Minutes

Board	Charities SORP Committee
Date	1 December 2021
Time	10:00 – 13:00
Venue	Microsoft Teams

Joint Chair	Laura Anderson	*Office of the Scottish Charity Regulator (OSCR)*
	Nigel Davies	*Charity Commission for England and Wales (CCEW)*
	Rossa Keown	*Charity Commission for Northern Ireland (CCNI)*
Members present	Michael Brougham	*Independent Examiner*
	Tony Clarke	*Clarke & Co Accountants*
	Tom Connaughton	*The Rehab Group*
	Gareth Hughes	*Diocese of Down and Connor*
	Noel Hyndman	*Queen's University Belfast*
	Joanna Pittman	*Sayer Vincent*
	Carol Rudge	*HW Fisher*
	Max Rutherford	*Association of Charitable Foundations*
	Jenny Simpson	*Wylie and Bisset LLP*
In attendance	Alison Bonathan	*CIPFA, Secretariat to the SORP Committee*
	Sarah Sheen	*CIPFA, Secretariat to the SORP Committee*
Observers	Jane O'Doherty	*Financial Reporting Council (FRC)*
	Jelena Griscenko	*The Charities Regulator in Ireland*

| Claire Morrison | *Office of the Scottish Charity Regulator (OSCR)* |
| Amie Woods | *Charity Commission for England and Wales (CCEW)* |

Apologies	Caron Bradshaw	*Charity Finance Group*
	Daniel Chan	*PwC*
	Diarmaid Ó Corrbuí	*Carmichael Centre for Voluntary Groups*
	Tim Hencher	*Scottish Council for Voluntary Organisations*
	Neal Trup	*Neal Howard Limited*
	Gillian McKay	*CIPFA*

1.   Welcome, apologies for absences and declarations of interest   Action

1.1   The Chair welcomed SORP Committee Members to the meeting.

1.2   Declarations of interest

1.3   The Chair noted two standing declarations of interest:

Sarah Sheen has worked substantially for CIPFA on the IFR4NPO project and is secretariat to the CIPFA Charities and Public Benefit Entities Faculty Board.

Caron Bradshaw requested, by email prior to the meeting, for her interest as a Country Champion for the IFR4NPO project to be recorded as a standing declaration of interest. The Secretariat noted that Caron had requested that this interest be recognised for past meetings attended since being appointed as a Country Champion. The Chair accepted this as a standing declaration of interest.

2.   Minutes of the Meeting of 22 October 2021

2.1   No amendments were noted. The minutes of the meeting were accepted as an accurate record of the Committee's discussions.

3.   Matters arising: Notes of the research meeting of 11 November 2021

3.1   It was agreed that a point on the usage of presentation materials from PwC's presentation should be added to the notes of the meeting of 11 November 2021.

Otherwise, the notes were accepted as an accurate record of discussions after each presentation

4.   Paper 3: Summary report on Expenditure Classification

4.1   The Chair invited the Secretariat to introduce Paper 3.

The Secretariat introduced the main themes of the paper, being:

- the suggestion that a greater range of charities could be permitted to use natural classifications

- the view that natural classifications should be more prominent in the SORP

- possible improvements that could be made to SORP with respect to activity based classification.

The Secretariat noted the overlap between this paper and Paper 4 on support costs. Some feedback that had been provided in response to the briefing on Expenditure Classification had been summarised with other feedback on Support Costs in Paper 4 to avoid duplication.

The Secretariat referred to the questions posed at the end of Paper 3. The Chair invited comments from Committee Members in response to these questions, and on any other aspect of expenditure classification.

4.2   **SORP Committee discussion of Paper 3**

4.3   *Natural classification in the SORP*

The Secretariat noted that, if the SORP Committee is of the view that it would be appropriate, it would be useful to make natural classification more prominent in the SORP at drafting phase.

A Committee Member expressed support for natural classification but noted that not a lot of charities use it. The Committee Member therefore supported the idea of promoting natural classification in the SORP.

A Committee Member suggested sub-dividing the relevant SORP modules to separate natural classification from activity based classification. Each sub-section could then contain its own examples.

A Committee Member expressed support for activity-based reporting, as this encourages the creation of links between the narrative in the annual report, the financial information in the accounts and the work the charity undertakes. The Committee Member supported a better link to encourage charities to think about what their activities are and how the financial information from the accounts relate to them. The Chair noted that the public want to know what a charity's money has been spent on; activity-based reporting was designed as a response to this.

