Robinson Reed Layton
Charity Newsletter – Autumn 2014

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CHARTERED ACCOUNTANTS and CHARTERED TAX ADVISERS

Introduction

Welcome to our latest charity newsletter. Two new Statement of Recommended Practice (SORPs) were issued in July 2014 by the joint SORP making committee (Charity Commission and OSCR).

In this edition we take an initial look at these new SORPs and how this may affect your charity. If you would like any further information about these changes please do not hesitate to contact one of the charities team.

Mark Williams
Partner

Changes ahead for charities

At present, in order to produce your charity accounts, relevant legislation and the SORP 2005 (amended in 2008) are used to determine the relevant accounting treatments, formats and disclosures. SORP 2005 is based on current UK GAAP. A new Financial Reporting Standard (FRS 102) is replacing all existing UK accounting standards, with the exception of the Financial Reporting Standard for Smaller Entities (FRSSE) which is available only for small entities.

For accounting periods commencing 1 January 2015 the current version of the Charities SORP will be withdrawn.

One of the new SORPs will need to be implemented. Smaller charities will have the choice of Charities SORP (FRS 102) and the Charities SORP (FRSSE). Larger charities will have no choice and will need to adopt the Charities SORP (FRS 102).

The Charities SORP has always provided a comprehensive framework on charity accounting and disclosure for the sector and this is still the case.

One question that will certainly be on the mind of charity Trustees for smaller charities will be which SORP to use going forward – the FRSSE or the FRS 102 version.

Pages 3 and 4 highlight the pertinent facts that charity trustees will need to consider in order to answer that question. It also includes an overview of what the key changes will be and how this could impact your charity in particular regarding the disclosures in the accounts and any impacts on the level of surplus/deficit in the SOFA.

Frequently asked questions (FAQs)

We have answered below a number of FAQs which we hope will assist your understanding of the impact of these changes.

For most charities, and in most areas of the accounts, the changes introduced will not be significant but for some they will be. This means that certain decisions will need to be made and in some cases information will need to be collected well in advance of actual implementation.

Both SORPs (and various helpsheets) are available on a new charity SORP website: http://www.charitysorp.org/.

The SORPs have been published in a modular format and this has been greatly welcomed by the sector as it allows users of the accounts to pick and choose the relevant modules for their particular charity and allows them to effectively only chose what is required.

Why are there two new SORPs?

The reason for having two new SORPs (rather than having just the one like we have seen previously) is that one SORP is specifically for smaller charities (see below) applying the FRSSE and is called the SORP (FRSSE) and the other is for larger charities and is based on the new accounting standard, FRS 102. The SORP (FRSSE) is relatively unchanged from the 2005 SORP.

The changes focus on financial statement presentation with the underlying accounting requirements relatively unchanged from the 2005 SORP.

What is the definition of small in this context?

Although not all charities are incorporated as companies, in order to determine whether a charity can use the FRSSE, the size definition from company law is used. There are three criteria:

Turnover (in the case of a charity: income)
£6.5m
Balance sheet total (gross assets)
£3.26m
Average employees
50

Only two out of the three criteria need to be met and there is a prior year rule which must also be considered (i.e. the size that they were in the previous year and the size they reported as this will impact the size they report as in the current year).

These limits are likely to increase in the future but when this will be is still in doubt.

The charity did not apply the FRSSE previously, is this an issue?

No, as long as they meet the criteria, a charity can choose to apply the FRSSE even if they have not done so previously. However this would be a change in accounting policy and thus restatement of figures would be required.

What about really small charities?

Unincorporated charities with income of less than £250K can prepare 'receipts and payments' accounts. If you fall into this category then you will not have been preparing your accounts under the Charity SORP previously and this will still continue under the new SORPS. Both new SORPs are solely for accruals accounting.

NB: all charitable companies must prepare accounts under accruals accounting.

As a small charity, why would we not apply the SORP (FRSSE)?

The SORP (FRSSE) is similar to the 2005 SORP and so on first glance it may seem beneficial for small charities to adopt. However the life of this particular SORP is likely to be short.

Initially when FRS 102 was drafted, it was expected that this would only be used by the larger entities and that the FRSSE would be retained for smaller entities. However, recent government consultations have highlighted plans to withdraw the FRSSE for periods commencing 1 January 2016. As such charities which plan on using the SORP (FRSSE) should be aware that it is anticipated they will face further change to accounting policies and disclosures once the accounting treatment for small entities has been decided on. CC guidance in the form of Help Sheet 3 (on the SORPs) notes that in due course the SORP (FRSSE) will need to be withdrawn and updated to align with the replacement framework.

There are a number of accounting areas where the FRSSE is silent such as:

- non-exchange items (donations/grants/ legacies);
- financial instruments;
- heritage assets; and
- some areas of group accounting; joint ventures and associates and merger accounting.

