

Response to invitation to comment on SORP draft Update Bulletin 2

This response has been prepared by Joanna Pittman, partner of Sayer Vincent LLP, on behalf of partners and colleagues at Sayer Vincent.

We prepare our response as auditors, independent examiners, preparers of accounts and advisors for charities. We also respond as trustees and treasurers of various charities.

Q.1 Do you agree with how the amendments to FRS 102 have been reflected in the proposed amendments to the Charities SORP (FRS 102) in draft Update Bulletin 2? If not, which of the proposed changes do you not agree with, and why?

We accept that the changes in Update Bulletin 2 are required in order to recognise the changes made to FRS 102 in December 2017. As the SORP is an interpretation of FRS102 for charities, we acknowledge that the underlying FRS takes precedence and the SORP must not conflict with it. However, we feel that there are some amendments proposed in Update Bulletin 2 which are not consistent with FRS102 or could be reflected in a different way.

Immediate application

Paragraphs 1.4 and 4.2 of the Update Bulletin require some of the amendments to be applied immediately or will be effective immediately. FRS 102 does not require immediate application, but permits early adoption as a choice.

While the amendments may be presented as “clarifications” to reflect the original drafting intention of FRS 102, they are amendments and were required as the original drafting intentions of FRS102 were not clear. Many charities will have to change the way they account for things, such as the payment to a parent charity from a subsidiary, and it is not practicable to switch to a new accounting regime with immediate effect.

We suggest that the application of the amendments to FRS 102 should be as required in FRS 102, so for reporting periods beginning on or after 1 January 2019, with early application permitted to mirror the restrictions provided in FRS 102.

Comparative information

We accept that FRS 102 requires comparatives for all amounts presented in the financial statements, including the notes, unless there is a specific exemption provided in FRS102.

We also note that the FRC wishes to “cut clutter” and the SORP making body would like charity accounts to be accessible and understandable. We are concerned that providing copious comparative information will make the accounts unwieldy in length and confuse the reader of the accounts.

We note that FRS102 provides exemptions for the comparatives for notes that are reconciliations, such as property, plant and equipment (section 17) and investment properties (section 16).

The SORP requires additional notes and disclosures that are over and above the requirements of an entity preparing accounts in accordance with FRS 102. As such, there is not scope for FRS 102 to explicitly provide an exemption for the comparative information. We ask that the SORP making body approach the FRC so that the SORP can provide specific exemptions for the comparative information for certain notes required by the SORP.

For example, the “movement in funds” note provides a reconciliation of the opening and closing balances for each class of fund. As a reconciliation, it may be possible to get an exemption from providing the comparative information. Another example is the detailed analysis of expenditure (SORP table 3) which is presented to reconcile the direct, grant making and support costs and the charitable activities they support.

Component accounting

Paragraph 3.4 removes the undue cost or effort clause and we accept that this cannot be avoided. This means that component accounting will be required where material. We ask that “where material” is added to paragraph 10.31 of the SORP to make this explicitly clear.

Legal obligation for Gift Aid payment from subsidiary

We accept that the amendments to FRS 102 now only permit the payment of Gift Aid from a subsidiary to be recognised where there is a legal obligation. We would like the SORP to address two implications that arise from this amendment.

Firstly, the SORP provides one example of a legal obligation, as a deed. This may give the impression that the only way to create a legal obligation is through a deed of covenant, which requires legal advice and therefore a cost to the charitable group. It is possible that other simpler and less onerous situations could create the necessary legal obligation. It would be helpful if other examples that the FRC accept as legal obligations could be cited in the SORP, such as:

- a resolution of the charity as member of the subsidiary
- explicit requirements in the governing document of the subsidiary

Secondly, the FRS 102 amendment was concerning the recognition of the liability from the perspective of the subsidiary. The amendments to FRS 102 did not address the income recognition for the charity as parent. We are concerned that there could be confusion and divergence in treatment of when the charity should recognise the income from the subsidiary. Therefore we ask that the SORP include in section 5 when the charity should recognise as income the Gift Aid payment from the subsidiary.

Paragraph 5.52 of the SORP requires that dividends should be accrued when the shareholder's right to receive payment is established. Gift Aid from a subsidiary as a distribution may be akin to a dividend, but is not a dividend. We recommend that an additional paragraph(s) be added to SORP section 5 to explain the treatment of income from a subsidiary for the charity as parent, perhaps providing some of the helpful background information in paragraph 3.5 of draft Update Bulletin 2.

Definition of financial institution

We understand that the change in definition of 'financial institution' was intended to narrow the number of entities caught by it. We are concerned that charities that make social investments are now likely fall within its scope. Section 34 of FRS 102 requires some three extra pages of disclosures for financial instruments which appears excessive in the context of the not-for-profit sector.

Q.2 Are there any other amendments to the Charities SORP (FRS 102) that you consider to be necessary based on the recent amendments to FRS 102? If so, please state the amendment to FRS102 and the relevant SORP paragraph(s).

SORP for smaller charities

We acknowledge that the SORP was originally written with smaller charities in mind and there was a desire to "think small first". When the FRSE SORP was retired, we understand that the SORP making body considered if a "Section 1A SORP" would be feasible as a replacement for the FRSE SORP, but the requirement to consider all sections of FRS 102 where material, made it effectively no shorter than the FRS 102 SORP. However, as FRS 102 grows and smaller charities are swept along with the requirements of medium and large companies, it seems to be time to reconsider if there can be a simpler SORP for smaller charities based on section 1A of FRS 102.

We would encourage the SORP making body to reconsider if a section 1A SORP could be a feasible option for smaller charities.