A Committee Member expressed a view that natural classification can encourage users of the accounts to view some expenditure as 'bad'. The Committee Member noted that care should be taken not to promote a presentation of the use of charitable funds that will lead to interpretation as 'good' or 'bad'.

A Committee Member noted that charities may adopt the activity basis for classifications because of their choice of software package. Adopting natural classification may therefore be more work for the charity. Further, the Committee Member noted that natural classifications may not help the charity to tell its story, while the activity basis for classifications better supports the narrative. However, the Committee Member agreed there is a case for enabling charities to make a better-informed decision about the use of natural classifications. The Committee Member supported the suggestion of separate sections in the SORP for natural classification and activity based classification and suggested the SORP could usefully include an illustrative SoFA for each approach.

4.4   *Extension of the option to adopt natural classifications*

A Committee Member indicated their support for the use of natural classifications by all but the largest charities.

A Committee Member noted that if a charity only has one activity, the notes are almost natural classification even where activity based classification is adopted.

Another Committee Member expressed support for extending the option of natural classifications. However, the Committee Member noted that care should be taken not to complicate the SORP with too many different options, therefore thought should be given to tying any extension of the option to use natural classification to the decisions made on tiered reporting. Another Committee Member agreed with this suggestion.

However, a Committee Member noted that the next tier may include charities that are too large for natural classifications to be an appropriate choice. The Committee Member questioned whether tiered reporting is the solution on this issue or whether the SORP could be the same for all charities, including a clarification that activity-based classification would be expected for charities that have a range of activities.

The Chair commented that Committee Members were seemingly uncomfortable with larger charities adopting natural classifications. The Chair asked, why this may be the case, if this supposition was true. A Committee Member expressed the view that they would be fine if a charity with income of, say, £10m were to use natural classifications, but suggested that it may be appropriate to require charities to include a note explaining their policy choice in this respect. This would ensure that charities gave thought to which expenditure classification approach would be most suitable for their circumstances. Another Committee Member expressed agreement with this but noted that accounting software may lead charities back to a 'default' position (of activity-based reporting). The Chair expressed the view that this may be the case, but this could not be a guiding factor when drafting the SORP.

A Committee Member commented that larger charities with income of, say, £10m are unlikely to only have one activity. The Committee Member expressed a view that in such cases, the use of natural classification is unlikely to allow a charity to effectively tell its story. The Committee Member would therefore caution against using natural classification for any charities other than smaller charities. Noting this word of caution, the Chair commented that a principles-based approach could be taken, allowing charities to decide on the approach expenditure classification that best fits their circumstances.

The Chair noted that when drafting previous iterations of the SORP, activity-based classification had been put forward in response to criticism of financial reporting not being meaningful in explaining how funds were used. It was felt that users of the accounts particularly needed to know the cost of a charity's activities.

The Secretariat asked whether this issue should be revisited at the same time as tiered reporting is considered. The Chair commented that this may be the necessary approach.

A Committee Member expressed a view that the ability to use natural classification should not be extended to a greater number of charities. The Committee Member supported better promotion of natural classification to the charities already permitted

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to adopt this method of expenditure classification. However, the Committee Member expressed a preference for larger charities to continue using activity-based reporting, and to improve this form of reporting.

A Committee Member noted that discussions had referred to a £10m threshold and questioned whether there could be a compromise. The Committee Member asked whether a threshold could be set higher than the existing threshold of £500k, but low enough that the SORP Committee would be comfortable. Another Committee Member suggested setting the threshold at £1m, in line with the audit threshold. The Committee Member commented it would be helpful to know the updated thresholds for tiered reporting in discussions such as this, therefore it would be useful to decide on the tiers as soon as possible.

4.5   *Other discussion points*

A Committee Member underlined the earlier discussions on the need to avoid the perception of some costs as 'bad'. The Committee Member was of the view that the SORP should minimise the use of 'other' for essential costs such as expenditure on safeguarding.

With reference to the questions posed in Paper 3, the Chair asked Committee Members whether they would support the retention of choice between natural classifications and activity based classification for smaller charities. Committee Members confirmed that they supported the retention of choice in this respect.