In these instances, charities should have regard to their existing accounting policies first. If it is a new transaction (and thus there is no existing accounting policy) then there should be due regard for current practice (i.e. consideration of FRS 102).

The format of the SOFA has been amended to align with the format for FRS 102 (see below).

Are there any benefits of using the SORP (FRSSE)?

As noted above, the underlying accounting is very similar to the 2005 SORP and thus charity trustees (and other users of the accounts) may find them perhaps easier to prepare and analyse.

The key changes between the SORP 2005 and SORP (FRSSE) are as follows:

- Goodwill should be amortised over its useful economic life which should be no more than 5 years unless its useful life can be measured reliably. It must not exceed 20 years;

- the related party definition has been updated to align with FRS 102 including the definition of key management personnel; and

- an exemption for disclosure of intra-group related party transactions where subsidiaries are owned 100% has been added.

The biggest perceived advantage for the preparers of accounts will be the fact that no statement of cash flow is required under the FRSSE. However this could be seen as a disadvantage to users of the accounts who find that level of information helpful.

When do we need to start using the new SORPs?

Both SORPs are mandatory for charities with reporting periods beginning on or after 1 January 2015.

Can we early adopt either SORP?

Not at present. The 2008 Accounting Regulations require that the 2005 SORP is used to prepare accruals accounts. Until there is an update to these regulations to allow for either of the new SORPs then SORP 2005 must be used.

Does this mean our first set of accounts under the new SORP will be in 2015?

It applies for reporting periods beginning on or after 1 January 2015. As it is very rare for charities to have a longer or shorter reporting period than 12 months, the likely impact is that first time accounts will start from 31 December 2015. For charities with March year ends, the first set of accounts will be 31 March 2016.

Why are charities being told to prepare now?

For many charities the first year set of accounts under either of the new SORPs will be 31 March 2016. The change to the either of the new SORPs will be a change in accounting policy and this means that the comparative figures will need to be restated.

If the charity has a March year end, then the figures for 31 March 2015 will need to be restated (re-prepared under the new accounting regime). In order to get these figures correct, it is necessary to actually go back to the beginning of that year. As such the numbers will need to be recalculated for 1 April 2014 and this date has already passed. This date is referred to as the transition date.

Both SORPs use the words, 'must' and 'should' – what is the implication?

The new SORPs have tried to make it clear what is a requirement (must) and what is best practice for the sector (should). These words are used throughout the new SORPs. Non-adherence to a 'must' in the standard is a departure from the SORP. However non-application of a 'should' is not regarded as a departure from the SORP but merely not conforming to best practice. Non-disclosure (or non-accounting) may lead to the accounts not representing a true and fair view. If the accounts are audited this will potentially impact the audit report.

Summary of the key changes from SORP 2005

Trustees Reports (for all size charities under either FRS 102 or FRSSE):

- Reserves policy – if trustees decide that holding reserves is unnecessary then the report must disclose this fact and provide reasons; and
- Where the number of charity trustees is more than 50 the concession has been dropped regarding non-disclosure of all their names. Now all trustee names must be reported.

For charities which require a statutory audit (again under both FRS 102 and FRSSE):

- Extra disclosure on social investment policies;
- Explanation of the financial effect of significant events;
- More disclosure on the principal risks and uncertainties;
- If the charity makes material grants to institutions then disclosure must be made in the notes or the trustees' report.
- Disclose arrangements for setting pay and remuneration of key management personnel and any benchmarks / criteria used in their setting.

SOFA

Changes	SORP FRS 102	SORP FRSSE
Income recognition based on entitlement, measurement and '*probable*' rather than *'virtually certain' (2005 SORP)*	Yes	Yes
SOFA headings (horizontally) changed to 'plain English'	Yes	Yes
Gains / losses on investment assets above net income / expenditure line	Yes	No – must go below net income / expenditure line

Transfers between funds must always net to nil	Yes	Yes
Extra guidance and clarification on accounting for legacies	Yes – also includes if distribution is deferred more than 12 months	Yes

Other

Changes	**SORP FRS 102**	**SORP FRSSE**
Statement of cash flows required	Yes	No
More disclosure on going concern: material uncertainties	Yes	Limited
More disclosure on going concern: no material uncertainties	Yes	No
Updated definition of related parties	Yes	Yes

Balance sheet

Changes	**SORP FRS 102**	**SORP FRSSE**
Holiday pay accrual / prepayment required	Yes	No – but can include if preferred
Discounting of liabilities if settlement is over 12 months	Yes	Not required
Guidance on investment properties held as mixed use	Yes	No
More technical accounting for complex financial instruments (e.g. interest rate swaps)	Yes	No

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