

Feedback from Engagement Strands on Notes to the Accounts

<ul style="list-style-type: none"> • Engagement Strand: Academics and regulators and proxies for the public interest
<p>A. Options Considered by the Engagement Strand</p>
<ul style="list-style-type: none"> • Option 1 – details of all material grants given to other institutions should be included within the accounts, not on the website. • Option 2 – amendments suggested to Note 9 - staff costs and employee benefits and remuneration and benefits received by key management personnel: <ul style="list-style-type: none"> - Amend paragraph 9.29 to require disclosure of an estimate of average FTE and a choice to disclose average headcount, which represents a reversal of the current requirement. - Amend paragraph 9.29 to allow charities the choice to disclose an estimate of average available FTE e.g. excluding staff on payroll but unavailable for work. - Clarify paragraph 9.30, which requires disclosure of the number of employees whose total employee benefits (excluding employer pension costs) for the reporting period fell within each band of £10,000 (€10,000) from £60,000 (€70,000) upwards. Suggested clarifications are: include employer pension costs; clarify that calculations are based on take-home pay in the reporting period rather than annual, full-time equivalent gross salary; clarify paragraph 9.32, which requires disclosure of the total amount of any employee benefits received by trustees and its key management personnel, as it is currently unclear whether employer pension costs should be included. Suggestion that disclosure of employee benefits split using the categories listed in 9.26 would be a more meaningful disclosure. <p><i>[For information, paragraph 9.26 requires analysis of total staff costs and employee benefits in the following categories:</i></p> <ul style="list-style-type: none"> • <i>wages and salaries;</i> • <i>social security costs;</i> • <i>employer's contribution to defined contribution pension schemes;</i> • <i>the operating costs of defined benefit pension schemes (excluding pension finance costs related to defined benefit pension schemes); and</i> • <i>other forms of employee benefits.]</i> • Option 3 – require comparative information for total figures only, rather than for all figures in the accounts. • Option 4 – reduce the content in the pensions note.
<p>B. Advantages/Disadvantages of Options Considered</p>
<ul style="list-style-type: none"> • Option 1 – Details of material grants in the accounts: The engagement strand commented: <ul style="list-style-type: none"> - Websites aren't audited; the accounts are. By including information on material grants given to other institutions in the accounts, it will be audited. - Data on a website cannot be searched electronically, whereas data in the accounts can be. - A link to the website may change.

- Some charities are merely providing the information by mail on request. Inclusion in the accounts will make the information more readily available.
- Option 2 – Amendments to staff cost disclosures:
Comments included the following:
 - A focus on FTE rather than headcount would reduce confusion and misunderstanding about disclosure requirements, improving consistency and mitigating the risk of reputational damage to the charity or the sector.
 - Amendments to paragraph 9.29 to allow disclosure of available FTE will provide more meaningful information for the analysis of staff costs.
 - Clarification of paragraph 9.30 will improve consistency and reduce confusion. Inclusion of employer pension costs will ensure consistency with paragraph 9.26. Clarification of paragraph 9.30 and the employee benefits included in the disclosure will reduce misunderstanding of users of the accounts, who may incorrectly believe the disclosure is based on annual gross salary.
- Option 3 – Comparative figures for totals only:
The engagement strand was of the view that:
 - Inclusion of comparatives for total, rather than all, figures can reduce clutter, without necessarily removing useful information (i.e. the detailed comparative information is potentially not too helpful).
- Option 4 – Reduced content in the pensions note:
 - The pensions note is often lengthy and technical. Removing some information will increase the usefulness of the note to the users of the accounts.

C. Conclusions

See Advantages/Disadvantages outlined in B.

D. Other comments

- It was noted that the first submission to the FRC periodic review includes a request to reduce the required defined benefit plan disclosures.
- The briefing paper made reference to replacing items from the trustees' annual report with links to other information produced by the charity. Use of hyperlinks raises concerns from a regulatory perspective as links could become broken. This could be problematic for years after the publication of the annual report and accounts, for example in the case of an inquiry.

