

The SORP Governance Review – Changes ahead for accounting by smaller charities

STRIVE Third Sector Conference

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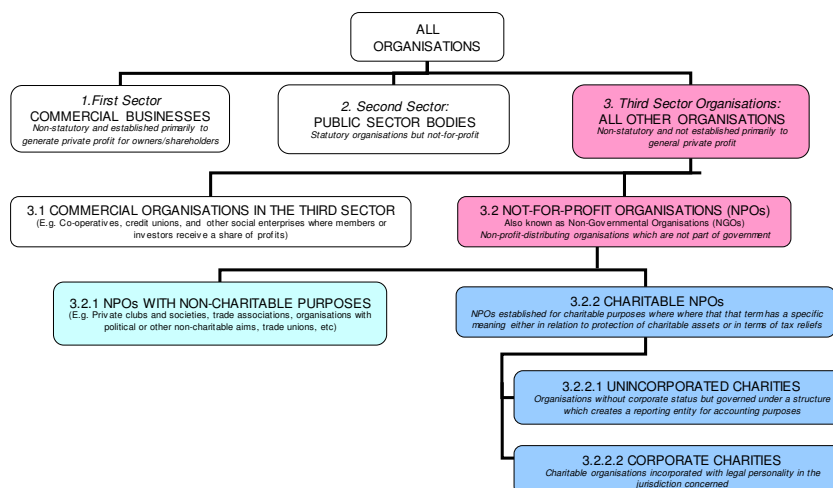
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The Kubernesis Partnership



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Charitable Status



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Charity Law: spanning the jurisdictions

- **In the UK, charity law is devolved:**
 - Always differences: England & Wales, Scotland, Northern Ireland
 - Charity regulation a devolved matter for Scottish Parliament / N Ireland Assembly
 - But tax law is *not* devolved: whole of UK, uses English definition of “charity” *except* in specific areas such as property taxes/business rates
- **So across Britain and Ireland there are *four separate systems of charity law and regulation* – *four jurisdictions*:**
 - **England and Wales:** *Charity Commission for England & Wales (CCEW)*
 - **Scotland:** *Office of the Scottish Charity Regulator (OSCR)*
 - **Northern Ireland:** *Charity Commission for Northern Ireland (CCNI)*
- **Primary legislation:**
 - **Charities and Trustee Investment (Scotland) Act 2005**
 - **Charities Act 2011** as amended by Charities (Protection & Social Investment) Act 2016
 - **Charities Act (Northern Ireland) 2008** as amended by Charities Act (NI) 2013

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CHARITY ACCOUNTING IN SCOTLAND:

The Principles

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Charity Regulation in Scotland – the key landmarks

- **1999 Scottish Parliament Established**
 - Scottish charity law now devolved to Scottish Parliament
- **2001 McFadden Commission on charity regulation in Scotland**
- **2004 OSCR Established**
 - Office of the Scottish Charity Regulator
- **Charities and Trustee Investment (Scotland) Act 2005**
 - Scottish Charity Register
 - OSCR given statutory powers
 - Mandatory charity accounting requirements
 - All charities must file annual return with OSCR
 - All charities must file a Trustees' Annual Report and Accounts with OSCR
 - Mandatory audit or independent examination of charity accounts
- **2006: Modern charity accounting regulations implemented in Scotland**
 - **Charities Accounts (Scotland) Regulations 2006**
 - Various thresholds determined by *total income* of the charity
 - Amended in 2007, 2010, 2014, 2016, 2017

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Charitable Status and Structures

- **The definition of a Scottish charity is an organisation:**
 - Established in Scotland
 - Meeting the charity test in the 2005 Act:
 - Exclusively charitable purposes: under one or more of 16 headings in the Act *AND*
 - Provides public benefit
 - Entered on the Scottish charity register (maintained by OSCR)
 - *Also some cross-border charities on the Scottish Charity Register: often operating UK-wide.*
- **But Scottish charities can have many different structures – mainly:**
 - Charitable trusts
 - Charitable associations
 - Charitable companies
 - SCIOs – Scottish Charitable Incorporated Organisations
- **Choice of structures**
 - Wide range of structures for existing charities
 - Two thirds of new charities are formed as SCIOs
 - *Existing charities can be restructured as SCIOs*
- **But also many non-charitable organisations in third sector – e.g:**
 - Associations with non-charitable aims
 - CICs (Community Interest Companies) are not charities
 - Charity accounting rules not applicable

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Scottish charity accounting rules:

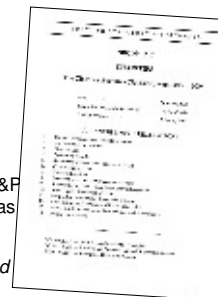
1: The Presentation of the Accounts

- **ALL Charities must produce Annual Report and Accounts**

- No lower limit
- Public document – anyone can request a copy
- Must be filed with OSCR by 9 months after year end

- **£0 to £250,000 income – choice of two formats:**

- (a) Receipts and Payments (R&P) Accounts
 - Cash basis
 - Receipts and payments account and Statement of Balances
 - Notes to the accounts
 - In Scotland (unlike E&W) the regulations prescribe the content of R&P
 - R&P allowed for SCIOs but *not* available if the charity is structured as
- (b) Accrual Accounts following the Charities SORP
 - *Accounting and Reporting by Charities: Statement of Recommended*
 - The regulations refer to the SORP
 - Statements of Financial Activities (SOFA) and Balance Sheet
 - Notes to the accounts – extensive disclosures required



- **Over £250,000 income – must use accruals/SORP accounts**

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Scottish charity accounting rules:

2: The Scrutiny of the Accounts

- **£0 to £500,000 income – choice of two forms of scrutiny of accounts:**

- (a) Independent examination
- (b) Full professional audit

- **Independent examination**

- An independent examiner is someone *reasonably believed by the charity trustees to have the requisite ability and practical experience to carry out a competent examination of the accounts*
- For R&P accounts, IE can be a lay person with some financial experience – *but must still understand the duties of IE*
- For accruals accounts, IE must be a member of one of the professional bodies specified in the regulations – e.g:
 - ICAS members (Institute of Chartered Accountants of Scotland)
 - Full members of ACIE (Association of Charity Independent Examiners)

- **Over £500,000 income – accounts must be audited**

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Scottish charity accounting rules:

2: The Scrutiny – The Independent Examiner's Report:

- **The IE's Opinions – Four points *always* addressed in the examiner's report** (expressed as negative opinions if OK)
 - 1. Adequacy of accounting records
 - 2. Accounts in agreement with accounting records
 - 3. Compliance of accounts with regulations*
 - 4. Other matters which need to be drawn to the reader's attention to enable a proper understanding of the accounts
- **The IE's Opinions – Three points to be addressed in case of concern** (expressed as positive opinions if applicable)
 - 5. Expenditure or action outside the trusts/purposes of the charity
 - 6. Inconsistency between the accounts and the trustees annual report*
 - 7. Lack of information or explanations from trustees or officers
- **In serious cases may also need to consider IE's whistleblowing obligations –**
 - IE must advise OSCR directly in the event of matters for regulatory attention

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Scottish charity accounting rules:

The Final Accounts

A full set of Scottish charity accounts must always include 3 elements (usually combined into one document):

- **The Trustees' Annual Report**
 - Factual information as specified in the regulations
 - Explanation of how the charity has advanced its objects during the year
 - Signed and dated by the trustees
- **The Annual Accounts**
 - Receipts and payments account with a Statement of Balances and Notes (R&P basis)
 - *OR*
 - Statement of Financial Activities, Balance Sheet, Extensive Notes – all following the *Charities SORP* (Fully accrued basis)
- **The Scrutiny Report**
 - Independent examiner's report – or Audit report if required

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Charity Accounting: Differences between UK jurisdictions
Income levels at which requirements become compulsory*

Requirement	England & Wales	SCOTLAND	Northern Ireland
Must keep proper accounting records	£0	£0	£0
Must publish annual statement of accounts (can be on a receipts and payments basis).	£0	£0	£0
Must register with relevant regulator if not a CIO/SCIO (local charities in jurisdiction concerned)	£5,000	£0	£0
Annual report and accounts must be filed with regulator	£25,000 (£0 for CIOs)	£0	£0
Accounts must be independently examined (lay examiner)	£25,000	£0	£0
Accounts must be prepared on an accruals basis (as opposed to receipts and payments) complying in most respects with the SORP indicated.	£250,000 SORP 2005 (<i>unless</i> applying "True & Fair override")	£250,000 SORP 2015 (FRS102)	£250,000 SORP 2015 (FRS102)
Independent examiner must be professionally qualified	£250,000	All accruals accounts	£250,000
Full audit required (by a firm of registered auditors). Accounts must comply fully with Charities SORP (with any departures disclosed).	£1M	£500,000	£500,000

***Excluding charitable companies and non-company charities with £3.26m+ assets**
 Requirements shown are for financial years starting in 2016 or later.

