

Report

To: Charities SORP Committee

From: CIPFA Secretariat

Date: 22 February 2023

Subject: Presentation of the financial statements in the Charities SORP

Purpose

The purpose of this report is to outline the suggested amendments to SORP for modules 2 (Fund accounting) and 4 (Statement of financial activities) and the rationale for the suggested amendments.

Report

1. Introduction

1.1 At its meetings on 4 August 2021, 9 September 2021 and 22 October 2021, the Charities SORP Committee discussed matters pertaining to content on the presentation of the financial statements in the Charities SORP. Specifically, the topics of presentation of the Statement of Financial Activities (SoFA), notes on financial information, the funds note and materiality were discussed, having been identified as important topics during the previous stages of SORP development.

1.2 The Secretariat has prepared draft modules for the new Charities SORP based on the tentative advice provided by the Charities SORP Committee at these meetings. The Secretariat has reviewed and produced drafting recommendations for:

- module 2 (Fund accounting); and
- module 4 (Statement of financial activities).

The Secretariat notes that as the modules on the balance sheet and the statement of cash flows were not identified as in need of amendments during the reflection and problem-solving phase. The modules have therefore not been reviewed as part of this topic. The modules will be reviewed as part of the review of the other SORP modules at the later stages of the drafting phase.

1.3 The Charities SORP Committee has already reviewed some proposed amendments to module 4 pertaining to expenses and activity reporting. These amendments were presented to the Committee at its meetings on 26 July 2022 and 5 October 2022. For ease of reading and for this paper, **any amendments to module 4 agreed at previous Committee meetings have been accepted** (i.e. not presented as tracked changes) to allow the Committee to focus on the newly proposed amendments under this topic.

- 1.4 As can be seen in Table 1 below, the tentative conclusions on materiality reached at the reflection and problem-solving stage by the Charities SORP Committee indicate that no changes are necessary to the text of module 3 of the SORP (Accounting standards, policies, concepts and principles, including the adjustment of estimates and errors) with respect to materiality. Therefore, the Secretariat has not considered the drafting of module 3 at this stage but has included comments on materiality in section 2 of this report. Drafting proposals for module 3 will be presented to the Charities SORP Committee at a later meeting when the implications of FRED 82 *Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and other FRSs* (the FRED) are considered.
- 1.5 Annex 1 to this report provides a detailed analysis of the proposed amendments to the Charities SORP including the rationale for the proposals. Appendices 1 and 2 include the draft modules in full. Appendix 1 includes the 'clean' (i.e. untracked) draft modules. Appendix 2 presents the same modules in track changes so that the SORP Committee can identify new or revised content.
- 1.6 To aid detailed discussion of the draft modules, questions for discussion have been included throughout this report and in Annex 1.

2. Tentative advice provided by the Charities SORP Committee

- 2.1 The tentative advice given by the Charities SORP Committee at earlier stages in the process is summarised in Annex 3 below. The Secretariat produced the drafts of modules 2 and 4 in response to this tentative advice.
- 2.2 Table 1 below presents a summary of the tentative conclusions relevant to the text of the SORP on the topics related to the presentation of financial statements as the Charities SORP Committee reached at the problem solving and reflection stage of the process, and how the Secretariat has responded to the tentative conclusions.

Table 1

Topic	Tentative conclusions of the Charities SORP Committee	Response in drafting
Presentation of the SoFA	Retain current headings and analysis (<i>subject to discussion on activity reporting</i>)	Current headings and analysis have been retained.
	Consider allowing an option to change the sequencing of income and expenditure in the SoFA. (<i>Subject to FRC response to this point made in the first submission</i>)	The Secretariat does not recommend allowing an option to change the sequencing of income and expenditure in the SoFA. Additionally, at its meeting on 4 August 2021, the Charities SORP Committee agreed not to proceed with this suggestion (see paragraph 2.5 of this report below). Please see paragraphs 2.3 – 2.6 of this report below.
	Retain current requirement for SoFA comparatives but offer option by way of note.	The Secretariat cannot recommend allowing an option to present comparatives in a note as this does not accord with FRS 102.

Topic	Tentative conclusions of the Charities SORP Committee	Response in drafting
		<p>Please see paragraphs 2.7 – 2.11 of this report below.</p>
Notes on financial information	<p>Look to simplify requirements for smaller charities wherever possible.</p> <p><i>(Subject to FRC's response to the first submission made in respect of the application of Section 1A and simplification to the pensions note.)</i></p>	<p>The Charities SORP Committee is reviewing disclosure requirements on a module-by module basis as various topics are discussed.</p> <p>With respect to Modules 2 and 4, the Secretariat has retained the current approach that that module 2 applies in full to all charities. See paragraph 3.1 and question 5 below.</p> <p>Module 4 allows some charities in tier 1 to adopt the natural classification basis of reporting, which will likely reduce the burden of reporting.</p>
	<p>Develop a definition of 'transparency' as a criterion for editing the text.</p>	<p>The Secretariat is of the view that the development of a definition of transparency is unnecessary. The suggestion was made in the context of a discussion on decluttering the notes by removing some content where possible, but while retaining sufficient information to ensure transparency.</p> <p>The Secretariat is of the view that preparers should refer to the definition of "materiality" in such circumstances and that the development of a definition of transparency could lead to confusion.</p>
	<p>Evaluate practicality of weblinks in accounts.</p>	<p>The Secretariat considers that the use of weblinks in accounts is a regulatory matter rather than a matter that can be addressed through SORP drafting.</p>

