



**CHARITY COMMISSION  
FOR ENGLAND AND WALES**

**OSCR**  
Scottish Charity Regulator

**The Charity  
Commission**  
for Northern Ireland



**An Rialálaí  
Carthanas**  
Charities  
Regulator

Ms Claire Hadgrave  
FRC Review Secretariat  
Victoria 1  
1<sup>st</sup> Floor, Victoria Street  
London, SW1H 0ET

Charity Commission  
102 Petty France  
London  
SW1H 9AJ

6 August 2018

Dear Ms Hardgrave,

On behalf of the charities SORP-making body for the UK and Ireland we are responding to the call for evidence as a body with an interest in the FRC's effectiveness. The Charity Commission for England and Wales, the Charity Commission for Northern Ireland, and the Office of the Scottish Charity Regulator are established by law as the regulators and registrars of charities in the UK and currently comprise the charities SORP-making body. We are assisted by the Charities Regulator, the regulator and registrar of charities in the Republic of Ireland. Charities represent the larger part of the not-for-profit sector in the UK.

The Charities SORP is an interpretation of UK-Irish Generally Accepted Accounting Practice for charities and in developing the SORP framework our organisations' work closely with the FRC. As our expertise is confined to charities we have answered, see annex, those questions relevant to our remit.

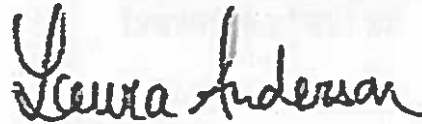
We welcome the review of the role and purpose of the Financial Reporting Council and would draw the following points to the review board:

- The FRC's remit for setting accounting standards extends to the Republic of Ireland and therefore any changes in this respect should be discussed with, and agreed by, the relevant authorities in the Republic prior to any changes being made.
- The terms of the review should encompass public benefit entities and a reference to public benefit entities be included in the mission statement of the FRC.
- Since the FRC's remit as setting accounting standards extends to not-for-profits we recommend at least three board members have either a detailed knowledge of the not-for-profit sector or professional expertise in that sector.

- It is the opinion of the SORP-making body that the nature and scope of audit needs a fundamental revision if the audit is to address both the needs of members of the company including trustees of a charity and wider stakeholders.

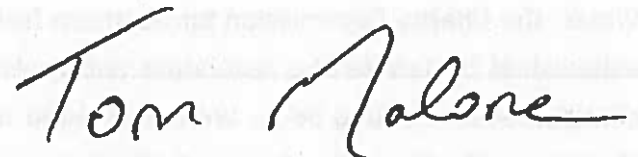
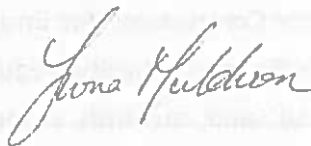
In the event of any enquiry concerning our response please contact Nigel Davies at the above address.

Yours sincerely,



Nigel Davies  
Joint Chair of Charities SORP Committee  
Head of Accountancy Services  
Charity Commission for England and Wales

Laura Anderson  
Joint Chair of Charities SORP Committee  
Head of Professional Advice and Intelligence  
Office of the Scottish Charity Regulator



Fiona Muldoon  
Joint Chair of Charities SORP Committee  
Monitoring and Compliance Manager  
Charity Commission Northern Ireland

Tom Malone  
Observer on the Charities SORP Committee  
Head of Compliance and Enforcement  
Charities Regulator

**Annex: Charities-SORP-making body response to the call for evidence: Independent Review of the Financial Reporting Council**

**Q1: What should the FRC's objective(s) be? Is its present mission statement the right one?**

The FRC's standards are applicable to other entities as well as the business sector and its role is also extended as the FRC also sets standards for public benefit entities. We would like to see this reflected in its mission statement. We would suggest that the FRC seeks: "to promote transparency and integrity in business and in public benefit entities"

**Q3: Are the functions and structure of the FRC still relevant and appropriate, or is there a case for any structural change? Should any of the FRC's functions move to other regulators?**

There is an important synergy in having the setting of auditing standards and accounting standards established by one body. Due to the FRC's scope including public benefit entities we advocate changes to the FRC's board and committee structure to more fully recognise this important role.

**Q5: How effective has the FRC been in influencing wider debates that affect its ability to deliver its objectives – for example, around audit competition, or its legal powers?**

The FRC has a good track record in our view in engaging with the accountancy profession and organisations representing sector or professional interests and views but wider engagement with other stakeholders could be improved. In our view a wider appreciation of the views of commentators, academics, researchers, journalists, and the public whether in the guise of investor in a company or donor to a charity. As a SORP-making body approved by the FRC, we recognise how difficult engaging with Government, the public and smaller social organisations can be and we are currently considering how we might also improve our engagement with other stakeholder groups.

