

I make this submission as:

- A sole practitioner who has been preparing accounts and conducting independent examinations for almost 10 years for charities with incomes ranging from £26k to £400k; my qualification for the upper part of the range is being a Fellow of the Association of Charity Independent Examiners.
- The trustee treasurer of 4 charities, subject to independent examination and audit, during the last 11 years.
- A holder of the ICAEW 'S Diploma in Charity Accounting.

Some of the points in this submission were covered in my article entitled 'SORP 2015 terminology quirks' in the technical briefing section of the March 2016 edition of Charity Finance magazine. I am keen that the SORP should be accessible to people involved with smaller charities who are not accounting professionals and are looking for guidance.

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*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?*

Broadly yes with one significant exception. The modular approach is a good implementation of the bottom-up concept of the FRS 102 SORP; 13 of the 29 modules do not apply to any of my clients - all smaller charities.

The significant exception (easily corrected) is reserves information for smaller charities. Reserves comment is an important aspect for smaller charities, but the SORP fails smaller charities wanting information on reserves. The Glossary entry for reserves just refers readers to the TAR Module 1, but para 1.22 (applicable to smaller charities) gives no explanation of reserves. The calculation/definition part of para 1.48 should be moved to para 1.22 - leaving just the extra disclosure requirements for larger charities in para 1.48.

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

Yes, three topics:

**Example accounts focused on smaller charities.** The current two example accounts (Rosanna and Arts Theatre) are really for larger charities and have several features that do not apply to most smaller charities. A 'quick win' would be an update to the SORP 2005 example accounts for the Dorsetshire Drugs Advice Centre; this was an accessible example that was relevant to most smaller charities.

**Understanding restricted funds.** I find that the concept of restricted funds is quite often difficult for smaller charities and the SORP could ease the understanding. Restricted funds are mentioned twice in the Glossary: the 'Restricted fund' entry is helpfully straightforward, but the 'Funds' entry introduces the legal jargon also of being held on trust. Para 2.8 and 2.9 take the legal jargon further by mentioning respectively specific trusts and a non-binding preference that falls short of a trust law restriction. I would like to see a more user-friendly, less jargonistic text in the SORP - with some examples.

**Summary or Index.** An indexed summary of the requirements and exemptions for small charities could usefully be given in an appendix along the lines of that included as Appendix 5 to SORP 2005.

*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?*

Two meanings for 'should' have slightly reduced the overall success of this approach:

- For English and Welsh charities, there are two versions of 'should' in force for financial issues:
  - **CC3:** trustees are generally expected to follow good practice, and be ready to justify not doing so. However, trustees are warned that they will be in breach of their legal duties if they do not follow good practice on financial controls and risk management.
  - **SORP:** Encouraged to follow the particular SORP recommendation, but not doing so is not regarded as a departure from the SORP.

The demarcation is that CC3 applies to ongoing financial aspects, whereas the SORP covers 'after the event' statutory reporting.
- Thus, to give a broad example, trustees effectively must specify appropriately robust controls for everyday financial transactions but are free to submit minimally-compliant statutory accounts (without explanation) if that is deemed to be in a charity's best interests. As one of the six CC3 'musts' is that trustees must comply with statutory accounting and reporting requirements, it seems ironical that the milder SORP 'should' 'trumps' the CC3 'should' on SORP issues.
- Given the everyday applicability of the CC3 'should' compared with the once-a-year applicability of the SORP 'should', I suspect that English and Welsh charities could initially interpret the SORP 'should' as 'must'; such an initial interpretation is to the advantage of users of the accounts. In the light of Kids Company etc and given that 'the objective of the trustees' annual report and accounts is to provide information about a charity's financial performance and financial position that will be useful to a wide range of stakeholders ...' (Scope and Application para 11), perhaps the SORP 'should' needs to match the stronger CC3 'should'. If not, it would be helpful if the SORP drew attention to the different meaning of 'should' in CC3 and explained the demarcation.