Topic	Tentative conclusions of the Charities SORP Committee	Response in drafting
	Consider greater use of numerical definitions of materiality to ease the burden of reporting.	The Secretariat would note that such an approach does not accord with the specifications of FRS 102 regarding materiality. Thresholds are unlikely to be able to address the needs of users to enable them to take decisions. See paragraphs 2.17 – 2.21 of this report below.
Materiality	n/a	n/a
Funds note	No change but may need to revisit the discussion.	As no tentative conclusions were reached by the Charities SORP Committee on drafting requirements with respect to fund accounting, no response could be made in drafting. Some amendments to module 2 have been proposed to enhance the clarity of the SORP. These amendments are discussed in Section 3 of this report below. For information, the Secretariat notes that on review of the minutes from the meeting of the Charities SORP Committee held on 22 October 2021, it appears that the Committee wished to revisit its discussion of the presentation of the primary financial statements with respect to the use of multiple columns.

Sequencing of the SoFA

- 2.3 Paragraph 5.5 of FRS 102 requires that an entity present the items to be included in a profit and loss account in accordance with the general rules and formats of the relevant schedule of either [the Large and Medium-sized Companies and Groups \(Accounts and Reports\) Regulations 2008](#) or [the Large and Medium-sized Limited Liability Partnerships \(Accounts\) Regulations 2008](#). This requirement limits the ability of the Charities SORP to permit charities to present an ‘upside-down’ SoFA.
- 2.4 In the [annex](#) to its [first submission](#) to the FRC ahead of the drafting of the FRED, the SORP-making body proposed that an additional paragraph be added to FRS 102 to allow PBEs to reorder the line items within the income statement where the applicable SORP permits. This submission was made on 25 May 2021 and was based on feedback from the Engagement Strands.
- 2.5 The Secretariat would highlight that at its meeting held on 4 August 2021, the Charities SORP Committee tentatively advised that an ‘upside-down’ SoFA should not be introduced, noting a minority view that flexibility could be helpful to some. No changes have therefore been proposed regarding the sequencing (including an ‘upside-down’ SoFA).
- 2.6 This approach has been supported by a review of the FRED which indicates that although there are proposed amendments to Section 5 *Statement of Comprehensive Income and Income Statement*, there appear to be no changes which would explicitly permit a different sequence.

1. Does the Charities SORP Committee have any further comments on the presentation of the SORP?

Comparatives

- 2.7 Paragraph 3.14 of FRS 102 requires that an entity presents comparative information in respect of the preceding period for all amounts presented in the current period's financial statements. Paragraph 3.20 of FRS 102 further specifies that a complete set of financial statements means that an entity is required to present, as a minimum, two of each of the required financial statements (noting that the SoFA is a financial statement).
- 2.8 Paragraph 3.20 requires that two financial statements are prepared and therefore has clear specifications for comparative information (the two statements including the current and prior year).
- 2.9 Paragraph 3.21 of FRS 102 then states that "In a complete set of financial statements, an entity shall present each financial statement with equal prominence."
- 2.10 The Secretariat is also of the view that it is not possible to present a comparative SoFA that is of "equal prominence" to the current year SoFA if the comparative is presented as a note to the accounts. Presenting the comparative figures for the SoFA by way of a note would also reduce the comparability and understandability of the financial statements.
- 2.11 The Secretariat has therefore concluded that comparative information for the SoFA is a requirement of FRS 102 any changes to the presentation by way of a note would not be consistent with its provisions and risks reducing comparability and understandability. It has not therefore presented any proposals for change.