• Engagement Strand: Trustees

A. Options Considered by the Engagement Strand

- Option 1 – to re-commit to the recommendations made by the engagement strand at the end of phase one. Specific recommendations relevant to the notes to the accounts include:
 - The use of Plain English language in the SORP accompanied by an additional 'think non-financial expert first' approach.
 - Inclusion of a comprehensive glossary (reflecting terms and definitions used by the regulators) and full indexation to assist cross-referencing.

- Make it easier to identify within the SORP what is a legal or regulatory requirement and what is recommended practice, citing sources where relevant.
- Reduce the length and complexity of the financial notes by better use of referencing, signposting, cross-referencing and hyperlinking.
- Option 2 – To accept all/some of the issues identified in Appendix A of the briefing paper to be removed from the financial notes, i.e.:
 - Aggregate disclosure of the total amount of donations donated by trustees or other related parties without conditions.
 - The requirement for comparative to be provided for all amounts presented in the SoFA.
 - Disclosures to be made in the notes to the accounts in respect basic financial instruments.
 - Disclosures in the notes to the accounts of defined benefit plans.
 - Requirement for a Statement of Cash Flows
 - Disclosure of redundancy or termination payments relating to the reporting period
 - The recognition of a liability for paid annual leave and paid sick leave
 - Salary banding disclosure (the number of employees whose total employee benefits fell within each band of £10,000 (€10,000) from £60,000 (€70,000) upwards)
 - The judgements management has made in the process of applying the entity's accounting policies that have the most significant effect on the amounts recognised in the accounts; and
 - Discounting obligations to their present value
- Option 3 – To establish the 'bare minimum' disclosure requirements for all charities and identify additional disclosures for the next two tiers
- Option 4 – a "building block" approach in which the SORP Committee/Making Body should consider:
 - Establishing what aspects of the financial notes are universal to all charities;
 - Identify those disclosures which are additional or discretionary and as such could be applied to the different tiers, according to a range of factors;
 - Exception reporting for those discretionary or additional disclosures; and
 - Reviewing the inclusion of comparative data.

B. Advantages/Disadvantages of Options Considered

- Option 1 – a reduction in complexity will avoid the notes to the accounts becoming overwhelming.
- Further exemplification of Option 4 is included in D below.

C. Conclusions

- There was broad agreement for option 1.
- There was not agreement on options 2 or 3. In particular, the engagement strand was of the view that removing disclosure requirements on executive pay would reduce transparency.
- Further details on the aspects of Option 4 recommended by the engagement strand are included in D below.

D. Other Comments

- Further suggestions were made with respect to Option 4:

- Universal disclosure requirements could include the following modules of the current SORP:
 - Module 3 Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors;
 - Module 4 Statement of Financial Activities;
 - Module 5 Recognition of income, including legacies, grants and contract income;
 - Module 7 Recognition of expenditure;
 - Module 8 Allocating costs by activity in the Statement of Financial Activities;
 - Module 10 Balance sheet; and
 - Module 14 Statement of Cash Flows.
- It was suggested that the remaining disclosures are unlikely to apply to all charities, therefore could be assigned to a different tier threshold.
- The remaining disclosures from the current SORP are in:
 - Module 6 Donated goods, facilities and services, including volunteers;
 - Module 9 Disclosure of trustee and staff remuneration, related party and other transactions;
 - Module 11 Accounting for financial assets and financial liabilities;
 - Module 12 Impairment of assets; and
 - Module 13 Events after the end of the reporting period
- Factors to consider when deciding which charities should apply the additional requirements could be:
 - Relevance;
 - Materiality;
 - Size of the charity;
 - Income;
 - Risk; and
 - Liquidity

With additional guidance in the SORP to help make decisions on which requirements need to be applied.

