SORP Committee

Minutes of the SORP Committee Meeting of 13 March 2013
(Approved at 5 June SORP Committee Meeting)

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Present:

Laura Anderson, Joint Chair of the SORP Committee
Debra Allcock- Tyler
Pesh Framjee
Peter Gotham
John Graham
Keith Hickey
Noel Hyndman
Ray Jones
Carol Rudge
Kate Sayer
Sam Younger, Joint Chair of the SORP Committee

In attendance:

Caron Bradshaw (observer member)
Nigel Davies, Secretary to the SORP Committee
Fiona Muldoon, Charity Commission Northern Ireland (observer member)
Joanna Spencer, Accounting Standards Board (observer member)

Apologies:

Tidi Diyan
Tris Lumley
Lynne Robb
Catriona Scrimgeour
Paul Spokes

Item 1: Opening remarks and declarations of interest

1.1 Laura Anderson opened the meeting and on behalf of the Committee she thanked MHA MacIntyre Hudson for hosting the meeting.

1.2 Laura Anderson noted that a key milestone had been reached. With this meeting, the initial drafting process for the new SORP would be completed. She thanked Committee members for all their contributions over the past two years with the development and review of the SORP modules. In connection with the papers for this meeting, she thanked Pesh Framjee for conducting the equivalent of a 'fatal flaw' exercise on the draft SORP in preparation for this meeting.

1.3 She invited 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 26 February 2013 were considered and approved.

Item 3: Review of the complete draft SORP

3.1 Nigel Davies introduced this item by referring to paper 2. He noted that the final changes made to the draft SORP reflected the outcome of a meeting between the Financial Reporting Council's (FRC) project team and the representatives of the joint SORP-making body (Laura Anderson, Ray Jones and Nigel Davies) held on 28 February. That meeting had been an opportunity to discuss those areas of charity accounting which differed from for-profit reporting with the project team. It provided an opportunity for the FRC's project team to identify any changes needed in the draft SORP so that it was consistent with the new Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102).

3.2 The FRC's project team identified a number of changes that were essential if the draft SORP were to be in keeping with the views of the Accounting Council. These changes, together with substantive changes recommended by the Committee at its two February 2013 meetings, were now reflected in the draft presented.

3.3 The SORP Secretariat, using information provided by the FRC's project team, had reviewed the draft for consistency with the new FRS 102. A number of changes had been made to the draft to align it with the settled text of FRS 102.

3.4 Taken together, there were 22 substantive changes being recommended by the SORP Secretariat. In addition to these, Ray Jones had drawn up a schedule of the drafting points identified by Pesh Framjee and had identified a further 19 substantive matters for the Committee's discussion. To facilitate the discussion it was agreed that the drafting changes recommended by paper 2 would be reviewed first.

3.5 In discussing the changes recommended in Paper 2, the Committee noted that there was a tension between commercial sensitivities of charities involved in competitive tendering exercises and the needed for transparency by charities in their finances and activities to donors, funders, and the public. Charities are not for-profit entities and have a broader range of stakeholders and different values and ethos. The Committee concluded that where a balance has to be struck, the SORP must err on the side of transparency. However where flexibility can be offered to charities to describe and disclose their income and expenditure, provided it is not detrimental to being sufficiently transparent to beneficiaries, funders and the public, that flexibility should be offered. In particular, the draft already allows for the aggregation of similar expense items and so where a charity enters into several contracts in relation to taking forward a particular activity, there is already considerable scope for aggregating the costs of those contracts. However, if a charity carries out its operations through a single contractual arrangement then there is little that can be done to disguise the contract's costs.

3.6 Considering each of the amendments recommended in Paper 2, the Committee agreed that:

- **The proposed changes to the introduction module be made, subject to the phrase ‘application guidance’ be replaced with ‘how to apply’;**
- **the Committee decided to revert to the disclosure of going concern as being made solely as an element of accounting policies rather than to having both an accounting policy disclosure and a discussion of going concern in the trustees’ annual report;**
- **charities should be encouraged to disclose in the trustees’ annual report any uncertainties about going concern;**
- **the accounting policies module should include a reference to charities not applying international financial reporting standards;**
- **the figure illustrating the FRSSE accounting choice should be revised to more clearly explain the effect of applying the FRSSE;**
- **where investment income is material it must be disclosed separately from other income;**
- **gains and losses on investments shall be shown before striking the total for net incoming resources/ resources expended;**
- **internally generated databases cannot be capitalised;**
- **for the avoidance of doubt, the SORP should specifically rule out the use of the accrual model when recognising income from government grants;**
- **to comply with FRS 102 goods donated for distribution are normally recognised at the time they are received rather than when distributed;**
- **that where extended credit terms provide for settlement to be deferred for more than 12 months it must be discounted (if material) to present value whether or not the item becomes current at the reporting date; and**
- **the proposed extra section on the impairment of financial assets be added.**

3.7 Ray Jones introduced the discussion of Pesh Framjee’s drafting observations. He referred to the schedule of changes and each of the substantive issues was discussed in turn. It was agree the SORP secretariat would amend the non-substantial items identified in the schedule where to do so would improve the clarity of the drafting.

3.8 The Committed considered the conclusion in the draft SORP that contract income is always unrestricted income in the accounts of the recipient charity. Although this would normally be the case, the application of substance over form meant that there were certain circumstances when in substance income from a contract is analogous to restricted funds even though it is not a gift under trust law.