Natural classification

- 2.12 At the meeting of the Charities SORP Committee held on 26 July 2022, as part of a discussion on the inclusion of a definition of 'natural classification of expenses' in the SORP glossary, some Committee Members commented that natural classification should be available for both income and expenses.
- 2.13 The Secretariat reviewed financial reporting standards (FRS 102, IFRS for SMEs and IAS 1 *Presentation of Financial Statements*) to consider whether there is any standard practice for analysis of income. Further details are presented in [Annex 2](#) to this report. The Secretariat has determined that it is common for financial reporting standards to include requirements or illustrations regarding the analysis of expenses by function or nature. However, there were no equivalent requirements or illustrations for the analysis of income.
- 2.14 The Secretariat would therefore not recommend including specifying the analysis of income by nature in the SORP as this is not included in standards, including IFRS. However, paragraph 4.5 has been amended to provide clear guidance for smaller charities accounts preparers in tier 1 using the natural classification basis of reporting. The amendment provides minimal specifications, as classifications of income by nature do not normally occur within standards, but also to ensure that the reporting burden is minimised. This allows charities in tier 1 to choose their own headings to present income, provided the headings chosen are useful to the users of their accounts.
- 2.15 Table 2a has also been amended to support and underline this change by presenting fewer headings for income and removing the links to sections A1 – A5 of the module, which provide guidance to

charities that adopt the activity basis of reporting (and analysis). A cross-reference to paragraph 4.5 has been included in paragraph 4.28 and in an additional paragraph (4.34). Additional text has been proposed in paragraph 4.47 to emphasise that only charities adopting the activity basis of reporting are required to use the standardised headings specified in the SORP. These amendments have been proposed to ensure that the reporting burden for smaller charities is proportionate and that there are clear specifications for the reporting of income.

- 2.16 Should a charity have a material income stream within an income classification that requires separate reporting (e.g. income from research work within income from charitable activities, retail income within income from trading activities), the SORP allows for this. For example, paragraph 4.14 of the current SORP states that:

“All charities must disclose the nature and amount of any material item(s) of income or expenditure when this information is relevant to an understanding of the charity’s financial performance.”

This requirement has been retained in the redrafted SORP modules (see paragraph 4.17 of either Appendix 1 or 2).

2. Does the Charities SORP Committee agree with the Secretariat’s recommendation to differentiate between natural classification analysis and activity-based analysis with reference to expenses only based on precedents set in standards?

If not, how can the draft SORP be amended?

3. Is the Charities SORP Committee content with the amendments made to paragraph 4.5 and Table 2a to better reflect the reporting burden for charities adopting the tier 1 natural classification approach to analysis have over presenting income on the face of the SoFA?

If not, how can the draft SORP be amended?

Materiality

- 2.17 In response to the tentative advice that consideration be given to greater use of numerical definitions of materiality, the Secretariat reviewed the definition of materiality per FRS 102 and the content of FRED 82 *Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and other FRSs Periodic Review* (the FRED).

- 2.18 [FRS 102](#) paragraph 2.6 states

“Information is material – and therefore has relevance – if its omission or misstatement, individually or collectively, could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances.”

- 2.19 FRED 82 (paragraphs 2.11 – 2.12 of the FRED [consultation document](#)) similarly sets out that

“information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the users of general purpose financial statements make on the basis of those financial statements. Materiality depends on the nature or magnitude of information, or both.

An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.”

- 2.20 Neither FRS 102 nor the FRED (in common with other standards) set absolute or relative thresholds for materiality. Importantly, paragraph 2.14 of the FRED emphasises the needs of the users of an entity’s financial statements, requiring an entity to consider the characteristics of the users of the financial statements when determining whether information is material. The FRED retains the current approach to materiality that requires preparers to exercise considerable judgement about the needs of users when determining whether information is material.
- 2.21 The Secretariat would note that to be consistent with FRS 102 thresholds should not be set, as they are unlikely to be able to appropriately address the needs of the users of charities’ accounts to enable them to take decisions. The Secretariat has therefore not made any recommendations for thresholds for materiality as this would be inconsistent with FRS 102 and is likely to be inconsistent with any future changes to the SORP.

4. Does the Charities SORP Committee consider that there is any alternative approach (possibly in separate guidance or other educational material) to assisting accounts preparers with materiality?

3. Funds – Module 2

Approach to tiered reporting

- 3.1 A table indicating the requirements of different tiers included. Note that module 2 as redrafted retains the current approach that the requirements of the module will apply equally to all three tiers.
- 3.2 The Secretariat is of the understanding that the first and last bullet points in paragraph 2.33 are not required by regulations in England and Wales, being the disclosure of
- a summary of the assets and liabilities of each category of fund of the charity, if not provided by presenting this information in a columnar balance sheet; and
 - details of the planned use of any material designated funds, explaining the purpose of the designation.

Though the impact of reducing disclosure requirements for charities in tier 1 is likely to be marginal, the Charities SORP Committee is invited to consider whether to remove these two disclosure requirements for charities in tier 1.

5. Is this an appropriate approach to tiered reporting for module 2?

The SORP Committee is invited to consider

- a) whether any additional reporting requirements might apply to any of the tiers for accountability or transparency.
- b) whether disclosure requirements could be reduced for tier 1 charities as indicated in paragraph 3.2.