- Exception reporting would allow for a reduction of content in the accounting policies note (often Note 1). Rather than include 'boilerplate' disclosure of the accounting policies being applied, charities could instead just state that the annual reports and accounts adhere to the required accounting policies, together with an (optional) explanation of any additional disclosures that have not been presented and the reason why (e.g. non-disclosure of heritage assets where a charity has none).
- The accounting policies note could be moved to the end of the notes, with appropriate references in the individual notes, or the text for each item could be included as a footnote in the note to which it relates.
- It was noted that the SORP Making Body had written to the FRC about a number of issues, including comparative data and was awaiting a response. The engagement strand was therefore of the view it would not be helpful to comment on comparative data until a response had been received.

- Engagement Strand: **Larger Charities**

A. Options Considered by the Engagement Strand

- Option 1 – Simplify/reduce the length of the pensions and financial instruments notes, providing references to other sources of information. Simplification could be achieved by considering materiality against the balance sheet. The pensions note could focus on what the risks and the important factors are. The key detail could be provided, with an offer to provide further information on request. Details of the valuation of the pension assets and liabilities could be provided (e.g. name and source of pension professionals).
- Option 2 – With respect to disclosure of accounting policies (often Note 1), over-arching policies that are not linked to a specific item could remain where they are, but all other policies could be positioned with the relevant note.
- Option 3 – The SORP should consider materiality in terms of which related party transaction should be disclosed.
- Option 4 – The SORP should require disclosure of highest paid employee (by position, not name) for all charities.
- Option 5 – The note relating to the Statement of Cash Flows should only be required for the largest charities (in terms of the 3-tiered approach)

B. Advantages/Disadvantages of Options Considered

- Option 1 – simplify/reduce the length of the pensions and financial instruments notes – will reduce clutter in the accounts. Provision of supporting information outside the accounts will avoid a reduction in the value of the notes.
- Option 2 – include accounting policies within the relevant disclosure – avoids the description of an accounting policy being detached from the relevant note. This is more user friendly and avoids details of accounting policies being overlooked.
- Option 4 – disclosure of highest paid employee – would support the principle of transparency.
- Option 5 – remove the need for small charities to include a note about the Statement of Cash Flows – was suggested to avoid unnecessarily including unhelpful information in the accounts of smaller charities; the engagement strand feels that the note relating to the Statement of Cash Flows is not used by users.

C. Conclusions

- There was strong agreement for options 1 and 2.
- Other suggestions/options were not as strongly supported.
- With respect to Module 9, Disclosure of Trustee and Staff Remuneration, Related Party and Other Transactions, the engagement strand agreed with earlier suggestions to remove the need to disclose the aggregate disclosure of donations donated by trustees or other related parties without conditions. The engagement strand disagreed with suggestions to remove the need to disclose redundancy costs and felt that this was an important note for donors.

D. Other Comments

- The trustees' annual report could (optionally) be linked to relevant part of the accounts.
- The engagement strand was keen to keep in the option to provide further details on grants made if requested. This information can be quite detailed and clutter the accounts.

- Module 18 Heritage Assets: request that the flexibility is not removed regarding valuations in that it can be via a note and not a balance sheet item.
- Module 19 Accounting for Funds Received as Agent or as Custodian Trustee: suggestion that more explanation should be given on this to offer clarification and avoid errors.
- Module 20 Total Return (Investments): As this is relevant to England and Wales only, there may be confusion.
- Module 25 Branches, Linked or Connected Charities and Joint Arrangements: Clearer language could be used as it is not easy to follow.
- No issues were noted with respect to Modules 12, 13, 15, 21 – 24 and 26 – 29.

• **Engagement Strand: Professional and Technical (B)**

A. Options Considered by the Engagement Strand

- n/a

B. Advantages/Disadvantages of Options Considered

- n/a

C. Conclusions

- Recommendations were provided for several modules, please see D below.