The Chair posed a question of whether activity-based reporting gives the public the information they want about charities, or whether natural classification better meets the public's information needs. A Committee Member commented that the 'public' could be a reference to the media, who pick up and report on items in charities' accounts. In this respect, transparency can be a double-edged sword. Care must be taken to avoid the publication of information that can be misunderstood, leading to the dissemination of flawed interpretations of charity accounts. Information needs to be accessible to, and understandable by, the users of accounts. The Chair, referring to the November 2021 research meeting noted that CCEW research indicated a reasonable number of members of the public do access information about charities.

The Chair asked Committee Members whether they would prefer a more guided approach to natural classifications in which the types of expenditure that charities are expected to report, such as salaries, heat and light etc., are listed in the SORP, or a more flexible approach. One Committee Member expressed a preference for guidance rather than making requirements a 'must'.

The Chair asked Committee Members if they wished to make any points on guidance for activity-based classification. No views were expressed at this meeting, however, activity-based reporting is the subject of a separate briefing paper that will be discussed at a future meeting.

A disconnect was noted between the accounts and the Trustees' Annual Report (TAR) for some charities. Specifically, the notes of some charities are prepared on the basis that the charity has only one activity, but on review it appears that the TAR indicates the charity undertakes more than one activity.

4.6   **Chair's summary of discussions of Paper 3**

4.7   The Chair noted that:

- the Charities SORP Committee agreed it would be preferable to retain the option currently offered to smaller charities in deciding between natural classification and activity-based reporting.

- there were a range of views and no consensus on whether it would be reasonable to extend natural classifications to more charities. This should be revisited at the same time as tiered reporting. However, the Chair noted that some Committee Members were against extending the use of natural classification.

- there was support for amending the SORP to allow smaller charities to make a more informed choice between natural and activity-based classifications, for example by use of separate SORP modules.

- there was support for the suggestion of including an illustrative SoFA using natural classification in the SORP, alongside an illustrative activity-based SoFA.

- there had not been support for giving guidance on what the natural classifications should be.

The Chair noted that discussions referred to how charities can be supported in 'telling their stories'. The principles underpinning expenditure classification should reflect how the charity is functioning and what the charity does. This suggests the need for a clear link between the SORP modules on expenditure and the TAR.

Comments around perceptions of expenditure as 'good' or 'bad' were noted, with the Chair commenting that this indicates the need to consider an education 'piece' for the users of the accounts.

The Chair thanked Committee Members for their contributions to the discussion.

5.   Paper 4: Summary report on Support Costs

5.1   The Chair invited the Secretariat to introduce Paper 4.

The Secretariat introduced the main themes of the paper, being:

- the need for an education 'piece' to avoid the perception of support costs and other overheads as 'bad'

- the role the SORP Committee can play in any education 'piece'

- whether 'support costs' should be removed as a heading, with lots of discussion but no consensus between engagement strands

- whether certain costs should be shown separately on the face of the SoFA

The Secretariat noted the feedback did not indicate a consensus in favour of making a substantive change to the SORP on the topic of support costs.

The Chair provided additional background by summarising the development of support costs and expenditure analysis in past versions of the SORP.

The Chair invited comments from Committee Members.

5.2 **SORP Committee discussion of Paper 4**

5.3 A Committee Member expressed the view that the current treatment of support costs leads to the unfair perception of some costs as 'bad'. To the extent that such perceptions are unfair, charity accounts are not providing users with the information they need to make informed decisions. The Committee Member would therefore support the removal of the support costs heading in a set of accounts. Another Committee Member expressed agreement with this view.

A Committee Member reflected that the requirement for separate disclosure of governance costs had been removed from the SORP because charities tended towards including only audit costs in the governance cost category therefore the category lost meaning. There is a risk that charities wanted to reduce this cost as much as possible because the media focused on it. The Committee Member therefore agreed with the previous contribution and the suggestion to remove requirements around separate disclosure of support costs. The Committee Member expressed a view that the cost category can be unfairly used to misrepresent charities.

A Committee Member highlighted the importance of language. Rather than referring to "support" costs, the Committee Member suggested referring to "enabling" costs. The Committee Member suggested amending the SORP to more positively present support costs. However, the Committee Member noted that this might not be necessary if we could have confidence that allocation and apportionment were not being used to 'disguise' some costs. In the experience of the Committee Member, allocation and apportionment does not always follow proper practice.

The Chair referred to previous research findings that indicate support costs may have become a proxy for understanding the difference a charity has made where insufficient information about a charity's impact has been reported. Improved impact reporting could therefore mitigate reliance on metrics around support costs when assessing charities.

The Chair asked Committee Members what contribution the SORP could make on an education 'piece'.