Separate section on Tangible fixed assets funded through an appeal, grant or donation

- 3.3 Content on tangible fixed assets funded through an appeal, grant or donation has been moved into a separate section of the SORP (paragraphs 2.28 and 2.29). This amendment has been proposed because in the existing SORP, content on tangible fixed assets funded through an appeal, grant or donation is included part-way through the section on restricted funds. However, the content notes that the asset can be categorised as either restricted or unrestricted. The amendment would improve the clarity of the provisions, make them easier to understand and avoid any unintended consequences which might arise from being included in the restricted funds section.

6. Is the Charities SORP Committee content with the new location of the content on tangible fixed assets funded through an appeal, grant or donation?

Disclosure of movements in funds – table

- 3.4 Additional lines have been proposed for inclusion in the outline summary of fund movements table at the end of module 2. This amendment has been proposed to illustrate the disclosure requirements of paragraph 2.32 in greater detail and to ensure that charities' funds disclosure can be reconciled to the SoFA.

7. Is the Charities SORP Committee content with the proposed amendments to the outline summary of fund movements table? Does the Committee have suggestions to further improve this table?

Use of the term "Capital"

- 3.5 In both modules 2 and 4, endowment funds have been referred to as "capital", reflecting terminology used in charity law. The Secretariat is concerned that there is potential for confusion as some preparers or users of the SORP may confuse "capital" referring to endowment funds with "capital" as used in discussions of capital expenses or capitalising assets, as this use of "capital" is common to accountants. However, the Secretariat recognises there is frequent use of this term in relation to funds.
- 3.6 The Secretariat has suggested cross-referencing "capital" to the glossary where the term is used to refer to endowment funds to avoid the potential confusion. The current glossary definition of "capital" is:

Capital is the charity law term used by the SORP for resources received by the charity which the trustees are either legally required to invest or retain and use for the charity's purposes. Capital is the term applied to permanent endowment where the trustees have no power to convert it into income and apply or spend it; the term also applies to expendable endowment where the trustees do have this power.

The Charities SORP Committee is invited to consider whether it would be beneficial to clarify in this glossary definition that “capital” as a charity law term should not be confused with capital expenditure on fixed assets.

8. a) Does the Charities SORP Committee consider there is potential for confusion with respect to the use of “capital” in the SORP?
- b) Is the Charities SORP Committee content that cross-referencing “capital” (when used in the context of endowment funds) to the glossary will adequately reduce the potential for confusion? If not, what further amendments to the SORP does the Charities SORP Committee recommend?
- c) Does the Charities SORP Committee recommend that the glossary definition of capital should be amended to clarify that it does *not* refer to expenditure on fixed assets when used in the context of funds?

Use of “specific trusts”

- 3.7 Paragraph 2.9 contained the only references to “specific trusts” in the SORP. References to “specific” trusts have been amended to read “special” trusts. These amendments are proposed to ensure consistent use of terminology throughout the SORP, improving the understandability of the SORP.

9. Is the Charities SORP Committee content to remove references to “specific” trusts from this paragraph of the SORP?

4. Other amendments

- 4.1 Annex 1 contains a detailed explanation of all proposed amendments made to modules 2 and 4 of the SORP. Amendments (other than those outlined above) that are similar in nature can be summarised as follows:

- **Amendments to the wording of requirements:** Several revisions to the wording of the SORP have been proposed for a range of reasons, including:
 - i. to ensure alignment and consistency with FRS 102
 - ii. to ensure consistent language is used across the SORP
 - iii. to simplify the language used in the SORP such that the SORP uses plain English where possible
 - iv. to improve the readability of the SORP (for example by removing any duplication across the SORP, or by reducing the length of sentences).

- **Cross-referencing:** The level of cross-referencing has been increased. Cross-references have been included to direct SORP users to other paragraphs within the same SORP module and entries in the glossary. This will reduce duplication across the SORP (i.e. where cross-referencing replaces content in a paragraph) and enhance the understandability of the SORP (e.g. by making clear which terms are defined in the glossary or where a SORP user can look for more the relevant originating specifications).
- **Amendments to the order of content within the modules:** Some proposals for re-ordering content within the SORP have been made. These amendments have largely been proposed to improve the flow of the SORP, and therefore its readability.

5. Detailed Drafting Proposals

- 5.1 Annex 1 itemises the drafting proposals for modules 2 and 4 as they relate to the presentation of the financial statements. Questions for discussion are included, although not every proposed adjustment to the SORP has a discussion question. Committee Members are invited to make comments or recommendations with respect to any suggested amendments, including those that do not have a specific discussion question.
- 5.2 Unless otherwise indicated, paragraph references in the table in Annex 1 refer to the paragraph numbers in the draft SORP modules presented as appendices to this report.

The SORP Committee is invited to consider the list of amendments and discussion question in Annex 1 relating to the drafting suggestions for the income modules within the SORP.

