



GUIDING THE DEVELOPMENT OF THE CHARITIES SORP

Issued 4 February 2019

ICAEW welcomes the opportunity to comment on the invitation to comment on *Guiding the Development of the Charities SORP* published by Charities SORP Governance Review Panel on 26 November 2016, a copy of which is available from this [link](#).

The Charity SORP is produced under authority of the Financial Reporting Council (FRC) in connection with its responsibilities for financial reporting, in particular in relation to FRS102. Technical accounting knowledge and skills are therefore inevitably required for an informed use of the SORP and the SORP making process needs to reflect this.

If there is a desire to change the scope or purpose of the SORP, it must be clear which body is accountable for it and what are the objectives of that body. The FRC itself is to be reformed under the Kingman proposals and its ongoing responsibilities for SORPs (including the Charity SORP) will need to be considered in that context.

Charities may be required, or may wish, to produce information of various kinds for a variety of stakeholders. This does not necessarily mean that the information should be contained in the financial statements or covered by the SORP. For instance, information might be required as part of the regulators' requirements for annual reporting by charities.

This ICAEW response of 4 February 2019 reflects consultation with its Charity and Business Law Committees which includes representatives from public practice and the charity community. The Business Law Committee is responsible for ICAEW policy on business law issues and related submissions to legislators, regulators and other external bodies.

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KEY POINTS

1. We welcome the open nature of this consultation.
2. We believe that users need some technical accounting expertise to understand the SORP and its purpose fully. If the scope or purpose of the SORP is changed, it must be clear which body is accountable for it and what are the objectives of that body. The Kingman proposals in relation to the FRC need to be considered in that context.
3. If stakeholders would like charities to be required to publish other kinds of information, consideration is required as to whether this information should be included in the financial statements (and covered by the SORP) or elsewhere, for instance as part of the regulators' requirements for annual reporting by charities. It is important that the scope of purpose of SORP is clear in that context.

ANSWERS TO SPECIFIC QUESTIONS

Q.1 Please explain your role (or the charity or organisation on whose behalf you are responding) including your specific interest in or use of charity accounts. (However, please do not include any personal information in your formal response which you do not wish to be published.)

4. The nature of our organisation and our role is outlined in the cover sheet to this response. Our members and member firms provide accounting, audit, independent examination and related services to numerous charities of all varieties (eg, as regards size, geographical reach, sector and structure).

Q.2 Who do you see as being the main users of charity reports and accounts? To whom are charities being accountable when they prepare their reports and accounts?

5. Given the purpose of the financial statements and the legal and regulatory regime that shapes them (see Q3 below), the financial statements are likely to be most useful to those who have a significant interest in the financial position of the charity and at least a general understanding of accounting practice. This includes, major funders, government (including HMRC) and regulators. It would not typically include public donors or beneficiaries.
6. The press may also take an interest in the financial statements, but journalists may not always have the right skills to interpret the information or the desire to understand the nuances that may be involved.
7. The range of users of the reports (principally the trustees' report) may be broader than that of the accounts as the reports are in narrative form that may be more accessible, for instance to beneficiaries and the press.
8. The trustees are responsible for preparing the financial statements and can be personally liable under law and regulation (eg, to the charity) for their failures generally (and in particular circumstances, for instance if they have given warranties related to the accounts). The fact that financial statements may be of interest to a variety of audiences does not mean that the charity (or trustees) should be legally liable to those audiences. If 'accountable' means something other than 'liable', it would be helpful if the SORP making body could provide a definition.

Q.3 What do you see as being the main purpose of the Charities SORP? Do you feel it is effective at meeting that purpose? If not, what changes would you suggest to the processes of developing the SORP to improve its effectiveness for those who prepare and use charity accounts?

9. Our understanding of the purpose of the Charities SORP is set by the FRC's **policy on developing SORPs**, FRS102 and the SORP itself. We have provided extracts from those

publications in the Appendix for ease of reference. In short, the SORP appears to have a relatively narrow purpose closely linked to accounting under FRS102 (and must always be compatible with FRS102). It could be that the purpose could be better expressed in those documents, particularly if it needs to be understood by a wider audience than those familiar with accounting practice.