The Secretariat noted that different terminology, including a description of how expenditure enables charitable activity, would contribute to the broader education 'piece'.

A Committee Member commented that it is important for charities to incur sufficient costs to allow charitable outreach work to take place, noting that some charities would benefit from spending more on this rather than less. The Committee Member commented that the wording of the SORP could help avoid pressure on charities to minimise reported support costs.

A Committee Member commented that the SORP needs to explain the principles behind costs and why they are incurred. The Committee Member expressed the view that charities just have costs – how the charity reports its activities and operations will

depend on individual needs. The Committee Member questioned whether regulators would still require detailed disclosure from charities if requirements to disclose support costs are removed from the SORP.

The Chair responded and noted that OSCR has been assessing the information that it needs to request from charities in the context of the Annual Return that every charity completes, concentrating on how the information would be used to avoid unnecessarily asking for information. Furthermore, CCEW sometimes asks for information from outside the accounts. It cannot be guaranteed that CCEW will not ask for information on support costs irrespective of SORP requirements. The Chair noted that the SORP Committee cannot expect the charity regulators to give prior notice of what information they are planning to request.

The Chair asked if any Committee Members supported the use of more lines for expenditure on the SoFA. A Committee Member expressed a view that this suggestion would add clutter to the SoFA, therefore should not be pursued. Two other Committee Members agreed with this view.

5.4 **Chair's summary of discussions of Paper 4**

5.5 The Chair noted that the discussion of support costs goes back to the SORP helping charities to tell their stories. The Chair reflected that transparency can be a double-edged sword where it is possible for disclosures to be misinterpreted and used to misrepresent a charity. This had led to some Committee Members supporting the removal of requirements for support costs.

The Chair noted the potential benefits of a positive wording for the cost category, such as 'enablers'. The Chair reflected that this wording had garnered broad support from Committee Members and could serve as a platform for an education piece.

The Chair noted that costs are costs – it is up to a charity to best decide how to best present the costs required to undertake its charitable operations and activities.

The Chair noted that there was no support for including additional lines on the face of the SoFA, confirming this with the SORP Committee as a whole. Rather, the SORP Committee supported the use of narrative information to emphasise how the charity is functioning.

6. **Paper 5: Aims and principles of the SORP**

6.1 The Chair commented that a version of this paper was originally discussed by the SORP Committee over the summer and is now being presented following its publication. The Chair indicated that, as the process approaches drafting phase, it is helpful to reflect, as the drafting stage progresses, and compare proposed changes to the text with the aims as set.

The Chair noted that the principles are not in a hierarchy.

The Chair commented that where there are trade-offs at drafting phase, this document will guide decision making.

A Committee Member noted that there is not an action attached to Principle 4. The Chair commented that this principle can be amended to reframe it as an action. It was suggested that the principle would benefit from the inclusion of the words "to ensure".

A Committee Member noted, and the Chair confirmed, that the SORP Committee had previously discussed in reviewing the draft version that it needed to bring out the needs of beneficiaries in the Aims. *Secretariat note: Drafting Aim 1 makes reference to the needs of beneficiaries.*

7. Any other business including future Committee meetings

7.1 **Future meetings**

Dates for future meetings were noted per the agenda:

- the meeting on 12 January 2022 will focus on activity reporting. Additionally, a guest speaker from the Department of Business, Energy and Industrial Strategy (BEIS) will present on sustainability issues reporting by corporate entities in the UK.

- the meeting on 26 January 2022 will address sustainability reporting.

- Meeting with Engagement Strand Convenors: 16 February 2022

*Secretariat note: The meeting on **2 March 2022** was omitted from the agenda. Invitations for this meeting have already been sent to Committee Members.*

7.2 **AOB**

Joint Chair Nigel Davies noted that he will be leaving CCEW in mid-January; the first meeting in January will therefore be his last meeting with the SORP Committee. On behalf of the Joint Chair and the SORP Committee, Laura Anderson thanked Nigel for his contributions to the SORP Committee and the development of the SORP.

The Secretariat noted that the Annual Review had been drafted with the assistance of CIPFA for submission to the FRC. The Secretariat suggested that this is included as an item of business in January.

Joint Chairs/ CIPFA

The Secretariat reminded Committee Members of the practical arrangements for the Working Groups.

As the Joint Chairs do not attend Working Groups, the Chair thanked Committee Members for their contributions to the meeting and brought the formal part of the meeting to a close.