

SORP Committee

Minutes of the SORP Committee Meeting of 24 January 2014 (Approved at the 12 February 2014 SORP Committee Meeting)

Contact: Nigel Davies, Secretary to the SORP Committee
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Present:

Tidi Diyan
Pesh Framjee (present for items 2 to 6)
Peter Gotham
John Graham
Keith Hickey
Noel Hyndman (present for items 1 to 3)
Ray Jones
Sam Younger, Joint Chair of the SORP Committee (joined the meeting for the discussion of income from government and subsequent items)

In attendance:

Caron Bradshaw, Charity Finance Group (CFG) (observer member)
Nigel Davies, Secretary to the SORP Committee
Mei Ashelford, Financial Reporting Council (FRC) (observer member)
Claire Stuart, Office of the Scottish Charity Regulator

Apologies:

Debra Allcock-Tyler
Laura Anderson
Tris Lumley
Fiona Muldoon (observer member)
Carol Rudge
Kate Sayer
Catriona Scrimgeour
Paul Spokes

Item 1: Opening remarks and declarations of interest

1.1 Ray Jones, acting Chair, opened the meeting and noted that Sam Younger would be joining the meeting later.

1.2 He asked if there were any declarations of interest to be made. No declarations of interest were noted.

Item 2: Approval of the minutes and matters arising

2.1 The minutes of the meeting of the 9 January 2013 were considered and approved subject to:

- minute 3.13 being changed to replace the words ‘three’ and ‘two’ with ‘few’ and ‘a few’; and
- minute 3.15 being changed with the substitution in the first sentence of the term ‘accounts of the combination’ in place of ‘consolidated accounts’.

Item 3: Discussion of controversial topics

3.1 Nigel Davies introduced this item and noted that paper 2.3 had been updated for the issues of performance reporting and materiality following the discussion at the SORP Committee meeting of 9 January. He noted that e-mail submissions on the topics covered by paper 3 had been submitted by Peter Gotham (re the SoFA), Carol Rudge (all items) and Tris Lumley (re performance reporting).

3.2 The discussion items were those where either a significant minority had feedback on a matter or where a particular point in a module had provoked a divergence of views from respondents. Revisiting these topics provided a further opportunity for reflection and debate before settling the text of the SORP. Paper 2.3 summarised each topic and the views received and offered a proposed solution or identified matters for discussion.

3.3 There were seven topics identified for discussion: prior year comparatives and the SoFA, the option of a single column SoFA, the retention of governance costs as a heading in the SoFA, and the analysis of expenditure in the SoFA, the recognition of income from legacies, the nature of performance conditions and expenditure recognition, the disclosure of senior staff pay, performance reporting, and materiality.

3.4 The first topic was the Statement of Financial Activities (SoFA). The Committee noted that the format of the SoFA was longstanding since SORP 1995 and that comparatives had only been provided for the total column and not for the unrestricted funds, restricted funds and endowment columns. A small number of respondents had noted that a strict reading of paragraph 3.14 of FRS 102 would require comparatives for each column. The Secretariat had had initial tentative discussions with the FRC on this point and the FRC had confirmed that this was also their view.

3.5 The practical effect of this requirement was considered. An 8 column SoFA would be: hard for users to interpret, cluttered and unwieldy. In the context of a group this would imply 4 SoFAs, parent and group current year and previous year and for a company group 2 summary income and expenditure accounts. The feedback from the SORP consultation to question 8 on the format of the SoFA was an emphatic endorsement of the current approach. There was already a requirement to reconcile movement in funds, albeit not replicating the SoFA format, and this had always been considered sufficient. If this requirement of FRS 102 was enforced, the Secretariat’s recommendation to amend the SORP module 4 was accepted and it was agreed that charities should have flexibility as to how to accommodate providing prior year comparatives.

3.6 The Committee considered the recommendation to allow the option of a single column SoFA with the analysis by heading across unrestricted, restricted and endowment funds being given in the notes to the accounts. Requiring a single column SoFA was emphatically rejected by the respondents to the SORP consultation but permitting the option might assist a minority of charities that wished to use this presentation. Although an option might be attractive, the Committee noted that the SORP research conducted in 2008-09 and the SORP consultation had provided overwhelming evidence that the sector and users of accounts saw the analysis of income and expenditure by heading by fund in the SoFA as an essential feature of charity accounting. The Secretariat's recommendation to permit an option for charities to have a single column SoFA was rejected.