D. Other Comments

- The engagement strand made detailed suggestions for a range of disclosure requirements. A summary of suggestions is provided below:

Module 9, Disclosure of Trustee and Staff Remuneration, Related Party and Other Transactions

Comments made:

- The SORP would benefit from clearer requirements on aspects of pay such as compensation for loss of office, extra-contractual payments, ex gratia payments to related parties and redundancy pay.
- In respect of certain payments relevant to this module, for example, ex gratia payments, guidance on whether a payment should be considered non-charitable is required.
- More clarity is needed about the treatment of non-disclosure agreements and court settlement payments. Where such a payment is to a junior member of staff and is small, clarity is required over whether this would be considered material by nature.
- Donations from a related party with conditions attached should continue to be disclosed.
- The requirement to disclose the aggregate of the total amount of donations received without conditions, including from a charity's trustees, can be problematic (e.g. cash collections in a church), therefore the requirement to disclose donations from related parties without conditions should be removed or changed to a "may" requirement.
- In paragraph 9.8, there should be a requirement to show trustee remuneration separately from any remuneration a trustee receives as a member of staff. This is required for consistency with paragraph 9.32.

- In paragraph 9.18, the first bullet point is revised to avoid confusion. This paragraph is in a section about what does not need to be disclosed and goes on to refer to what must be disclosed.
- The requirement for senior management pay disclosures should be a 'must' requirement.

Module 16, Presentation of Grant-making Activities

Comments made:

- Simplify/reduce (but not remove) the amount of disclosure required for grant-making activities in the notes to the financial statements to declutter the financial statements and to focus on the most significant grants. This could be achieved by, for example, focussing on the top ten grants by value. Comparatives should be retained for the top ten, and for new entries to the top ten and institutions falling out of the top ten.
- Highlighted that if, per paragraph 16.17, a charity chooses to provide information about institutional grants on its website, this information could be changed at any time, including post-audit.
- There was disagreement on removing comparatives, as they can provide useful information.

Module 21, Accounting for Social Investments

Comments made:

- Programme related buildings should not be depreciated if they are measured at cost. They should just be reviewed for impairment and impaired if necessary.

Module 22, Accounting for Charities Pooling Funds for Investment

Comments made:

- There is scope to introduce less onerous requirements for charities pooling funds for investment. Not all charities pooling funds for investment are able to comply with the disclosure requirement to name all the charities pooling funds as there are too many.

Module 5, Recognition of Income

Comments made:

- There is scope to simplify the presentation of deferred income and the notes on income.
- Notes required on deferred income that analyse the movement on deferred income and explain the reasons why income is deferred were not considered useful. Requirements to produce these notes could be removed.
- Some disclosure requirements for income could be simplified or combined and therefore reduced. For example, the requirement to disclose components of income (SORP paragraph 4.25) and the requirement for further sub analysis of income (SORP paragraph 4.42). There appears to be some overlap in the existing disclosure requirements.
- There is also a lot of cross over with the restricted funds note which also analyses and explains income by category and purpose. It would be helpful if these requirements could be reduced to one statement or two consistent statements in one place.

Module 11, Accounting for Financial Assets and Liabilities

Comments made:

- Engagement strand members noted seeing an increase in charities investing in more "racy" financial instruments without the knowledge of how to account for these. Further support, such as worked examples, is needed for charities.

Module 14, Statement of Cash Flows

Comments made:

- Less complex charities do not find the Statement of Cash Flows useful and the engagement strand would favour a concession from its preparation for such charities.
- The engagement strand would like to see the Statement of Cash Flows presentation tailored to the charity sector in the same manner that the SoFA has been tailored.

Module 17, Retirement and Post-employment Benefits

Comments made:

- There are gaps in FRS 102 requirements covering a number of aspects of the accounting. It may be possible to address some of these solely within the SORP but it would be preferable for FRS 102 to be amended.
- Gaps arise in FRS 102 in relation to accounting for multi-employer schemes.
- Gaps in FRS 102 would require amendments to be made to FRS 102; the SORP Committee could raise these issues in a further submission to the FRC as part of the current periodic review of FRS 102.
- Gaps in FRS 102 include how to account for a move from defined benefit accounting to recognising an agreed recovery plan liability instead or, more likely, a cessation debt.
- It may be more appropriate for non-profit entities to account for defined benefit pensions on a funding basis in order to reduce complexity both of the accounting treatment and of the notes.

No changes were recommended for Modules 19, 20 and 25.