**Q17: Can questions regarding the effectiveness of the FRC be separated from the wider question on whether change is needed to audit arrangements to take account of shifting expectations?**

We agree the views expressed by the Public Administration and Constitutional Affairs Committee (UK Parliament) on Kids Company with respect to professional firms: '...they were able to avoid making any examination of the wider issues that threatened the charity's existence. In the partial assurances they offered, the resulting reports may actually have obscured more than they revealed to those who read them'. The auditor cannot replace, nor should they, the duty of the investor or funder to have due regard to their interests but the failure of businesses and charities damages public confidence. Were the auditor asking harder questions with respect to the financial sustainability of the business model and culture of financial governance and reporting thereon this would enable greater transparency to funders and donors who would be able to make better informed decisions. Management would also have to address the concerns raised rather than simply view the statutory accounts as a compliance exercise. This issue is broader than the FRC and asks questions of the audit profession too.

**Q18: Has the FRC been effective in influencing the development of accounting standards internationally as well as accountable and effective in setting UK GAAP?**

The predecessor to the FRC established the first Statement for Recommended Practice for charities in 1988 and has gone on under the auspices of the FRC to create a reporting and accounting framework for charities which is world-leading and has been copied in several countries around the world. Although International Financial Reporting Standards are developed by the International Accounting Standards Board, the FRC retains an important role in maintaining local UK and Ireland Generally Accepted Accounting Practice including Statements of Recommended Practice. Local GAAP is used by the vast majority of entities. But for the FRC, the modern reporting and accounting framework for charities would not exist.

**Q20: Are there wider issues of financial and other reporting on which a stronger regulatory role would be desirable to better meet the information needs of investors and other stakeholders?**

We understand why this review is drawn with an investor focus but the public benefit entity sector is a significant employer and contributes to civil society. The NCVO almanac provides an estimate of the sector's size which indicates an economic impact of a scale comparable with that of the construction sector in terms of GDP.

We would advocate that the FRC has a remit to:

- actively report to the charity regulators adverse trends it observes in reporting and accounting; and
- assist the regulators in maintaining confidence in charity by making recommendations and issuing best practice guidance aimed at encouraging transparency, high quality accounting and reporting and effective charity stewardship and financial governance.

**Q27: Is there more the FRC could or should do to help reduce the risk of major corporate failure?**

It is the responsibility of owners and managers, or in the case of charities their trustees and senior management team, to effectively manage and operate their organisations. External parties, whether auditors, regulators or the FRC tend to be involved after an event or as an event is unfolding rather than at the point of the decision(s) that initiate that sequence of events.

There is a need to ensure effective accountability of directors, trustees or professionals for the decisions made and advice given. The effectiveness of these arrangements including the operation of and enforcement of ethical codes may merit review. Since much of this would fall to Parliament and devolved jurisdictions to effect through legislation we believe this is best done as a separate exercise.

**Q28: Is the FRC quick and effective enough to act on warning signs arising from its work on accounts and financial reporting, or on evidence of concerns over poor corporate governance?**

There may be greater scope for the existing corporate and charity sector regulators to work with the FRC. Such collaboration would help to identify cases of wrongdoing in reporting and accounting or poor professional practice so that effective action can be taken by the regulators, the professional bodies and the FRC. The FRC needs to have sufficient sanctions in cases of misconduct or poor practice.

**Q38: Is the Board's composition appropriate? Is it the right size? Does it have appropriate membership?**

Since the FRC's remit in setting accounting standards extends public benefit entities, we recommend at least three board members have either a detailed knowledge of the not-for-profit sector or have professional expertise in that sector. To assist the Board, a separate committee for setting the auditing and accounting framework for public benefit entities should be established.

**Q40: Is the Board's structure appropriate, including given the FRC's roles on standard setting, assessment and enforcement? Does the Board's accountability appropriately reflect its role and functions? Are its decisions appropriately transparent, bearing in mind the need to balance public interest and confidentiality?**

The FRC Board should include expertise in public benefit entities as the main aspect of some members CV rather than a personal interest, so that a good understanding of the needs of public benefit entities is available to inform the Board. The Republic of Ireland has approved the FRC as standard setter and so due regard should be had to reflecting the interests of the public benefit entities in the Republic of Ireland as well as that of the UK.

**Q45: Are there any other issues relevant to the terms of reference that respondents would like to raise?**

In framing your recommendations due regard should be given to the FRC's role in setting standards in the Republic of Ireland with any recommendations for change being agreed by the Republic of Ireland before these are effected. This is likely to remain the case until such time as the European Commission goes further than the Accounting Directive and takes responsibility for setting accounting standards within the EU for all entities.

In practice external stakeholders have an interest in the outcome of an audit and place a degree of reliance on it. In the opinion of the SORP-making body the current scope of an audit does not address these wider interests with its focus on the financial statements and in it being addressed to the members. Reflecting on the Carillion and Kids Company cases and the views expressed by the UK Parliament we are struck by the apparent gulf between what the public and stakeholders expect of an audit and what an audit apparently delivers. Also with respect to the financial statements (accounts) in our view the prevalence of discounted cash flow calculations in terms of measurement and presentation of otherwise simple transactions such as trade creditors, trade debtors, short leases, and investments and the use of technical terminology such as financial instruments in the accounts are raising barriers to the wider understanding of both members (trustees) and stakeholders. In our view the notes to the accounts potentially are not addressing those matters of real interest to stakeholders but are being cluttered with technical disclosures. Our research evidence from SORP consultation exercises particularly cites pension disclosures and financial instruments as in particular need of simplification. These trends need addressing.