*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.*

Yes, the SORP gives charity-focused advice suitable to a certain extent for the lay user that is unlikely to be as readily discernible from the broader FRS 102 - which is perceived as being aimed at the accounting professional. Examples of such advice are reserves, restricted funds, fundraising aspects and the Glossary. I hope that the SORP can continue to serve as a 'one-stop shop' for most charities - with appropriate signposting to FRS 102 where necessary. A finding from the 2008/9 research is still pertinent today: the SORP's robust framework is vital for continuing support and confidence in both individual charities and the sector (with a memorable quote: 'I would weep if it was removed').

*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.*

The preamble to the question mentions ambiguity - to which I would add inconsistency and overlap. Such aspects should be avoided if the SORP is meant to be accessible to people who are not accounting professionals and are looking for guidance - especially for smaller charities. I have come across six issues in the SORP that I think should be improved.

**No time requirement for spending unrestricted income funds?** Reserves comprehension is not helped by an inconsistency between the TAR Module 1 and the Fund Accounting Module 2. Para 2.11 mentions the general trustees' legal duty that restricted income funds are to be spent within a reasonable time of receipt, but para 2.6 states that unrestricted funds are spent at the discretion of the trustees. Whilst the reserves information at para 1.48 (which under the current drafting does not apply to smaller charities) steers readers away from concluding from a comparison of paras 2.6 and 2.11 that unrestricted income funds are not subject to a time requirement, the SORP should make this aspect explicit (as done in CC19 para 5.2) by including the income fund time requirement at para 2.6.

## Donations & Grants.

- Para 4.32 positions donations as coming from individuals and corporations, and grants (non-performance-related) as coming from government and foundations. In contrast, the Glossary gives different definitions for ‘donations’ (gifts that will not provide any economic return to the donor - excluding performance-related conditions) and ‘grant income’ (any voluntary income received by the charity from a person or institution - but treated differently if subject to performance conditions). Para 4.34 is straightforward in identifying performance-related grant income as conditional on delivering specified goods/services. My conclusion on trying to weigh-up these various phrases is that I agree with this quote from a well-known charity finance pundit: ‘Grants don’t exist; they are either contractual/trading arrangements or gifts’.
- Para 5.58 on disclosure of government grants further clouds the understanding. At face value, the term ‘government grants’ means grants from government. However, the Glossary definition (with phraseology such as ‘compliance with specified conditions’) implies that the term covers only performance-related grants. Thus a charity in receipt of non-performance-related grants from government could reasonably argue that it is exempt from the disclosure requirements of para 5.58 as it has received ‘grants of a general nature provided by government’ as per para 4.32 rather than ‘government grants’ as per the Glossary.
- The SORP improvement I suggest is along the lines of:
  - The only reference in the SORP to grants should be a Glossary entry to the effect that, whilst a well-used term, it is irrelevant for accounting presentation purposes - and refer the reader to the ‘donations and legacies’ or ‘charitable activities income’ sections as appropriate.
  - All other SORP references to grants should be amended to terminology appropriate to the ‘donations and legacies’ or ‘charitable activities income’ contexts.

**Restricted fund spend automatically includes support costs?** Para 2.15 makes the unqualified statement that restricted costs include the support costs associated with the activities undertaken by restricted funds, but para 8.7 rules out the inclusion of support costs if prohibited by the terms of a gift. I think that para 2.15 should be amended to reflect para 8.7.

**Collective trustee expenses are now disclosable?** SORP 2005 para 232 excluded routine expenditure attributable collectively to trustees, perhaps room-hire for meetings/awaydays, from disclosure. There is no such exemption at FRS 102 SORP para 9.18, so presumably such expenses fall under para 9.12 as disclosable expenses paid directly to third parties. However, the completion notes for Note 28.2 of the FRS 102 CC17 proforma accounts imply, by referring only to ‘expenses incurred by trustees in fulfilling their duties’ that all collective expenses are still exempt from disclosure - but that is not what the SORP states. As a ‘brake’ on holding trustee meetings at costly venues, I believe there is a case for a SORP requirement that material collective trustee expenses are disclosable.