10. We have suggested in the past how the SORP might be developed to improve its effectiveness, particularly for smaller charities, for instance in our response to the 2016 consultation ([representation 189/16](#)).
11. It may be that others think that the SORP should have a broader purpose than that noted above. However, it is important for stakeholders to understand that the accounts and reports cannot practicably provide all the information that all possible users might want in the way that they might want it. There is also a cost in requiring charities to provide information in ways that they would not otherwise do. Clarity is therefore important as in some quarters there currently seems to be an 'expectation gap' (currently a topic of public debate in the context of audit).
12. It may be that some users prefer information to be contained in financial statements (rather than separate documents) because they are subject to audit or independent examination (where applicable) and this may make the information more reliable than might otherwise be the case. These users might want the scope of the SORP broadened so that more information is subject to audit. We suggest, however, that whether or not information should be subject to audit or another form of independent assurance or review should be considered as a distinct matter.

Q.4 Do you agree that having an advisory SORP Committee is the best way of ensuring stakeholder engagement with the development of the SORP? If not, what alternative arrangements would you recommend and why?

13. The SORP Committee derives its authority from the FRC. As the main purpose of the Charities SORP is related to accounting matters within FRC's competence, we query whether delegation to a separate body is the optimal model. It might be preferable for FRC to control the process more directly, obtaining charity and accounting sector input as it considers appropriate. This may result in a greater awareness of charity sector issues in the context of accounting and SORP development generally which could be helpful for the charity sector
14. If the delegation model is retained, we query whether the SORP making body should be made up solely, or even predominantly, of charity regulators. While the requirement for relevant charities to apply FRS102 (and so, the SORP) is a matter of charity law and regulation (in part at least), the purpose of the SORP is as noted above. Much has changed since the model was first put in place, for example, with the creation of the Scottish and Northern Irish regulators (OSCR and CCNI).
15. It is likely that our comments on the SORP Committee below could broadly speaking apply equally to a group formed by the FRC directly to develop the SORP or to a reformed SORP making body, but given the hypothetical nature of future structures, we comment on the SORP Committee in its current guise below.
16. As regards the SORP Committee:
 - we are not convinced that the distinction between members and observers is necessary or desirable (observers might alternatively have a role on the working groups suggested below).
 - while we understand the desire to cover the various jurisdictions, the emphasis on this may be disproportionate and there might be other ways of ensuring that any regulatory/legal differences between jurisdictions are appropriately addressed

- it is important that the number of committee members is at a level that supports the effective working of the committee (and it might be helpful to consider best practice on size of boards of directors in that context) and the number of representatives from the regulators is particularly relevant in that context
 - it is important that the SORP is not unduly burdensome for smaller or local charities so that it may be helpful if their interests are more distinctly represented on the Committee, for instance through relevant representative bodies or through individual members' own experience (eg, as trustees/treasurers or independent examiners of charities) rather than incidentally, for instance, through audit and accounting firms who have experience of a range of charities
 - it may be that funders are under-represented, given the relative importance of the SORP to those making economic decisions (see para 2.2 of FRS102).
17. We believe that the SORP making process should be informed by views and thoughts of users and potential users of the financial statements (which we take to mean 'stakeholders') but this does not mean that all stakeholder groups should be directly represented on the Committee. SORP is a technical document to be read in conjunction with FRS102, which is itself a technical document designed primarily for individuals with certain skills and experience rather than the general public. The SORP Committee should reflect this primary purpose.
18. Rather than looking at the matter from the perspective of different stakeholders therefore, it might be helpful to consider from the perspective of what issues or difficulties are arising from time to time. Examples might include: reporting; the needs of smaller charities; fundraising; and grant funding. Working groups might then be established to consider each of the issues drawing on experts in the relevant fields, with each group being led by individuals with the requisite technical knowledge (of FRS102/SORP). The head/chair of each working group would be a member of the SORP Committee and would report back to the Committee to consider how best to incorporate into the SORP (or to refer outcomes to others, such as the regulators, if more appropriate). These working groups would be information gathering, rather than 'advisory', groups. They could be formed as and when a perceived need arises and disbanded when an issue has been addressed.

Q.5 Do you consider that the composition of the current SORP Committee is appropriate both:

- a) **to provide the necessary expertise in charity accounting and**
- b) **to reflect the range of stakeholders who use charity accounts and reports?**

If not, what changes are necessary to the membership of the Committee and why? For example if you feel more representation is needed from beneficiaries or from donors, or from particular types or sizes of charities, please give details.

