

DSC consultation response

# Guiding the Development of the Charities SORP

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## 1. Summary

We have responded to the specific consultation questions in Section 3 below. We would like to make the following summary points:

1. **A vision and mission for the SORP Committee** – The Committee should consider what it is trying to achieve above and beyond technical accounting considerations and develop a vision and mission. If one already exists, the Committee should review it. This should consider the Committee’s wider remit and purpose – for example, whether its function goes beyond producing a SORP that correctly integrates accounting rules for the charity sector, to improving charity accounting generally and informing the wider public.
2. **Composition of the Committee** - The Committee needs to incorporate diverse stakeholders beyond the accounting profession. Considering the Committee’s purpose more widely in terms of ‘vision and mission’ could help refine what kind of stakeholders are needed and how they should best participate.
3. **Consideration for small charities** – Thousands of charities are above the £250k income threshold for the SORP but could still be considered ‘small’ – in that they likely have few staff or specialist in-house finance expertise, and much work will be done by trustees. Thousands more will be small CIOs or dual-registered charity/companies, including many below the £250k threshold. Further, grant-makers with relatively large balance sheets may still have low staff capacity and in practice operate as very small charities (for example, many Community Foundations or other local grant-makers would fit this description). The Committee needs to take the needs and viewpoints of these organisations into consideration not only in its decision-making but in its composition.
4. **Development of the SORP must be seen in the context of open charity data** – The SORP is an integral part of the mix of current issues and debates about charity transparency and the provision of data to the public, which are related to questions of public interest and charity effectiveness. The Committee’s work inevitably has an impact on what information and data charities provide to the regulators and how it is provided to the public. The Committee needs to consider how it interacts with and facilitates discussions and decision-making by the charity regulators and other stakeholders about open data – not just between the Committee members.

## 2. Background

### What's a SORP?

Statements of Recommended Practice, generally referred to as SORPs, provide recommendations for comprehensive accounting and reporting. In the charity world it is recommended that we follow the Charities SORP, (currently Charities SORP 2015).

The Charities SORP provides a mechanism which enables charities to meet the legal requirement for their accounts to give a true and fair view, and also provides consistency in the sector's interpretation of accounting standards - detailing recommendations for annual reporting that are relevant to the charity sector and stakeholders' needs.

The SORP-making body for charities consists of the three charity regulators in the UK - the Charity Commission for England and Wales (CCEW), the Office of the Scottish Charity Regulator (OSCR), the Charity Commission for Northern Ireland (CCNI) - together with the Irish Charities Regulator as an observer.

The Charities SORP 2015 was developed by the Charity Commission in conjunction with the Charities SORP Committee, an advisory committee made up of charity finance directors, charity auditors, academics, charity advisers and charity regulators.

### What is this consultation about?

The charity regulators in the UK, as the SORP-making body for charities, are seeking views on what changes may be needed to the process used to develop the SORP. The SORP-making body aims to make changes so that the Charities SORP continues to serve the needs of those interested in the work of the charity sector and the sector itself as well as it can.

For further links to the consultation documents and further information about the SORP see [www.charitycorp.org](http://www.charitycorp.org)

### 3. DSC's response to the consultation 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.**

The Directory of Social Change (DSC) has a vision of an independent voluntary sector at the heart of social change. We believe that the activities of charities and other voluntary organisations are crucial to the health of our society.

Through our research, publications, courses and conferences, we come in contact with thousands of organisations each year. The majority are small to medium-sized, rely on volunteers and are constantly struggling to maintain and improve the services they provide.

DSC has responded to the consultation as it affects the voluntary sector and its beneficiaries – including the tens of thousands of charities we work with. The requirements of the SORP can affect these organisations on a daily basis and for many reasons; for example, in keeping good records of monitoring and evaluation for projects to report annually on public benefit, or say, in the case of grant-makers, to be transparent in who their beneficiary organisations are, in order to make applying for funds an easier task for applicants. Charity accounts are widely used by DSC researchers when preparing our research.

DSC is also a charity and therefore uses the SORP to prepare its own accounts which feed into the preparation of our annual return.

We therefore have an interest in how the SORP develops over time and that it is useful to the people that apply it.