3.7 A number of respondents had argued that the heading of 'governance costs' was a worthwhile heading in the SoFA. They had also noted that by only requiring governance costs to be disclosed as an item of support costs in module 8, those smaller charities opting to report on an alternate basis would not be required to disclose governance costs in the notes to the accounts.

3.8 The Committee reflected on the troubled history of identifying 'management and administration costs' and subsequently 'governance costs'. The heading of governance costs was often immaterial and arguably charities defined them differently despite the best endeavours of the SORP. The approach taken in 2005 was to move the emphasis to activities and outcomes and information on governance costs of larger charities (those subject to statutory audit) would still be available in the notes to the accounts. The Secretariat's recommendation to reinstate the heading of governance costs in the SoFA was rejected.

3.9 Some respondents argued that the current analysis of expenditure between costs of generating voluntary funds, fundraising trading and investment management costs in the SoFA was very valuable and that combining these items in a new heading of 'expenditure on raising funds' risked losing valuable information. The Committee noted that the simplification to the SoFA by reducing the number of headings had been very well received. Reinstating this analysis would reintroduce headings and would potentially be a source of clutter. However charities could always provide this information if it was useful and the SORP should be amended to prompt charities to consider providing a compatible analysis if this information if it would be helpful.

3.10 The second topic was the disclosure of income and a request by some respondents for a figure of income from government to be given. Nigel Davies noted that funders had shown an interest in the sources of income in the SORP research exercise and this interest had been shown in some responses to the subsequent SORP consultation. The Committee also considered Peter Gotham's recommendation that given the diversity of treatment he had found in the sector, that charities be given discretion as to how to classify income from grants rather than as now where the SORP directs that general grants are a component of 'income from donations and legacies' and performance related grants are a component of 'income from charitable activities'.

3.11 The Committee considered that the current differentiation of grant income should remain unchanged. It noted that although income from government was topical, arguably others might be interested in corporate donations or other sources of funding. The Committee noted that it had previously considered and rejected requiring charities to report by the source of income in the SoFA rather than by the nature of the income. To require a parallel analysis by funder would be burdensome. The Committee noted that funders, including government funders, can always ask for additional information relevant to awarding or monitoring their grants. Consequently the Committee rejected the Secretariat's recommendation to require larger charities to report in the notes to the accounts on the total income received from government sources.

3.12 The third topic was recognition of income from legacies and whether additional guidance was needed around identifying entitlement. Nigel Davies noted the diversity of accounting treatments identified by respondents and the importance of this issue to the charity sector. He mooted that a more standardised approach to a common form of non-exchange transaction might be desirable in view of the apparent diversity of treatment and potential inconsistency in the reporting of legacy income in the charity sector.

3.13 The Committee considered the Secretariat's recommendations. It was noted that there is a difference of view amongst charity legacy officers and legal advisers as to whether probate can be considered the point of entitlement. Indeed entitlement arguably actually arose from the death of the benefactor and the presence of a valid will. However other legal advisers argued that until a firm communication of a settlement or a court ruling was made no entitlement could be held to exist as a will could always be successfully contested. Whilst probate provided a useful public record of total assets and liabilities it was at best a starting point.

3.14 As to there being a diversity of treatment, the Committee considered it appropriate that charities deal with legacies based upon their own circumstances, the availability of historical information on income from legacies and the advice that they received. It was noted that whilst accounting standards required the practice of depreciation of wasting tangible fixed assets, the SORP did not specify what method to use or standard economic lives for classes of assets. Arguably legacies were no different in requiring a degree of flexibility for charities to apply their own judgement and estimation techniques. Although charities with only occasional legacies might find the additional recommended guidance helpful it would hamper those charities with a well-developed policy of income recognition which receive many legacies. However the additional text regarding the use of mathematical models was useful.

3.15 The Committee rejected the Secretariat's recommendation to establish the granting of probate as the criterion for entitlement but accepted the recommendation to add text concerning a portfolio approach to recognising income from legacies.

3.16 The fourth topic was the nature of performance conditions and the recognition of expenditure. Nigel Davies noted that some respondents sought greater clarity over how the review conditions in a grant award could be construed as a break point thereby only requiring the recognition of expenditure for the commitment up to the point of the review. The Committee debated the Secretariat's proposal to require the presence of a particular clause notifying the recipient of a review in order for that break point to be present.

3.17 The Committee noted that FRS 102 emphasised two aspects: that the recipient had a realistic expectation that the funds would be paid and the grant-maker had no realistic ability to withdraw from that commitment. The award therefore had to be communicated and the form and content of that communication together with the experience of both the grant-maker and recipient informed the expectations of the recipient. The SORP was drafted at a principles level and this enabled grant makers to develop their own approaches. The Committee rejected the Secretariat's recommendation to require the presence of a particular clause as this had the disadvantage of inflexibility and introducing a rule. If the grant-maker has a right to withdraw, has a capacity to withdraw, and has communicated this to the recipient then the review will have substance.