19. Please see our answer to Q4 above.

Q.6 Do you consider that the work of the SORP Committee is overly technical in its approach? If so, what changes should be made? (In your answer you may wish to reflect on how the work of the SORP Committee could be made less technical, whilst still ensuring the SORP reflects the requirements of general purpose accounting standards and the requirements of charity law.)

20. No, given the current purpose of the SORP. The style and drafting of the SORP and associated communications might be somewhat more 'user friendly' but cannot escape the fact that accounting standards and practice are technical and complicated. See also our answers to Q3-4 above.

Q.7 Do you have any comments on the balance of the membership of the SORP Committee?

21. Please see our answer to Q4 above.

Q.8 Do you have any suggestions as to how the SORP making body might improve the consultation process – either at the research stage or at the exposure draft stage?

22. If working groups along the lines outlined above were to be established, they could provide ongoing comment in relation to any matters within their competence, including in relation to consultations.
23. The SORP making body used to run roundtable discussion groups and we suggest that these could usefully be reintroduced, particularly to ensure engagement from the regions.
24. As regards exposure drafts, it might be helpful if a version of the current document (ie, SORP) could be produced marked with the proposed changes along with a table showing the changes and explaining the reasons and likely impact of each one.
25. Although outside the immediate control of the SORP making body, we wish to note that the volume of consultations from government and others over the past few years and the apparent lack of forward planning and cross-governmental co-ordination is of significant concern in the sector. It would therefore be helpful if the SORP making body could do what it can to gather intelligence on possible government initiatives so that the sector can consider any matters arising in a holistic and efficient way.
26. Given the importance of good accounting practice in the charity sector to society as a whole, government should ensure that it makes sufficient funds available to those charged with developing the Charity SORP to implement relevant recommendations arising out of this consultation.

Q.9 Can you suggest any particular organisations (in particular, those that may not have taken part in past SORP consultations) that you consider it would be useful for the SORP-making body to consult?

27. Please see our answer to Q4 above regarding engaging stakeholders.

Q.10 Do you think that the balance given to various groups during consultations concerning the development of the SORP should change? For example, do you consider that more or less weight should be given to any of the following groups:

- a) **beneficiaries**
 - b) **the donating public**
 - c) **representatives of smaller funders**
 - d) **representatives of larger funders**
 - e) **representatives of smaller charities**
 - f) **representatives of larger charities^{1 6}**
 - g) **the accountancy profession**
 - h) **commentators on the sector and journalists**
 - i) **any other categories you consider relevant?**
28. We are not clear what balance is currently accorded to the different groups noted above. The consultations are open to all and we believe that the SORP making body should make decisions on the basis of the strength of arguments made irrespective of where they come from (with a view to meeting the objectives of the SORP and the needs of its users outlined above). However, comment from those who understand the legal, regulatory and accounting framework and are aware of possible alternative views (ie, informed comment) is likely to be most useful. Working groups of the kind outlined above in answer to Q4 might be helpful in

this respect and could be made up of representatives from some or all of those groups noted in this question above, or others, depending upon the topic at hand.

Q.11 If you felt in Q10 that more weight should be given to one or more groups listed, what are your suggestions as to how these views can be obtained?

29. Please see our answer to Q4 regarding the Committee and possible working groups.

Q.12 Do you have any other suggestions for improvements that can be made to the consultation process in the development of the Charities SORP?

30. We welcome the open nature of this consultation and urge caution in the use of more closed consultations (eg, those designed for on-line responses with 'agree', 'disagree' type options for responses). While we can see potential advantages from the perspective of the consulting bodies in using more closed questions, we are not convinced that it necessarily produces the best possible results or encourages as wide-ranging debates as possible. We would be happy to expand on this if it is of interest.

Q.13 Do you think that the SORP development process should cover all forms of financial reporting by charities – both those required by charity law (or company law) and other financial communications issued by charities – for example in a non-statutory annual review, summary financial reports, or visual summaries of a charity's finances?