#### **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?**

There is a range of users of charity reports and accounts, but hard evidence about the prevalence or method of their use is thin. Funders often use the information (or existence thereof) for making funding decisions, even if this is in a procedural way rather than involving deep scrutiny. For example, grant-makers often require a copy of the charity's latest accounts as part of the application process. A local authority may review the accounts when awarding a contract as a part of its due diligence or contracting procedure.

Charity trustees use them (one would hope) to make strategic decisions about the development of their own charities, or for example when considering merging or forming a partnership with another charity. Charity accounts are obviously widely used by regulators (the Charity Commission) and by organisations or individuals that have a commercial relationship with a charity such as contractors, creditors and lenders and other advisors. Researchers and journalists can also have a specialised interest in charity accounts. Information from charity accounts is also included in more charity reports which address

existing and new donors, as well as the wider public – but here the level of awareness and actual use (or ability to use and understand) is probably low.

These observations are based on experience, not wider research on who the main users are and how different user groups apply the SORP in practice. The Committee should consider conducting such research or at least doing a review of the evidence to see whether any exists. This could help inform future decisions about the expansion and composition of the Committee.

**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?**

The main purpose of the Charities SORP is to guide trustees to prepare the accounts of the charities they govern. This enables them to meet the legal and reporting requirements, for example when submitting their Annual Return to the Charity Commission. Assessing its effectiveness is a difficult question to answer, because it depends on who is being asked and their level of familiarity with accounting rules and good practice.

The SORP is a very large and detailed document. Updates and other accompanying documents which must be cross-referenced make it more difficult to navigate the document. In past consultations DSC has examined and commented on the online version which offers advantages in this respect, and that is something the Committee should consider in the future.

The capacity of charities that must apply the SORP also varies widely. Those charities that are slightly above the £250k threshold might have very limited capacity, relying on a volunteer board and minimal staff. Complying with a complex SORP document might be out of their reach and might have to be outsourced to an external person. A higher income also does not necessarily translate into higher capacity. Many grant-making charities might have a large income but are still run by a very small amount of staff who might struggle to engage with a complex SORP and apply its rules properly.

The SORP in its current form might therefore not be accessible to a lot of charities which do not have complex financial affairs but still fall under the SORP. Boards of larger charities would be more likely to have a dedicated person/treasurer/company secretary who will understand and apply the SORP and prepare the accounts or work with finance professionals to do so. But many trustees do not engage with the SORP in detail. Smaller charities without the capacity or the skillset available on their board might rely mostly on external people to prepare their accounts.

There is also no research available online that shows what kind of charities (differentiated by size and income) have a dedicated treasurer on their boards which has the capability to

fully apply the SORP. The Committee might consider conducting such research to find out more about the capacity in the sector to deal with the SORP.

**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?**

The Committee should consider what it is trying to achieve above and beyond technical accounting considerations and develop a vision and mission. If one already exists, the Committee should review it. This should consider the Committee's wider remit and purpose – for example, whether its function goes beyond producing a SORP that correctly integrates accounting rules for the charity sector, to improving charity accounting generally and informing the wider public.

The precise working and structure of the future advisory Committee or other arrangements should flow from this work. It's possible that the current arrangements might remain sufficient or would need to change significantly as a result – but it's a question of the mechanism being suited to the purpose, not the other way around.

**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.**

It is necessary that there is significant representation from the accounting profession on the Committee, which is related to its purpose. However, there could be more effective or inclusive representation of people that do not possess technical expertise, but who are users of derivative information that comes from charity accounts (such as donors) or who engage with charity accounts in other ways (such as journalists).

There are specific stakeholder groups which could be more represented. Funders and trustees are probably the biggest users of charity accounts and their involvement could be enhanced. Organisations which are specifically representing trustees or which deal with specific issues such as board diversity, do not seem to be included at the moment. Smaller funders which might not be represented by the larger umbrella bodies are also not included.

Smaller charities - and specialised preparers of accounts for those charities - should also have a bigger representation since they make up a significant constituency of charities that fall under the SORP, but whose interests may be overlooked. Furthermore, beneficiaries, donors, fundraisers as well as commentators and media representatives that deal with charity accounts in their reporting could be more represented.