3.18 The fifth topic was the disclosure of the pay of the most senior member of a charity's staff and the recommendation by some respondents that the public interest was better served by disclosing the remuneration policy for senior staff instead. In introducing this item, Nigel Davies noted this has provoked much discussion at the SORP consultation events and in the responses. Although funders desired to see the disclosure of the pay and post held by a charity's most senior member of staff, this proposal had been emphatically rejected by charities, sector umbrella bodies and auditors.

3.19 The Committee considered the feedback from the consultation and the recommendation by leading umbrella bodies and others that the public interest is better served by disclosure of the remuneration policy for senior staff in the trustees; annual report. The Committee accepted the Secretariat's recommendation that such a policy disclosure be required of larger charities and upheld the decision not to require charities to disclose the pay and post held by the charity's most senior member of staff. In view of the public interest, the Committee decided that the disclosure by banding of salaries should be extended to all charities as this would give useful information for decision making by those giving and funding charity and better meets the requirement of users than disclosing a single individual's salary.

3.20 It was noted that the disclosure of trustee remuneration and expenses was held necessary for reasons of transparency to donors and in the public interest. It was noted that a similar level of disclosures was not required under the FEHE SORP of universities and colleges. This was seen as anomalous as these were also charities whereas a similar requirement might not be anticipated in the SORP for Registered Providers of Social Housing as many registered providers of social housing are not charities.

3.21 The sixth topic was that of performance reporting and whether it was appropriate for the SORP to use the term 'impact' in reporting performance. Nigel Davies noted that the term had been defined and used in the 2005 SORP and that the only new features added to module 1 concerned references to wider society and the reporting of successes and failures. He noted that no recommendations were made by the Secretariat as to how to modify the text but questions were set out to assist debate.

3.22 The Committee noted that although the term impact was ill defined it was widely used and therefore the SORP must cover it. The Committee was broadly content with the SORP's requirements but paragraph 1.43 of the Exposure Draft might be more clearly worded to recognise that impact reporting, though worthwhile, is difficult. Noel Hyndman agreed to draft some text for adoption.

3.23 The final topic was materiality and whether the SORP might usefully give greater context for the application of this concept in the modules so as to assist practitioners. Nigel Davies noted that the SORP's definition was based on FRS 102 and that materiality required the exercise of judgement. Again the Secretariat offered no recommendations but a number of questions to prompt discussion.

3.24 The Committee agreed that practitioners and auditors needed freedom to apply judgment in those areas where the SORP did not specify an item was material. However a bit more context might be helpful where a specific mention of materiality is made in a module in order to assist practitioners.

3.25 It was recommended that the Secretariat should take the following actions or make the following amendments to the SORP:

- **The Secretariat to request the FRC treat the analysis of funds in the SoFA as being a charity SORP specific requirement and therefore not within the scope of paragraph 3.14.**
- **Module 1 be amended in accordance with text to be provided by Noel Hyndman regarding reporting performance.**
- **Module 1 be amended to require that larger charities must disclose their remuneration policy for senior staff.**
- **Amend module 4 as a back stop to advise charities that comparatives should be provided as things stand for each column and provide suggestions as to how this might be done.**
- **A single column SoFA option not be permitted.**
- **The heading of governance costs should not be restored and the disclosure of governance costs only be required as a component of support costs by those charities reporting on an activity basis in the SoFA.**
- **Module 4 be amended to note that charities may choose to further analyse expenditure on raising funds between its components.**
- **Module 5 be amended to note that charities with detailed historical information may apply a portfolio approach to recognising income from legacies by applying a formula or mathematical model.**
- **Module 7 consider information sheet 1 and incorporate any helpful additional advice about recognising commitments.**
- **Module 9 be amended to extend the disclosure of salaries over £60,000 in bands to all charities.**

- **The Secretariat draws to the FRC’s attention the anomaly in the disclosure of trustee remuneration between the charities and FEHE SORPs.**
- **The Secretariat reviews each module for circumstances where materiality is mentioned and adds some additional context where this might be helpful to users of the SORP.**

Item 4: FRSSE SORP

4.1 Ray Jones introduced this item and referred the Committee to paper 3. Since the Exposure Draft SORP had been put out to consultation there had been further developments with regard to the future of the Financial Reporting Standard for Smaller Entities (FRSSE) with plans now well advanced to bring into effect the new European Union Accounting Directive on company reporting. Although not-for-profit companies are scoped out of the Directive’s application, a change in company reporting will mean the withdrawing of FRSSE 2015 and its replacement with a new framework.