Disclaimer

This Charities SORP Committee paper including its Annexes has been developed to assist in the development and drafting of the Charities SORP. Readers should not treat the information contained in these papers as being definitive for the production of the Charities SORP FRS 102 (Third Edition) which will be subject to due process including a detailed consultation.

Rationale for proposed amendments to the Charities SORP

The table below is intended to be used alongside either Appendix 1 or Appendix 2, which contain relevant draft revised SORP extracts. Appendix 2 includes the draft revised SORP extracts with track changes on. Appendix 1 contains the draft revised text without track changes (for ease of reading).

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
Module 2 – Fund accounting			
Throughout	References to “expenditure” and “costs” have been changed to “expenses”.	These amendments are proposed to ensure consistent use of language throughout the SORP. This change in language was agreed by the Charities SORP Committee at its meeting on 5 October 2022.	<i>n/a – the Committee has already agreed this amendment.</i>
Throughout	Terms within this module that are defined in the SORP glossary have been coloured blue to denote a cross-reference to the glossary. It is anticipated that these definitions/explanations will be linked or otherwise made visible in an electronic SORP. (see also comments on amendments to paragraph 4.16 below regarding the inclusion of a definition of “general funds” in the glossary).	Cross-referencing to the glossary is suggested to improve understandability and avoid duplication across the SORP.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.1	A table indicating the requirements of different tiers included. Note that it is proposed this module of the SORP will be applied equally to all three tiers.	The proposed approach to tiered reporting in module 2 is covered in paragraph 3.1 of this report above.	<i>See question 5 immediately after paragraph 3.1 of this report above.</i>
Figure 1	Additional text has been included (i.e. “Income” has been changed to “Restricted income funds”).	This amendment has been proposed to better link the terminology in Figure 1 to that used in the SORP glossary.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
2.6	A cross-reference to paragraph 2.27 has been included.	This amendment is proposed to improve the understandability of the SORP by highlighting where users of the SORP can refer to for further information on the contents of the paragraph.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.8	The wording has been amended.	References to “earmarking” have been removed from the paragraph to ensure this type of fund is consistently referred to as a designated fund, with the intention of avoiding the potential for confusion. It is proposed that “during the reporting period” is deleted as designated funds created in previous reporting periods may still require separate disclosure.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.9	References to “specific” trusts have been amended to read “special” trusts.	The proposed approach to tiered reporting in module 2 is covered in paragraph 3.7 of this report above.	<i>See question 9 immediately after paragraph 3.7 of this report above.</i>
2.9, 2.10	An existing paragraph has been split into two.	This amendment is proposed to separate the explanation of restricted funds from the separate point, which is that there might be more than one restricted fund. This amendment is proposed to improve the readability of the SORP.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.11	A cross-reference has been included to paragraph 2.8.	This amendment is proposed to improve the understandability of the SORP by highlighting where users of the SORP can refer to for further information on the contents of the paragraph.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.5, old paragraphs 2.12 and 2.13, new	Content on tangible fixed assets funded through an appeal, grant or donation has	The proposed approach to tiered reporting in module 2	<i>See question 6 immediately after paragraph 3.2 of this report above.</i>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
paragraphs 2.27 and 2.28	been moved into a separate section. Paragraph 2.5 has been updated to reflect the creation of this new section.	is covered in paragraph 3.2 of this report above.	
2.15, 2.16	A single paragraph has been split into two. References to “expenditure” have been amended to “expenses”.	This amendment has been proposed to separate out content on the concept of charging expenses to a restricted fund from the accounting treatment of charging expenses to a restricted fund where there is an insufficient balance on the fund. This amendment is proposed to improve the readability and understandability of the SORP. Amendments to terminology have been proposed to ensure the consistent use of terminology across the SORP in line with the decision of the Charities SORP Committee to use “expenses” rather than “expenditure” at its meeting on 5 October 2022.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.17	Reference to “gift” has been removed.	This amendment is proposed to ensure consistency with amendments to module 5 of the SORP as agreed by the Charities SORP Committee at its meeting on 14 December 2022.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.19	The wording has been amended.	This amendment is proposed to improve the readability and understandability of the SORP.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
2.21	The wording has been amended to include “always”.	This amendment has been included at the request of the Joint Chairs and is proposed to improve the readability	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations</i>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
		and understandability of the SORP.	<i>with respect to the suggested amendments.</i>