The process of membership selection and why certain members have observer status could be also more transparent. Currently it is difficult for external people to obtain information on this. Explanations might be included in the governing document or terms of reference for the Committee's working, but these are not readily accessible. We would like to echo a point mentioned by Association of Charitable Foundations (ACF) in their consultation submission. Currently some Committee members have only an observer status. If there is no convincing rationale for assigning some members observer status, then this should be reconsidered. What is the purpose of observer status and why is it different? Does it work?

The expansion and diversification of the Committee membership could be led by three questions:

- Who uses charity accounts (and derivative information) mostly in practice?
- Who should use it, but is not sufficiently enabled to do so?
- Where and how could misuse or misinterpretation of information occur, and who therefore requires more knowledge about the subject?

We would also like to acknowledge that there might be limits to an expansion of the Committee in terms of its membership, either because of resources or because the internal governance of the Committee could become too complicated. The Committee needs a clearer rationale for why certain members are included and which stakeholders are given priority or should be included because they are currently not represented. This would be up for the Committee to decide, but we would argue it should include:

- Representation of lay/informed public
- Representation of trustees
- Representation of small charities.

**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.)**

The work of the advisory SORP Committee must be significantly technical by nature. A focus has to be on the discussion on technical rules included in the SORP. However, there can be wider considerations taken into account. For example, to what extent are the discussions user-centred and user-led? Are the views of all types of users of the SORP but also the users of charity account information reflected? Does the Committee have these different users as well as different types of charities in mind when preparing advise to the SORP-making body?

Smaller charities can already prepare Receipts and Payments accounts but there are also many charities that fall under the SORP but have less complex financial affairs. These

charities could benefit from a more simplified version of the SORP (a point which was raised by Association of Accounting Technicians (AAT) in their consultation response).

The SORP underpins the preparation of information that people use to make judgements. These can be strategic judgements by trustees, or judgements by donors about a charity's activities and its financial sustainability. Is part of the mission of the Committee to ultimately help trustees to make better strategic decisions and to help the public to have a better understanding of what charities do and how they spend their money?

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

Yes, please see answer to Q.5

**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?**

DSC's perception of previous consultation processes is that they are well organised, clear, that responses are taken on board and are thought through. The whole consultation process is no empty gesture.

Consultations on the SORP Exposure Drafts might be too overwhelming to engage with for some charities and other stakeholders with less capacity. Consultations could be staggered and thematically split up which would allow people to engage on a smaller set of questions/a sub-set of proposed changes instead having to navigate all questions on all suggested changes in one go (a point which has been raised by the Association of Charitable Foundations (ACF) in their consultation response).

The invitation to comment mentions that the engagement from certain groups, such as beneficiaries, donors, wider commentators on the sector, and smaller funders and some government funders remains low. There is a recognition that these under-represented groups could be more included by changing the consultation process.

Improvements could be made around notifying charities and press directly that the consultation is taking place. Direct visits to underrepresented groups and organisations could also increase uptake. This can be an opportunity to explain the content of the consultation and the added value of different groups taken part in it.

Feedback on consultation questions can be also collected via outreach events. This can represent another way to generate further replies from multiple stakeholders who might not submit a written response otherwise.

These site visits and outreach events might be time and resource intensive but they could drive up engagement of specific targeted groups.



Changes to the SORP could be also go through a phase of 'user testing'. The changed SORP could be piloted with different types of charities in order to decide whether the changes have been implemented in way that makes most sense to the end users of the SORP.

**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?**

We would like to echo the recommendations by the Association of Accounting Technicians (AAT) and the Association of Charitable Foundations (ACF) on reaching out to media and journalists (sector and trade press) and encouraging them to take part in consultations; as well as smaller charities and specialised external auditors/independent examiners that deal mainly with smaller charities by income.

There are some more specific organisations such as the Small Charities Coalition, Inclusive Boards and the Young Charities Trustees network which could be approached as well.

