concluding the options were the exposure draft of the IFRS for Small and Medium Enterprises (SMEs) and possible plans by the ASB to develop an IFRS compliant Financial Reporting Standard for Smaller Entities (FRSSE). Of these two options, the paper recommended the IFRS SME standard since it was likely to be available sooner than an IFRS compliant FRSSE and the standard, in terms of its constituency, was a good fit with the profile of the registered charities sector in England and Wales.

8.6 It was noted that the initial planned convergence date advised by the ASB was January 2009, however Alan O'Connor advised that the ASB had anticipated that the IFRS for SMEs would have been published and this project was already delayed and subject to a number of uncertainties. Whether the ASB would develop an IFRS compliant FRSSE was contingent on the form and content of the IASB SME standard. It was likely that the convergence date could therefore slip.

8.7 Kirsty Gray tabled an additional paper profiling the registered charities sector in Scotland and noted that although the sector in Scotland was also concentrated by income. Based on existing thresholds a FRSSE based approach would cover a far higher percentage of the Scottish charity population than in Scotland than in England and Wales.



8.8 In discussion the difficulty of progressing plans for the next SORP amidst this background of uncertainty was explored. With the IFRS compliant FRSSE not available and the final IASB SME standard not published it was considered premature to reach a final decision.

**8.9 The Committee concluded that:**

- **it was important that the SORP is maintained and it should be available on a timely basis to the sector as UK GAAP develops;**
- **that plans to develop the next SORP should progress;**
- **that SORP development draws on the latest available information on the IASB SME and IFRS compliant FRSSE standards in its early stages, pending a final decision on the preferred underpinning framework towards the end of the development process when the convergence agenda is clearer; and**
- **noted that the needs of the medium and smaller charities should inform the development of the next SORP.**

**Item 9: Work Plan for SORP 2010.**

9.1 The Chair invited Ray Jones to introduce the paper which was framed with the ASB's convergence strategy in mind. A considerable emphasis is placed on sector and stakeholder engagement in the early stages of the plan. The outline plan sets a demanding timescale and envisages the next SORP to be published in March 2010.

9.2 Alan O'Connor on behalf of the ASB advised that the ASB had yet to determine the future role of SORPs post convergence of UK GAAP and IFRSs and it had not been decided as to whether the ASB could offer the current negative assurance statement on SORPs that interpret IFRSs as opposed to UK GAAP.

9.3 In discussion it was agreed it was important to press on with SORP development and that any early work would remain useful to a final accounting solution for UK charities following convergence. The sector needs practical and timely advice. It was agreed that the Committee wished to be closely involved with the planning for the next SORP.

**9.4 The Committee concluded that:**

- **a further meeting be convened in November to review the detail of the planned consultation events in terms of topic, delegate list, and timing; and**
- **that the outline timetable be approved as the basis for developing the next SORP.**

**Item 10: Plan for meetings including Scotland.**

10.1 The timing of a meeting in Scotland to be considered at the next meeting along with the timing of future meetings.

**Item 11: Any other business and date of next meeting.**

11.1 The Chair invited members to submit any other business.

11.2 Chris Harris noted that at the April meeting (minute 5.4) those who wished to be involved in raising an international debate on a not-for-profit IFRS should contact him. He had been contacted by a non-Committee member and would brief the Committee as to developments.

11.3 John Graham advised that he was joining with a number of practitioners to consider the relationship between management accounts and an activity based Statement of Financial Activities in the context of explaining to donors and funders the use of resources. He invited any preparers of accounts on the Committee to contact him to take part.

11.4 **The date of the next meeting subsequently confirmed as 23 November.**