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CHARITY ACCOUNTING IN SCOTLAND:

The SORP and its development

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The Status of the SORP

- **SORP = Accounting and Reporting by Charities: Statement of Recommended Practice**
 - But it is more than “recommended”
 - The Charities Accounts (Scotland) Regulations 2006 (as amended) require charities to follow the principles in the SORP in the case of:
 - ALL charities of £250,000 income and above
 - Charitable companies (of any size)
 - Other cases where the charity's constitution or trustees decide to use SORP accounts
- **The SORP takes general purpose accounting standards – currently FRS102 – and set out the specifics for charities**
- **BUT – You don't need to worry about SORP if:**
 - Your charity has total income < £250,000 *and*
 - Your charity is not a company *and*
 - Your trustees are happy to use R&P accounts
- **Various versions of the SORP over the years**
 - Does the SORP meet the needs of those who use it?
 - Hence: *SORP Governance Review 2018/19*

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SORP 1995: Some key features

- **Central principles:**
 - Fund accounting
 - Multi-column Statement of Financial Activities (SOFA)
 - Functional analysis of income & expenditure
 - No netting off expenditure against income
 - Balance sheet – all assets/liabilities belong to funds of the charity
 - Extensive disclosures by way of notes
 - Inter-fund transfers
 - Transactions with connected parties
 - Details of grants made
 - 95 pages incl index and examples
- **Impact**
 - This was very scary for many charities
 - Some treasurers etc resigned
 - Many charities appointed or upgraded finance staff



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The first update: SORP 2000



- **Why change so soon?**
 - Commitment given to review the regime after 5 years
 - SORP needed updating for new accounting standards
- **What was different?**
 - Much stronger focus on link between accounts and TAR
 - Different functional breakdown on SOFA
 - Focus on reserves policy – also investment policy, grant-making policy
 - Risk-management section required
 - New sections giving more detail
 - 103 pages incl index (examples published separately)

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In the meantime: SORP 2005

- **SORP 2005: What had changed?**
 - New accounting standards esp FRS17 (Retirement benefits)
 - Different again functional breakdown on SOFA
 - Recognition of role of OSCR and new legislation expected in Scotland
 - More focus on smaller charities: specific exceptions for small charities, cross-references to FRSSE
 - 121 pages
 - Updated in law: Charities (Accounts and Reports) Regulations 2005
- **SORP 2005 re-issued 2008**
 - Not a new SORP, but a new intro with more emphasis on smaller charities
 - Now issued jointly by CCEW/OSCR
 - *In 2019 - this remains the current SORP according to regulations in England & Wales!*



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Two for the price of one: the 2015 SORPs

- **Financial Reporting Council set 1 Jan 2015 set as convergence date for UK accounting to come into line with IFRS**
 - All existing general standards replaced with FRS102 – *The Accounting Standard in the UK and Ireland*
 - Smaller entities (as in company law – up to £10.2M) initially allowed to follow FRSSE revised 2015 (still based on older UK standards)
- **SORP re-written: new modular format**
 - 12 modules applicable to all, others as required.
 - Two versions:
 - **Charities SORP (FRS102) and Charities SORP (FRSSE)**
 - 193 pages (FRS102 - all modules) / 181 pages (FRSSE)
- **2016: FRSSE and hence FRSSE SORP withdrawn**
- **All Scottish charities not doing R&P accounts must now follow SORP FRS102**



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But how do the SORPs differ?

- **Analysis of expenditure (formerly resources expended):**

SORP 1995	
Direct charitable expenditure	
Other expenditure:	
▶ Fundraising and publicity costs	
▶ Management and administration	

SORP 2000	
Cost of generating funds	
Charitable expenditure:	
▶ Grants payable	
▶ Activities for charitable objects	
▶ Support costs	
▶ Management and administration	

SORP 2005	
Cost of generating funds	
▶ Costs of generating voluntary income	
▶ Fundraising trading costs	
▶ Investment management costs	
Charitable activities	
Governance costs	

SORPs 2015 (FRS102 + FRSSE)	
Expenditure on raising funds	
Expenditure on charitable activities	

Of course, there are more fundamental issues that changed between SORPS –

But constantly changing the SOFA headings may just lead to confusion!