**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; (g) the accountancy profession; (h) commentators on the sector and journalists; (i) any other categories you consider relevant?**

DSC thinks that this is probably more a question of inclusion of different voices rather than weighting of responses. Weighting of responses might be difficult because this would probably come down to a qualitative exercise and it is difficult to imagine how this would be applied in practice. We assume that reviewers will already make some form of qualitative judgement on consultation responses, and there is already leeway to take some responses more into consideration than others.

In general, it makes sense to take the views of those affected by changes to the SORP and those with greater technical experience more into account. There is also a need to have a good balance between the views of those who read accounts and those who prepare them.

Changes to the advisory Committee and the consultation process would probably already help to achieve that balance to a larger extent (see answers to Q. 5 and Q8).

**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?**

Please see answer to Q.10.

**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?**

Please see answer to Q.10.

**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?**

There is a wider ecosystem of information sources that people use to explain and understand what charities do and how they deliver against their mission. This includes summaries and visualisations of financial information which are prepared for different types of audiences. For example, financial summary reports and overviews for donors who don’t have the technical knowledge to read the full accounts but want to be informed about different types of spending by charities. The Charity Commission register also provides financial information and rankings of charities for example on investment, spending and income based on financial information from the annual return and charity accounts.

The SORP development process though should be limited to all financial reporting that is legally required by charities. This will ensure consistency of the information provided, ensure reliability of the SORP document and limit the burden of compliance work for charities. It will also limit the burden on preparers because they do not have to take into account a second set of information on non-statutory financial reports and how the Charities SORP applies to it.

**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?**

Ideally statutory and non-statutory information that is used by practitioners and presented to others would be linked up and well explained. The Charity Commission’s registry is an invaluable source for the sector and is based on the best and most up to date financial information available. Parts of the information can be quoted out of context nevertheless. If used incorrectly it can add to a false narrative about the work charities do and how they operate, in particular when it comes to information on reserves and spending on charitable activities.

Any guidance and templates that can help to prevent this misuse of information and which can help charities to improve the understanding of what they do on behalf of various stakeholders can be helpful.

A separate document on non-statutory financial reporting could include guidance and templates that help charities to improve their communication of financial information to other stakeholders and provide information on how to prevent misquoting of charity financial information. Technical knowledge around the SORP can inform this guidance. The SORP Committee might not have enough capacity to develop such document but it could assist other bodies in doing so – for example the Charity Commission. This could also ensure

that new resources are integrated into other guidance that people already use (like the charity trustee welcome package).

**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?**

Please see previous responses above.

**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?**

Not at this time.

### 3. About DSC

The Directory of Social Change has a vision of an independent voluntary sector at the heart of social change. We believe that the activities of charities and other voluntary organisations are crucial to the health of our society.

Through our publications, courses and conferences, we come in contact with thousands of organisations each year. The majority are small to medium-sized, rely on volunteers and are constantly struggling to maintain and improve the services they provide.

We are not a membership body. Our public commentary and the policy positions we take are based on clear principles, and are informed by the contact we have with these organisations. We also undertake campaigns on issues that affect them or which evolve out of our research.

We view our role as that of a ‘concerned citizen’, acting as a champion on behalf of the voluntary sector in its widest sense. We ask critical questions, challenge the prevailing view, and try to promote debate on issues we consider to be important.

### 4. DSC’s Policy Principle of Responsible Regulation

DSC believes that charities’ activity should be regulated responsibly. Some regulation is necessary to safeguard and maintain the interests of the general public, the beneficiary, and of the organisations and individuals being regulated. However, it should have a demonstrable benefit and should aim to empower and strengthen charities rather than control them unnecessarily.

#### **a) Regulation should be proportionate**

Regulation must strike a balance between perceived risk and intended benefit. It should recognise the diversity of voluntary sector activity and be developed and applied in a proportionate way.

#### **b) Regulation should be appropriate**

Regulation must be informed by the characteristics, capacity, and needs of the organisations and individuals that are being regulated. Insofar as is possible it should be focussed, rather than acting as a blunt instrument that has unintended effects.

#### **c) Regulation should be enabling**

Regulation should seek to empower rather than control voluntary activity. The reasons for the regulation and the regulation itself must be properly understood by those institutions which are applying it. It should be accessible and intelligible to those being regulated. It should seek as far as possible to encourage self-regulation rather than focus simply on enforcement.