CHARITY COMMISSION FOR ENGLAND AND WALES

OSCR Scottish Charity Regulator

Head of Programme
IFR4NPO
Chartered Institute of Public Finance and Accountancy
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By email

Charity Commission
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26 July 2021

Dear Sirs,

IFR4NPO initiative and PART 1: General NPO financial reporting issues

The Charity Commission for England and Wales, the Charity Commission for Northern Ireland and the Office of the Scottish Charity Regulator act together as the joint SORP-making body for charities in the UK. The joint SORP-making body is recognised by the Financial Reporting Council and is established to prepare an interpretation of UK-Ireland Generally Accepted Accounting Practice (GAAP) for application by charities preparing their accounts on an accruals basis to give a 'true and fair' view.

Charities are a particular form of non-profit organisation, established for purposes exclusively charitable in law, where any private benefit can only be necessary and incidental to achieving a charitable purpose. A distinguishing feature is that charities do not remit dividends or make distributions from retained funds to owners, either as members or shareholders, so that neither individuals or entities enjoy a private benefit for their own non-charitable use.

In respect of charities, UK-Irish GAAP is primarily the accounting standard known as FRS102, which is a composite of: the IFRS for SMEs, some treatments found in full EU-adopted IFRS, and aspects of company law with some specific adaptations on certain topics for 'public benefit entities'. The SORP-making body is therefore very familiar with the IFRS for SMEs.

We are supportive of the IFR4NPO initiative but would note some limitations to the progress even this initiative can bring. Please see the annex for our detailed response to the questions posed by Part 1.

In support, we would note:

- The Part 1 consultation rightly identifies distinguishing features of not-for-profit accounting and stakeholder needs that mean a sector neutral adoption of IFRS or IFRs for SMEs is inappropriate, for example the matter of non-exchange transactions and gift accounting and the absence of the motive of distribution and return on capital as a key driver for reporting.
- The main accountancy bodies train accountants in IFRS and so adapting the IFRS for SMEs ensures foundations of common understanding.
- In particular the IASB has developed a wide range of educational materials to support IFRS for SMEs in many languages and so the basic foundations can be readily studied and understood with the IFRS for SMEs intended to be a simplified derivative framework of full IFRS more proportional and less demanding for SMEs.
- The adaptive approach has proven a successful compromise in the UK with the first SORP published in 1988 and it does provide a sophisticated and comprehensive accounting solution if supported by narrative reporting directly addressing stakeholder needs. Previously, the SORP-making body wrote to the IASB in 2015 to encourage the IASB to develop an accounting framework for non-profits: https://www.charitysorp.org/media/642683/iasb-foundation-trustees-2015.pdf

In respect of limitations we would note:

- Neither IASB nor IPSASB conceptual frameworks or accounting standards have been developed with non-governmental non-profits and their stakeholders in mind. Indeed, the IASB specifically notes in the IFRS for SMEs that, 'The IASB's Standards are designed to apply to general purpose financial statements and other financial reporting of all profit-orientated entities (paragraph P7)'.
- The objectives of the IASB include, '…financial statements and other financial reporting to help investors, other participants in the various capital markets of the world and other users of financial information make economic decisions (paragraph P3)'. The SORP-making body is of the view that this focus has necessarily led to the emphasis on cash-flows for return on capital invested, imputing capital financing costs to transactions of all types and, wherever possible, an emphasis on fair value with reference to derived, imputed or market based valuations. Although this focus may be very suitable for investors evaluating market return and the economic capacity of an investment to generate cash-flows and a market return, our research shows that stakeholders in charities are looking for the social impact of their donation and accountability as to how money is spent. This very different focus, if reflected in the conceptual approach, we believe should yield very different accounting presentations and solutions.
- Due to the direction of travel of IFRS, our longer term view is that the adaptation of for-profit accounting standards based on an acceptance of their conceptual underpinnings will increasingly lead to accounting and financial reporting ill-suited to the needs of stakeholders in charities to the detriment of stewardship and accountability.

In view of our experience of the limitations that an adaptive approach can bring, we have already written to the FRC encouraging them to take the next step and develop a conceptual framework and a not-for-profit accounting standard in the medium term as a more sustainable and better solution than continuing to adapt the for-profit accounting framework.

Having taken views from our advisory Charities SORP Committee, we will not be responding to future parts of the project. Our focus now is on anticipating an updated GAAP and taking forward our preparations on updating the existing SORP framework for UK-Ireland charities. We do offer our every good wish for the future with this important initiative that looks to establish internationally the recognition of non-profits and their separate reporting needs.

In closing, we would recommend the IFR4NPO project look to user experience of writing the guidance as a foundation for the development of a non-profits accounting standard in the longer term.

Yours sincerely,

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