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CHARITY ACCOUNTING IN SCOTLAND:

The SORP Governance Review

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CHARITIES SORP GOVERNANCE REVIEW 2018/19

Aim: To examine the *governance* of the process by which new versions of the Charities SORP are developed

In particular the membership and processes of the SORP Committee

Sponsored by the SORP-making body – the four charity regulators of UK and Ireland



CHARITY COMMISSION
FOR ENGLAND AND WALES

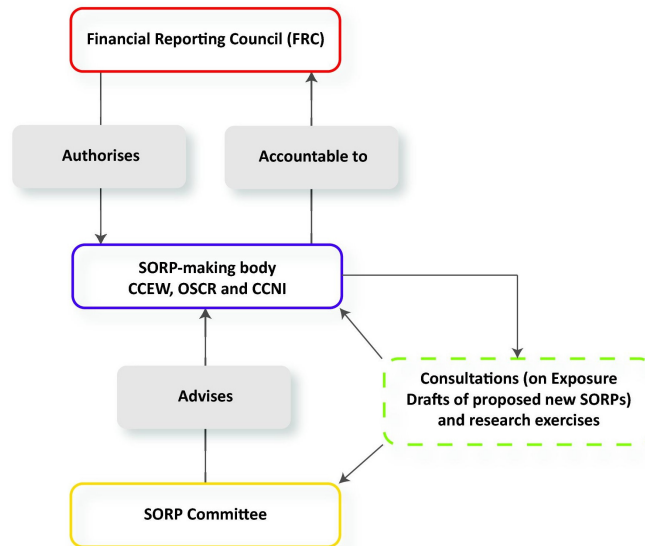
The **Charity
Commission**
for Northern Ireland

OSCR
Scottish Charity Regulator

 An Rialálaí
Carthanais
Charities
Regulator

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Role of the SORP-making body and SORP Committee



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Context of the Review

- **Charities SORP has existed as a standard under charity law since 1995**
 - Successive versions 1995, 2000, 2005, 2015
 - SORP-making body now comprises CCEW, OSCR, CCNI with Irish Charities Regulator likely to be added in near future
 - After 20+ years it seemed appropriate to re-examine the processes for development of the SORP
- **Oversight panel established, comprising:**
 - GM as Independent Chair (engaged by the charity regulators)
 - Sarah Atkinson – Charity Commission for England & Wales
 - Judith Hayhow – Office of the Scottish Charity Regulator
 - Punam McGookin – Charity Commission for Northern Ireland
 - Tom Malone/Jelena Griscenko – Charities Regulator (Ireland)
 - FRC Observer – Jenny Carter (and initially Mei Ashelford)
 - Current co-chairs of the SORP Committee (Nigel Davies/Laura Anderson) as Secretariat to the Panel
- **Consultation: Nov 2018 – February 2019** – 16 questions
- **Final Report of Panel – June 2019**

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SORP Governance Review: Final Report

- **48 PAGE REPORT**
 - Chair's Introduction, four sections, plus five appendices
 - Analysis of evidence received
 - Recommendations
 - Grouped under five headings corresponding to themes of the consultation
- **36 RECOMMENDATIONS MADE**
 - Mainly **recommendations to the SORP-making body** (with the support of FRC where appropriate)
 - Some **recommendations to others** including:
 - The **charity sector**
 - The **accountancy profession**
 - The **charity regulators** (separately from their role as the SORP-making body)



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SORP Governance Review: Examples of Key Recommendations

- **The rationale for charity accounts and the role of the Charities SORP**
 - 1. A new approach is needed by the SORP to better meet the needs of smaller charities reporting under the SORP.
- **The need for and composition of the SORP Committee**
 - 6. The composition of the SORP Committee should change with:
 - membership reduced to a maximum of 16
 - at least two members to be drawn from each of the four jurisdictions, with at least one of the two representing smaller charities
- **The consultation processes followed by the SORP-making body to engage with stakeholders**
 - 17. Illustrative examples should be provided to help explain proposed changes and the potential impact.
- **Other issues raised by the consultation**
 - 30. The Panel urges the SORP-making body, supported by the FRC, and the SORP Committee to take steps to **ensure the SORP is made more accessible to the majority of users who are applying it in the context of smaller charities**
 - 33. The Panel recommends the charity regulators consider their approach to education on the SORP with a view to improving compliance.

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Charity Accounting: Going forward

- **The charity accounting and reporting regime as applicable in the UK is probably the most thorough system of non-profit financial reporting anywhere in the world**
 - SORP is part of this – but also the auditing and independent examination regime
 - Other countries and jurisdictions are drawing on the UK framework
- **But are we too obsessed with SORP accounting?**
 - Receipts and payments regime allowed for charities up to £250K income (excludes charitable companies but includes SCIOs)
 - Is R&P sufficient for smaller charities? – R&P still subject to IE
- **Compliance remains a huge issue**
 - How many charities really follow the SORP effectively and produce meaningful financial statements
 - Too much use of templates? Some taking minimalistic approaches
- **Are accountants acting as auditors/IEs overriding what trustees want to say?**
- **Do we need some simplified alternative for smaller charities?**
- **The whole reason for charity accounting is *to give an account* –**
 - Is the accounting regime helping charities to be more accountable?

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