Heading above 2.25	The Heading has been changed from “Accounting for the investment return on income and endowment funds” to “Accounting for the investment return on funds”	Paragraphs 2.26 and 2.27 cover unrestricted funds, restricted income funds and endowment funds. It is proposed that the section heading is amended to cover the full range of funds addressed by the section.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
Table below paragraph 2.34	Additional lines have been included in the outline summary of fund movements table.	The proposed approach to tiered reporting in module 2 is covered in paragraph 3.3 of this report above.	<i>See question 7 immediately after paragraph 3.3 of this report above.</i>
Module 4 – Statement of financial activities			
4.4	“expenditure” amended to “expenses incurred”	These amendments are proposed to ensure consistent use of language throughout the SORP. This change in language was agreed by the Charities SORP Committee at its meeting on 5 October 2022.	<i>n/a – the Committee has already agreed this amendment.</i>
4.5	Additional text included to explain the headings for income where charities in tier 1 adopt the natural classification approach to analysis.	This amendment has been proposed in response to a comment from a Committee Member at the meeting of the Charities SORP Committee on 26 July 2022 that it comment that it should be clear that charities preparing accounts by nature should not have to split income by activity.	<i>This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.</i>
Table 2a	Amendments have been made to the suggested headings that are included in the income section of the illustrative natural classification SoFA, i.e. to reduce the number of suggested headings and to avoid duplication of the suggested headings on the illustrative activity basis SoFA (Table 2b).	These amendments have been proposed to better illustrate that charities preparing using natural classification are permitted to choose headings for income to best suit the charity and the needs of the users of the accounts.	<i>This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.</i>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
4.12	<p>The terms “restricted income funds”, “unrestricted funds” and “endowment funds” have been coloured blue font. This is to denote that the three terms are all explained in the SORP glossary. It is anticipated that these definitions/explanations will be linked or otherwise made visible in an electronic SORP.</p> <p>The explanations of the three terms have been deleted from the paragraph.</p>	<p>This amendment is proposed to avoid duplication across the SORP. The explanations as deleted from this paragraph differed slightly from the explanations as included in the SORP glossary, creating the potential for confusion and misunderstanding.</p>	<p><i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i></p>
4.16	<p>An example of how additional columns can be included on the face of the SoFA has been added to the paragraph:</p> <p><i>... the charity may wish to show two columns within unrestricted funds, being “general funds” and “designated funds”</i></p> <p>Both terms have been coloured blue to denote a cross-reference to the glossary. “General funds” is not currently included in the glossary – a suggested explanation of the term is included in a comment alongside the paragraph.</p>	<p>The inclusion of an example of how a column might be subdivided is intended to improve the understandability and usability of the SORP.</p> <p>Cross-referencing to the glossary is suggested to avoid duplication across the SORP.</p>	<p>1. Is the Charities SORP Committee content with the proposed definition of “general funds”?</p>
4.19, 4.20	<p>Paragraphs 4.19 and 4.20 have been re-ordered. Re-wording is proposed.</p>	<p>The amendment to reorder the paragraphs has been proposed to present the definition of an extraordinary item before any explanatory content on extraordinary items.</p> <p>The amendment to include the word “highly” in the aspect of the definition of extraordinary items relating to extraordinary items being highly abnormal is to ensure the consistency of the SORP with FRS 102 and to</p>	<p><i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i></p>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
		emphasise that extraordinary items are extremely rare. Other re-wording is proposed to improve the readability of the SORP.	
4.22	The definition of a discontinued operation per FRS 102 (amended slightly to refer to a charity rather than an entity) has been included in a new paragraph.	This amendment is proposed to ensure preparers have a clear understanding of what a discontinued operation is before reading the content on understanding discontinued operations in the context of charities.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
4.25	Content on the definition of a discontinued operation has been removed from this paragraph.	This amendment is proposed to avoid duplication across the SORP. The content is no longer required following the inclusion of a new paragraph that defines “discontinued operation”.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
4.26	The required presentation of a discontinued operation has been separated into its own paragraph.	This amendment is proposed to improve the clarity and accessibility of SORP requirements.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
Paragraph 4.28 of the current SORP	This paragraph, containing the text “Income must be analysed according to the activity that produced the resources. Expenditure must be analysed by the nature of the activities undertaken.” has been deleted.	It is proposed that content on analysing income by activity is deleted from the SORP for the reasons outlined in paragraphs 2.12 – 2.14 of this report above. The content on analysing expenses by activity undertaken is deleted because it duplicates the requirement of the paragraph that immediately precedes the deleted paragraph.	<i>Question 2 included in the main report above refers to this proposed amendment.</i>
4.28	A cross reference to paragraph 4.5 has been included.	This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.	<i>This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.</i>