4.2 He noted that although the Invitation to Comment had flagged uncertainties about the future of the FRSSE, the feedback to question 15 that the SORP should support the FRSSE had drawn emphatic support this endorsement preceded these latest developments. He also noted that although many warmly welcomed the SORP supporting the FRSSE, some, principally the Institute of Chartered Accountants Scotland (ICAS), had questioned the blended approach taken by the Exposure Draft as not fully recognising the FRSSE.

4.3 Before the SORP Committee was a version of the Exposure Draft which had all references to FRS 102 and FRS 102 measurement bases and terminology removed and replaced by FRSSE measurement bases and terminology. He noted that in practice in most situations the application of the FRSSE led to the same end result, for example in place of impairment the FRSSE talks of written down value. The FRSSE in practice was not a standalone standard as it frequently cross referred to old UK-Irish Generally Accepted Accounting Practice (old GAAP) and required users to have regard to the UK Companies Act. It also had virtually nothing to say on public benefit entity (PBE) issues. Once old GAAP is withdrawn applying the FRSSE becomes problematic and unclear.

4.4 He took the Committee through the proposed approach set out in section 3 of paper 3. He recommended that in order to apply the FRSSE once old GAAP is withdrawn that: if the FRSSE specifies a treatment the SORP reflects it, for a non-charity specific issue where the FRSSE is silent that the SORP is taken to represent current practice, where the SORP addresses a charity specific issue not found in FRS 102 or FRSSE the SORP is taken to reflect both current and accepted practice and that where the SORP reflects a PBE issue dealt with in FRS 102 it is considered current practice. The effect would be a separate SORP for users of the FRSSE with the same 29 modules but with the content of the modules rephrased and edited to closely align with the terminology used by the FRSSE.

4.5 The Committee noted that in all likelihood the FRC would be consulting on the future of the FRSSE soon and, given the uncertainty, a separate SORP for FRSSE users would avoid FRS 102 users being disrupted by the SORP having to be withdrawn because of a new FRSSE. Had the time-line for developments been clearer with regard to the implementation of the Accounting Directive by the Department for Business Innovation and Skills then perhaps the consultation might have asked instead if the FRSSE should be supported at all. However withdrawing the FRSSE option was not possible without a fresh public consultation and the need for the sector to have a framework in place was the paramount concern.

4.6 The Committee agreed with the way forward proposed which offered robust and coherent framework for the FRSSE SORP. The Committee were undecided whether to recommend imposing new developments in GAAP which are not found in the FRSSE, specifically the 5 year history of acquiring heritage assets and the recognition of a liability for agreements to pay additional contribution to a defined benefit pension scheme to make good a deficit where the charity's share of the actuarial deficit cannot be determined. It was noted that advocates of the FRSSE saw the ability not to include these items as being one of its key advantages over new GAAP.

4.7 It was noted that the draft FRSSE SORP would be updated for those changes to the FRS 102 version of the SORP already agreed by the Committee which were applicable. Since the FRSSE updates awaited the FRS 102 version being prepared the FRSSE SORP might not be ready for the 12 February meeting. In view of the tight timescale for its completion prior to submission to the Committee for Public Benefit Entities review (CAPE) in March, the Committee agreed that the FRSSE SORP might be approved, if necessary, by e-mail circulation.

4.8 It was recommended that the Secretariat should take the following actions:

- **The Secretariat to develop the FRSSE SORP using the principles set out in section 3 of paper 3.**
- **The FRSSE SORP be approved by e-mail circulation as a fall-back position if the text is not ready for the 12 February meeting.**

Item 5: Update from the FRC

5.1 Mei Ashelford advised that she had no further update following the meeting of 9 January. She noted that the SORP Secretariat had been invited to participate in the FRC's Technical Advisory Group which is taking forward work on the FRSSE.

Item 6 Any other business

6.1 Nigel Davies noted that the meeting for late March was tentative as it may not be required if there are no matters following the Committee for Public Benefit Entities review of the SORP to refer back to the SORP Committee. Dates for this tentative meeting, and the final meeting of the SORP Committee had yet to be settled.

6.2 He noted that an item for the June meeting would be the report of the Consultative Council of Accountancy Bodies' research into the need for a not-for-profit international accounting standard.

6.3 There being no other business the meeting closed.