**No difference between ‘Expenditure on Raising Funds’ and ‘Fundraising Costs’.** The scope of ‘expenditure on raising funds’, a prominent term in the Sofa, is covered by 8 bullets at para 4.45. The Glossary gives a definition of ‘fundraising costs’ with three bullets but does not mention ‘expenditure on raising funds’. The Glossary definition is explained by 3 bullets, which basically cover the same ground as the Sofa term. I suggest that the Glossary definition should be retitled as ‘expenditure on raising funds’, and that the sole module reference to ‘fundraising costs’ at para 4.50 is amended.

**Smaller charity definition.** SORP Update Bulletin 1 changed the Glossary definition of ‘larger charity’ to standardise the £500k income threshold, but did not change the definition of “smaller charity” at para 1.9 - where a smaller charity (not mentioned in the glossary) is defined as not subject to statutory audit. Thus a

charity in England and Wales with annual income between £500,001 and £1m, whilst complying with larger charity requirements such as a statement of cash flow, is apparently free to report as a smaller charity where the SORP specifies 'smaller charity'. The prime instance is the option at para 4.22 ('smaller charities' stated in section heading), as a charity not subject to statutory audit, to report income and expenditure on an alternative basis to the preferred activity basis. This loophole can be closed by removing the audit reference from these paras and adding a simple and obvious Glossary statement that a smaller charity is not a larger charity.

**'Legal Purposes' has not fully replaced 'Objects'.** The FRS 102 SORP introduced the term 'legal purposes', and so removed the previous SORP's terminological similarity between 'objects' (the statement of a charity's purposes in its governing document) and 'objectives' (performance targets). However, the FRS 102 SORP still has five references to 'objects' (19.13 (twice), 24.13, 27.16 and Glossary - programme related investments); I suggest these references are updated.

*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?*

I agree with the principle of progressive and proportionate regulation, and the medium company annual income threshold (currently £10.2m) seems a reasonable peg. However, having little knowledge of charities at this level, I suspect that a consensus will not be easily forthcoming on which SORP items to relax for the 'middle' tier - and thus the existing two tier structure will probably remain by default.

*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?*

See Q6 answer, but should there also be consideration of additional reporting requirements for a third tier?

*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?*

Better integration and detail could be achieved by having a wider set of example accounts that illustrate good practice. There was a suite of ten example accounts for SORP 2005; so far there are only two for the FRS102 SORP.

I do not agree with a key facts summary as an annex to the report/accounts - which often appear to the lay reader of accounts as a 'clunking', unwieldy document. It is likely that a progressive charity is already doing a separate, accessible key facts summary tailored to its particular circumstances - often known as an annual review. To counter any view that an annual review can completely disregard the SORP:

- The SORP could encourage an annual review appropriate to a charity; guidance should be given along the lines of the general principles of summary financial information and statements not carried over from SORP 2005.
- The information about a charity on the Charity Commission's internet register of charities, fed by the annual return, is arguably already a simplified key facts summary. This information could be expanded to give what is felt to be required for cross-charity comparison.

With regard to the latter, good practice should evolve whereby a charity explains (in the report and review) how the standardised information (ratios etc) given in the Charity Commission's internet register should be interpreted for that charity's circumstances.

I do not support further SORP reserves guidance; a cross-reference to CC19 should suffice.

*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?*

SORP 2005 accounts focused attention on fundraising and governance costs. Now that governance costs have

disappeared from the Sofa, my early observation on FRS 102 accounts is that attention has now moved to expenditure on raising funds and support costs - with heightened interest because support costs are generally greater than governance costs. Given that the accounts should give some indication of overheads, I think that the current required disclosure is good enough.