31. This question is so broad and involved that we are only making a few initial comments here. If the SORP making body would like to discuss further, particularly with regard to concrete examples of the types of communications of concern, we would be happy to do so.
32. As noted in the consultation document, if the SORP were to have wider scope, the SORP making body would need to have a new identity. Our comments in answer to Q4 are relevant in this context, not least as regards whether FRC (or any successor body) should have direct responsibility rather than delegating to the SORP-making body.
33. Leaving questions of form/legality aside, we naturally support the proposition that financial reporting by charities should be accurate, reliable and useful. However, charities also need to be free to run their own activities and to innovate and serve diverse needs. It is not practicable or desirable for regulation (or 'guidance') to prescribe everything they do or say. Financial information may be used in an immense variety of contexts and regulation that is too broad in scope could have a paralysing effect, whilst regulation aimed at specific types of publications could be circumvented or have other unintended consequences.
34. Our comments on audit (or other forms of assurance or review) in answer to Q3 are also relevant here. There may be good reasons why users of various kinds might like charities to be required to have additional documents/communications subject to independent verification/review, but it is highly debatable whether that means the requirement should derive from the SORP (or audit/independent examination requirements applicable to the financial statements).
35. We believe that current requirements in SORP result in the financial statements of some charities being longer or more cluttered than might otherwise be the case (and so less useful to some users) and charities adopting a box ticking approach in some cases. This concern might equally apply were the requirements or guidance of the SORP making body to apply to diverse sources of information (for instance, were full impact reporting to be separately required).

Q.14 If you agreed that the SORP Committee should issue guidance on non-statutory financial reporting by charities, what form do you feel such guidance should take, bearing in mind that (without a change in the law) it would not be mandatory?

36. We did not agree but suggest that any change in remit of the SORP Committee would need to be set by the FRC, perhaps more explicitly than is currently the case. There is a risk of confusion if the remit or legal basis of a body of this kind is unclear. Rather than considering this in the abstract, we suggest that specific issues be identified on which views are sought. It would then be possible to consider which bodies or groups might best consider the issues and, potentially, issue guidance (or suggestions for best practice). For instance, the FRC or the regulators themselves (rather than indirectly as members of the SORP making body), might wish to do so.

Q.15 If you considered that the SORP process should cover all forms of financial reporting by charities, what changes to the SORP Committee and SORP consultation process would you recommend and why?

37. Please see our answers to the relevant earlier questions. In general, we believe that the question needs to be addressed in relation to the FRC or SORP making body rather than the Committee.

Q.16 Do you have any other comments on how the SORP is developed, the SORP-making body, the advisory SORP Committee or the SORP consultation process?

38. Those involved in the SORP making process need to be sufficiently resourced for the purpose. For instance, if roundtable discussions are to be encouraged, they will require some funding, even if most of those engaging will be doing so on a voluntary basis. However, it is equally important that any new regulatory initiatives are developed in a cost-effective way and proper impact assessments conducted. See also our response to Q8 regarding funding.

APPENDIX

(Extracts concerning the purpose of the SORP)

EXTRACTS FROM FRC POLICY ON DEVELOPING SORPS

SORPs are sector-driven recommendations on financial reporting, auditing practices or actuarial practices for specialised industries, sectors or areas of work, or which supplement FRC standards and other legal and regulatory requirements in the light of special factors prevailing or transactions undertaken in that particular industry, sector or area of work that are not addressed in FRC standards. SORPs also address matters that are addressed in FRC standards, but about which additional guidance is considered necessary. When there are policy options in FRC standards, a SORP may recommend the most appropriate option to the particular industry or sector.

The FRC may recognise bodies for the purpose of developing and issuing SORPs. Bodies will only be recognised where the following criteria are met:

- a) the industry or sector represented by the body in question has special financial reporting, auditing or actuarial issues and the application or interpretation of FRC standards requires clarification in order to deal with those issues;
- b) the body in question represents the whole or a major part of the industry or sector;
- c) the body shares the FRC's aim of:
- d) high-quality financial reporting proportionate to the size and complexity of the entity and users' information needs; or.....

EXTRACTS FROM FRS102

Definition of SORP

An extant Statement of Recommended Practice developed in accordance with SORPs: *Policy and Code of Practice*. SORPs recommend accounting practices for specialised industries or sectors. They supplement accounting standards and other legal and regulatory requirements in the light of the special factors prevailing or transactions undertaken in a particular industry or sector.