Paragraph reference	Amendment made	Reason for Proposed Amendment	Question for consideration
4.34	An additional paragraph highlighting how charities adopting natural classification may analyse income has been included, with a cross reference to paragraph 4.5.	This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.	<i>This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.</i>
4.38	Minor amendment to wording (inclusion of “therefore”). Bullet points have been changed to a list of items from a – f.	This amendment is proposed to improve the clarity and readability of SORP requirements. Bullet points have been changed to a list for ease of cross-referencing in later paragraphs (specifically paragraph 4.40, see below).	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
4.40	Inclusion a cross reference to the definition of primary purpose trading.	This amendment has been proposed to avoid the potential for confusion in the SORP. For example, a charity whose charitable objectives are linked to the promotion of certain musical genres may include income from concerts within income from charitable activities rather than, as indicated in this paragraph, income from trading activities.	<i>There is no specific question on this paragraph. Committee Members are invited to make comments or recommendations with respect to the suggested amendments.</i>
4.47	Additional text has been included to clarify that the standard income headings per Table 2b are only <i>required</i> for charities adopting the activity basis of analysis.	This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.	<i>This amendment is addressed in the main report above – see paragraph 4.14 and Question 3.</i>

Analysis of income and expenses across various financial reporting standards

Paragraph 2.13 of this report sets out that the Secretariat has reviewed extant financial reporting standards to establish how requirements about the analysis of transactions by nature are framed. The following includes the relevant extracts or summary of provisions relating to income and expenses (note that the inclusion of expenses is for completeness as tentative advice has already been given on that topic).

1. FRS 102

FRS 102 does not contain a section on the analysis of income and expenses. Rather, Section 5 *Statement of Comprehensive Income and Income Statement* is framed by the requirements of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410).

The only reference to analysis by either nature or function is in the Appendix to Section 5 (see detail below, emphasis added), which refers to the analysis of expenses. No mention is made of the analysis of income.

Appendix to Section 5

Example showing presentation of discontinued operations

This appendix accompanies, but is not part of, Section 5. It provides guidance on applying the requirements of Section 5 paragraph 5.7E for presenting discontinued operations. The example illustrates the presentation of comprehensive income in a single statement **and the classification of expenses within profit by function**. A columnar format is used in order to present a single line item as required by paragraph 5.7E, while still complying with the requirements of the Act to show totals for items such as turnover, profit or loss before taxation and tax.

2. IFRS for SMEs

IFRS for SMEs contains a section on Analysis of Expenses in Section 5 *Statement of Comprehensive Income and Income Statement* (see detail below).

The standard does not contain similar requirements for the analysis of income.

Paragraph 5.11 states, “An entity shall present an analysis of expenses using a classification based on either the nature of expenses or the function of expenses within the entity, whichever provides information that is reliable and more relevant.”

Paragraphs 5.11(a) and 5.11(b) provide more detail:

Analysis by nature of expense

- (a) Under this method of classification, expenses are aggregated in the statement of comprehensive income according to their nature (for example, depreciation, purchases of materials, transport costs, employee benefits and advertising costs) and are not reallocated among various functions within the entity.

Analysis by function of expense

- (b) Under this method of classification, expenses are aggregated according to their function as part of cost of sales or, for example, the costs of distribution or administrative activities. At a minimum, an entity discloses its cost of sales under this method separately from other expenses

3. IAS 1 Presentation of Financial Statements

In IAS 1, information is provided on the analysis of expenses by nature or by function (see detail below).

The standard does not contain similar requirements for the analysis of income.

Paragraph 99, in the subsection on *Information to be presented in the statement(s) of profit or loss and other comprehensive income or in the notes* states:

“An entity shall present an analysis of expenses recognised in profit or loss using a classification based on either their nature or their function within the entity, whichever provides information that is reliable and more relevant.”

Paragraphs 102 and 103 provide more detail:

102 The first form of analysis is the ‘nature of expense’ method. An entity aggregates expenses within profit or loss according to their nature (for example, depreciation, purchases of materials, transport costs, employee benefits and advertising costs), and does not reallocate them among functions within the entity. This method may be simple to apply because no allocations of expenses to functional classifications are necessary. An example of a classification using the nature of expense method is as follows:

Revenue	X
Other income	X
Changes in inventories of finished goods and work in progress	X
Raw materials and consumables used	X
Employee benefits expense	X
Depreciation and amortisation expense	X
Other expenses	X
Total expenses	(X)
Profit before tax	X

103 The second form of analysis is the ‘function of expense’ or ‘cost of sales’ method and classifies expenses according to their function as part of cost of sales or, for example, the costs of distribution or administrative activities. At a minimum, an entity discloses its cost of sales under this method separately from other expenses. This method can provide more relevant information to users than the classification of expenses by nature, but allocating costs to functions may require arbitrary allocations and involve considerable judgement. An example of a classification using the function of expense method is as follows:

Revenue	X
Cost of sales	(X)
Gross profit	X
Other income	X
Distribution costs	(X)
Administrative expenses	(X)
Other expenses	(X)
Profit before tax	X