Furthermore the support costs category should be maintained - as dropping it could be interpreted as implying that a charity has no overheads. Another finding from the 2008/9 research was that the SORP gives a form of comparability across a diverse sector. A charity should use the narrative or expand the Notes to explain its particular overheads position.

Given the sole module reference to 'fundraising costs' at para 4.50 covers limited circumstances, there seems little need for a general requirement on greater disclosure of 'fundraising costs'. I think that the current required disclosure on 'expenditure on raising funds' is good enough.

I certainly agree with a Sofa distinction between revenue and capital items - especially because the custom and practice of designated fixed assets has absolutely nothing to do with the requirement at para 2.7 that designated funds cover just future projects. At the charity where I am currently the trustee treasurer, all the fixed assets are unrestricted functional assets and so there is an unrestricted property fund column on the Sofa - which shows depreciation etc. This means that the restricted fund and general unrestricted fund Sofa column details readily align with the management accounts, and it is easier to match the reserves to the financial statements. Returning to the custom and practice of designated fixed assets, I believe that the references to fixed assets in reserves calculation at para 1.48 adequately cover the concept - and thus the reference to a functional fixed asset should be deleted from the Glossary's designated fund definition.

*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?*

**Support:**

- **Public benefit** - I find that the concept of public benefit is not well understood by charities - especially where the benefit to the public is 'indirect' - such as with animal charities. As the main Charity Commission guidance on public benefit can seem forbidding, I suggest a cross-reference to the good summary of public benefit at CC3.
- **Risk management** - content with all proposals on issues. Risk management is a principal precaution against any trustee liability claim.
- **Going concern** - content with all proposals on issues, but on pensions I think there should be differentiation between a defined benefit liability and the broader, but smaller, auto-enrolment liability.
- **Staff pay disclosure** - the self-employed should be added to the list.

**Do not support:**

- **Administrative & fundraising costs** - see Q9 answer.
- **Funder disclosure.** I would not welcome a move to require the disclosure of individual donations; there should be respect for donor or recipient sensitivity. What perhaps could be suggested as good practice is disclosure of donor segment totals (eg charity, government, corporate and individuals) as appropriate to a charity.
- **Key facts** - see Q8 answer.

- **Spend outside jurisdiction.** At best this should be a ‘may’ - which would give an opportunity to highlight my concern that charities may not be aware that HMRC expects enhanced levels of due diligence, monitoring and evaluation of overseas spend, and that non-compliance can lead to Gift Aid being proportionately disallowed. See Para 9 to <https://www.gov.uk/government/publications/charities-detailed-guidance-notes/annex-ii-non-charitable-expenditure> dated 6 Apr 16.

*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?*

See Q10 answer

*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?*

I would like to see the requirement removed to give all Sofa prior-year comparatives; so far I have not seen that this adds any value. A charity can mention any significant aspects in the narrative and/or Notes, and a user can download the prior-year accounts from the Charity Commission website.

*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?*

We seem to be hardwired by custom and practice to have a lengthy and formidable policy note (now probably longer with FRS 102 aspects) at the beginning of the notes - as perpetuated in the FRS 102 example accounts. I think the accounts would be more user-friendly if the relevant policy was placed in the appropriate disclosure note. Perhaps Module 3 could have a phrase similar to para 1.11 (that TAR contents can be placed in any order etc) and future example accounts could illustrate this concept.

Para 9.29 requires disclosure of average head count and suggests full-time equivalent as a ‘may’. I would like to see the latter become a requirement alongside the former; the combination of the two gives a better picture

*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?*

None.

*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?*

The recommendation stated at para 8.1.5 of CC15d for non-company charities to give an explanation about the departure from the 2008 regulations. This adds to the ‘clunkiness’ of the accounts and the jargon serves no useful purpose to lay readers. When are the 2008 regulations going to be updated?

**End of submission**

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