3.9 Contract income should be included with restricted funds when the contract is for a specific purpose and any surplus on that contract, if any, could only be spent on that purpose or returned to the provider of the funding and is not freely available for any purpose of the charity. The Committee noted that statutory bodies in moving away from grants to contracts were specifying contracts in narrow terms and were even providing that any funds left over, if not used for the specific purpose being funded, must be returned to the funder. Ray Jones mentioned the possible VAT advantages in charities seeking funding for overseas projects through contractual arrangements as the supply of overseas services is zero rated allowing a higher proportion of input costs to be reclaimed. He was however concerned that showing contract income as restricted might blur corporate property and property held on specific trusts by the company charity.

3.10 Heritage assets remained an area of debate given that charities may use assets with heritage characteristics as operational assets in carrying forward their work. The motive for the original standard FRS 30 appeared to be ensuring that operational or heritage assets are, wherever practicable, reported on the balance sheet. However, the Committee noted that the heritage asset accounting treatment did permit the non-capitalisation of such assets but did require fuller disclosures, including preservation and management policies.

3.11 In the context of charities, it was questioned whether having conservation or preservation purpose meant necessarily that the asset should be accounted for as a heritage asset. Charities may use assets with heritage characteristics operationally. However, the distinction between heritage and operational assets could be difficult conceptually as museums and galleries and many preservation charities actually use their exhibits ‘operationally’ to further their ‘operational’ purposes relating to the conservation and preservation of those assets. This issue was debated and focused primarily on when a asset could or could not be regarded as ‘operational’ and the circumstances, if any, when there may be an element of discretion as to whether an asset was regarded as an item of property and equipment or a heritage asset.

3.12 In discussing the application of the branch accounting method the Committee agreed that it should not be extended to entities that are properly classified as subsidiaries by accounting standards. However, the clarification that special trusts only exist in England and Wales in the draft SORP may inadvertently lead to a change in practice when considering similar arrangements that may exist outside of England and Wales. Consideration should be given to preserving the branch accounting for arrangements outside of England and Wales that are in substance similar to special trusts but are not subsidiaries. Subsidiaries must be consolidated under accounting standards.

3.13 The Committee concluded that the new module ‘charities as subsidiaries’ was needed to ensure transparency. The disclosure of the details of the parent entity ensures that donors, funders, beneficiaries and the public fully understand the operational context of the charity and of any entity deemed to control it for accounting purposes.

3.14 The Committee agreed the following changes after considering the schedule of drafting points drawn up from the observations provided by Pesh Framjee:

- **the section within the accounting policies module be amended to remove the recommendation that the presentation currency be that of the jurisdiction of registration;**
- **the analysis of expenditure should not be prescriptive; instead flexibility is needed so that charities can provide an appropriate analysis relevant to their circumstances and activities;**
- **that in a very specific set of circumstances where contract income relates to a specific purpose and any surplus can only be spent on that purpose and not for any purpose of the charity or is to be returned to the funder then that contract income may be presented as restricted income;**
- **the reference to market price be dropped in the section on measurement bases in the module on accounting for donated goods, facilities and services because fair value is not necessarily a retail price, or wholesale price;**
- **the introduction to the module on accounting for donated goods, facilities and services should reassure users that practical considerations are taken into account for measurement and recognition;**
- **the detailed examples given for the recognition of multi-year grants are no longer needed as the criterion of probable transfer of economic resources is used in the recognition of a constructive obligation. The substance of any review clause is a factor in determining recipient expectations and the funder's ability to withdraw and therefore the probability of their making the payment;**
- **a consultation question be asked on whether grant making disclosures can be provided in a separate publication;**
- **an explanation of an operational asset be added to the heritage asset module with a consultation question asking whether this approach was the way forward for differentiating operational and heritage assets;**
- **the extension of the branch accounting method to a separate legal entity which is not a subsidiary provided it is administered by, or on behalf of, the reporting charity and whose funds are held for specific purposes which are within the general purpose of the charity be reinstated supported by a consultation question;**
- **in connection with the revaluation of fixed assets, substitute the requirements of the valuer as per FRS 102; and**
- **in the charities established under company law module the reference to filing requirements should be dropped and the table setting out the requirements of summary income and expenditure account simplified.**

Item 4: Next steps

4.1 Ray Jones introduced this item and reported that a domain name had been purchased for the planned SORP website but that the Charity Commission's web team had not started to design the website or its interactive features due to other work priorities. In relation to the SORP, he noted that once the final editing had been done, the draft SORP would be submitted to an external agency for a final proof read and formatting. The document would then be submitted for consideration by the FRC's Committee for Public Benefit Entities (CAPE) in April, and all being well, the Accounting Council in May.

4.2 Subject to the time and expertise of the Charity Commission's web services team being available, it was hoped to have the SORP micro-site operational and the SORP posted on the web for 1st week of 1 July in time for the intended 4 month public consultation.

4.3 The outcome of the public consultation would be considered by the SORP Committee at the end of the year. The SORP would then have to be reconsidered by the FRC's CAPE and Accounting Council and have to obtain the approval of the FRC's Board before publication/web launch in 2014.

4.4 Depending upon the jurisdiction, the new SORP could not be used by charities until the relevant regulations had been made.

Item 5: Any other business

5.1 There being no other business the meeting closed