Extract of Table Presented at the 16 February 2022 Meeting of the SORP Committee

Topic (date reviewed)	Tentative conclusions reached	Implications for the text
<p>Presentation of the SoFA (4 August 2021)</p>	<p>Committee members commented on matters around consistency of presentation as follows:</p> <ul style="list-style-type: none"> In their discussions, funders had focussed on consistency and the importance of being able to compare one year to the next. The merits of changing the order of presentation of the SoFA had not been the focus of discussions. Feedback from engagement strands indicated that their members were comfortable with the current, familiar presentation and were concerned that any new presentation would potentially increase complexity. The potential benefits of an upside-down SoFA in terms of improving financial governance had perhaps been overtaken by concern about the impact of making a change. For charities that are also companies, there are further potential complexities due to the need to adhere to company law as well as the SORP. <p>The Chair drew the discussion to a close with a tentative conclusion that an upside-down SoFA would not be introduced, noting a minority view that flexibility could be helpful to some. An option to allow flexibility could be considered at drafting stage, however, it was noted that options can increase complexity and therefore may not be the preferred route.</p> <p>The Chair closed the discussion with the tentative conclusion that it would be preferable for charities to be able to show comparative information either in the notes to the accounts or on the face of the SoFA. There is a need to think of the users of the accounts, including consideration of where the comparative information should be located to be of most use to the users of the accounts.</p> <p>There was broad consensus that there was no need to change descriptions. A sense check of the descriptions of income and (especially) expenditure may be useful. However, there was general agreement that, for reasons of consistency over time, the SORP should retain the current approach. There is not sufficient evidence that a new approach is needed.</p> <p>The Chair therefore expressed a tentative view that the SORP Committee would support steps to ensure natural classification is more obvious within the SORP and easier for charities to choose. Consideration as to setting out the natural classification format</p>	<p>Retain current headings and analysis (<i>subject to later discussion on activity reporting</i>)</p> <p>Consider allowing an option to change the sequencing of income and expenditure in the SoFA. (<i>Subject to FRC response to this point made in the first submission</i>)</p> <p>Retain current requirement for SoFA comparatives but offer option by way of note.</p> <p>Retain the 'natural' classification option. (<i>Note the November 2021 research</i>)</p>

Topic (date reviewed)	Tentative conclusions reached	Implications for the text
	would be given but it was not considered necessary to mandate the use of natural classification at the present time.	<i>making a case for mandating the format.)</i>
Notes to the accounts (4 August 2021)	<p>Several Committee members agreed that simplification of the notes would be beneficial; decluttering would be beneficial from both a user and an accounts preparer point of view. This could be considered module-by-module at the drafting stage. Feedback from the engagement strands as presented in Paper 3 was echoed by feedback from the Small Charities and Independent Examiners Engagement Strand, which supported simplification for smaller charities, in particular with respect to financial instruments and pensions.</p> <p>As users of accounts when making funding decisions, funders need information about the going concern status and governance arrangements in a charity to help inform the funders on the security of any grants. As preparers of their own charity accounts, funders understand the importance of transparency in disclosures. Such transparency allows an applicant for funding to perform due diligence on funders to ensure that funds are being sought from a source that does not run contrary to the applicant’s charitable aims. Decluttering was considered to be appropriate, but it was emphasised that transparency should be retained.</p> <p>If decisions are to be taken on retaining information in the notes for the purpose of transparency, a working definition of “transparency” would be required.</p> <p>It was noted that the SORP could make it clearer that disclosures may not be required for immaterial items.</p> <p>The Chair offered tentative conclusions as follows:</p> <ul style="list-style-type: none"> • At drafting stage, the option to allow weblinks in place of inclusion of information in the notes to the accounts can be revisited. • It is unlikely to be possible to direct users of the accounts to the SORP to establish common accounting policies as users are unlikely to access the SORP itself and the SORP is designed with preparers in mind. However, the SORP-making body will consider the other solutions suggested. • Subject to the outcome of the FRC’s periodic review of FRS102, consideration can be given to removing some notes for smaller charities, although decision-useful information cannot be removed from the notes. 	<p>Look to simplify requirements for smaller charities wherever possible.</p> <p><i>(Subject to FRC’s response to the first submission made in respect of the application of Section 1A and simplification to the pensions note.)</i></p> <p>Develop a definition of ‘transparency’ as a criterion for editing the text.</p> <p>Evaluate practicality of weblinks in accounts. <i>(Evaluate experience of the current SORP allowing weblinks for grant disclosures.)</i></p> <p>Consider greater use of numerical definitions of materiality to ease the burden of reporting.</p>
Materiality (9 September 2021)	In summary, the Chair concluded that there was not a consensus for asking the FRC to make changes to FRS 102 with respect to materiality, therefore no such changes would be sought.	-

Topic (date reviewed)	Tentative conclusions reached	Implications for the text
	The consensus was to retain the current content of the SORP with respect to materiality and to focus on educational materials and improving awareness.	
Funds note (22 October 2021)	<p>There is potentially a need for an education piece to highlight the importance of the funds note.</p> <p>The information in the funds note is useful and that an education piece would be helpful. Ideas around 'net assets over funds' and the presentation of the primary financial statements could be considered further at drafting stage as it had not been possible to reach a consensus.</p>	<i>No change but may need to revisit the discussion.</i>