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2.2 The objective of financial statements is to provide information about the financial position, performance and cash flows of an entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs.

2.3 Financial statements also show the results of the stewardship of management—the accountability of management for the resources entrusted to it.

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10.3 If an FRS specifically addresses a transaction, other event or condition, an entity shall apply that FRS. However, the entity need not follow a requirement in an FRS if the effect of doing so would not be material.

10.4 If an FRS does not specifically address a transaction, other event or condition, an entity's management shall use its judgement in developing and applying an accounting policy that results in information that is:

- a) relevant to the economic decision-making needs of users; and
- b) reliable, in that the financial statements:
 - i. represent faithfully the financial position, financial performance and cash flows of the entity;
 - ii. reflect the economic substance of transactions, other events and conditions, and not merely the legal form;
 - iii. are neutral, ie, free from bias;
 - iv. are prudent; and
 - v. are complete in all material respects.

10.5 In making the judgement described in paragraph 10.4, management shall refer to and consider the applicability of the following sources in descending order:

- a) the requirements and guidance in an FRS dealing with similar and related issues;
- b) where an entity's financial statements are within the scope of a Statement of Recommended Practice (SORP) the requirements and guidance in that SORP dealing with similar and related issues; and
- c) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses and the pervasive principles in Section 2 Concepts and Pervasive Principles.

10.6 In making the judgement described in paragraph 10.4, management may also consider the requirements and guidance in EU-adopted IFRS dealing with similar and related issues. Paragraphs 1.4 to 1.7 require certain entities to apply IAS 33 Earnings per Share (as adopted in the EU) , IFRS 8 Operating Segments (as adopted in the EU) or IFRS 6 Exploration for and Evaluation of Mineral Resources (as adopted in the EU).

EXTRACTS FROM CHARTIES SORP FRS102

This SORP includes charity-specific requirements that are additional to those of FRS 102. In particular, requirements relating to the trustees' annual report, fund accounting, the format of the statement of financial activities and additional disclosures aimed at providing a high level of accountability and transparency to donors, funders, financial supporters and other stakeholders. The phrase 'this SORP requires' is used to distinguish the additional disclosures required by the SORP which are not specifically required by FRS 102.

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- 8. The SORP is developed primarily to assist those involved in the preparation of the accounts and trustees' annual report of a charity. The SORP is also relevant to charity auditors, independent examiners and accountancy practitioners who are involved in the scrutiny of charity accounts or in advising on the application of accounting standards in the context of charities.
 - 9. It is anticipated that users of this SORP will be familiar with accounting concepts, principles and terminology and possess a reasonable knowledge of accounting practice.

OBJECTIVES OF THE SORP

- 10. The recommendations of the SORP are intended to achieve the following objectives:

- improve the quality of financial reporting by charities;
- enhance the relevance, comparability and understandability of the information presented in charity accounts;
- provide clarification, explanation and interpretation of accounting standards and their application to charities and to sector specific transactions; and
- assist those who are responsible for the preparation of the trustees' annual report and accounts.

Accounting and reporting by charities

THE INTENDED USER OF THE TRUSTEES' ANNUAL REPORT AND ACCOUNTS

11. The objective of the trustees' annual report (the report) and accounts is to provide information about a charity's financial performance and financial position that will be useful to a wide range of stakeholders in assessing the trustees' stewardship and management of charitable funds, and to assist the user of the accounts to make economic decisions in relation to the charity.
12. Although past, current and potential funders, donors and financial supporters of a charity are the primary audience for the financial information contained in a charity's report and accounts, the preparer should also be aware that interest in this information may also extend to a charity's service users and other beneficiaries.
13. The report and accounts should not be viewed simply as a statutory requirement or a technical exercise. The report and accounts, when read together, should help users of the information to understand what the charity is set up to do, the resources available to it, how these resources have been used and what has been achieved as a result of its activities.

SCOPE OF THE SORP

14. Except where an alternative reporting framework sets out in legislation or regulation, or in another SORP applies, the accounting recommendations of this SORP apply to all charities in the UK that prepare accounts on the accruals basis to give a true and fair view of a charity's financial position and financial activities regardless of their size, constitution or complexity. In the Republic of Ireland this SORP sets out recommended best practice....