THE NEW CHARITIES SORP

What do I need to know?

The new Charities SORP comes into effect for accounting periods commencing on or after 1 January 2015 and sets out the accounting treatment that charities must adopt.

The guide below sets out the key changes applying to those charities that prepare accounts under the Financial Reporting Standard 102 ("FRS 102").

STRUCTURE OF THE SORP

The SORP is split into 29 different modules – 14 core modules that apply to all charities, and 15 specific modules that relate to particular areas or types of transaction and should only be applied if relevant.

The SORP also takes a "think small first" approach throughout – beginning with the requirements for all charities, before stating the additional requirements for larger charities.

MUST, SHOULD AND MAY

Throughout the SORP, requirements and recommendations are distinguished by the terms:

Must	– mandatory
Should	– best practice but not compulsory
May	– optional

TERMINOLOGY

FRS 102 terminology has changed, with the balance sheet becoming the Statement of Financial Position, stock becoming inventory, and debtors and creditors becoming receivables and payables respectively.

The new SORP allows charities to retain existing terms and actually uses the old terminology itself. However, given trading subsidiaries will adopt the new terminology, it is recommended that charities also adopt this.

FUND ACCOUNTING

There are no changes to the requirements to adopt fund accounting but all fund transfers must net to £nil. This means that any transfers or acquisitions of assets from another trust or charity must be accounted for by recognising a gain in the Statement of Financial Activities equal to the value of the assets transferred.

STATEMENT OF CASH FLOWS

A statement of cash flows is now required, with cash flows categorised between operating, investing or financing activities. This may also be analysed by fund.

STATEMENT OF FINANCIAL ACTIVITIES ("SOFA")

Comparative figures for total funds must be shown on the face of the SOFA - the analysis of these comparative figures by fund can be done either on the face of the SOFA or prominently in the notes to the accounts.

Any discontinued operations must be separately disclosed on the face of the SOFA.

The SORP states that it is best practice to disclose material fraud or the loss of a material tangible fixed asset either on the face of the SOFA or in a supporting note.

SOFA CATEGORIES AND HEADINGS

The layout of the SOFA has changed: the number of categories has reduced, and the names of the headings have changed.

Net gains/losses on investments are now included within net incoming resources. All other gains/losses are still included within the recognised gains and losses section after net incoming resources.

ACCOUNTING POLICIES

Additional disclosures are now required and include: key judgements made in adopting accounting policies, and any assumptions or uncertainties that give rise to a significant risk of future material misstatement.

All charities must describe any uncertainties regarding their ability to continue as a going concern. If there are no such uncertainties, this fact should also be stated.

PRIOR YEAR ADJUSTMENTS

These are now required for all material errors, and not just fundamental errors as previously.

BRANCHES

The new SORP excludes from the scope of branch accounting those charities that are independently governed by a separate board of trustees. This includes overseas entities where local law requires operations to take place through a local legal entity.

This means that such entities must be consolidated into group accounts as subsidiary entities.

TRUSTEES' REPORT

The names of all trustees must now be disclosed within the accounts - this cannot be limited to 50 names.

The different sections can be included in the order the Trustees consider appropriate, but the new SORP has changed the suggested order so that objectives and activities, achievement and performance, and the financial review are the first three sections.

There has been a change in emphasis with the Trustees' Report such that it should be both fair and balanced. This means acknowledging both successes and failures, describing positive and negative factors affecting achievements and performance, and describing the impact on beneficiaries.

The SORP refers to Public Benefit for the first time and requires an explanation of activities undertaken for public benefit.

The financial review section must explain the charity's reserves policy, stating the amount of reserves held and why. If the Trustees consider that no reserves are required to be held, this fact must be disclosed together with the reasons behind this decision.

The Trustees' Report must also include details of any material fund or subsidiary that is in deficit, including explanations as to why the deficit has arisen and the steps being taken to rectify this.

Large charities must also include additional disclosures such as an explanation of major risks and how these are managed, details of criteria used to assess performance, and a description of plans for the future. Larger charities are also encouraged to develop and use impact reporting (i.e. the long-term effect of their activities on both individual beneficiaries and for wider society).

STRATEGIC REPORT

Medium and large charitable companies must prepare a strategic report, as required by company law, which is presented as a distinct section of the Trustees' Report. This involves integrating the achievements and performance, financial review, and future plans sections into one group headed as the Strategic Report.

INCOME

The recognition criteria have changed – income can be recognised if a charity is entitled to it, receipt is probable (i.e. more likely than not – this has changed from virtually certain), and it can be measured reliably.

GRANT INCOME

Income must be recognised under the performance basis. This means that grant income is recognised once both the income recognition criteria are met, and any terms and conditions attached to the grant are met. If a charity receives government grants, it must disclose the nature and amounts of such grants, any unfulfilled conditions applying to the grants, and an indication of any other forms of government assistance from which the charity has directly benefited.

LEGACY INCOME

There is now increased guidance around recognition of legacy income, and in particular with regards to entitlement.

The SORP states that entitlement cannot arise without knowing of the existence of the death of a benefactor and a valid will, and that evidence of entitlement exists when a charity is satisfied that a gift has been left to it and the executor is satisfied the asset in question will not be required to satisfy claims on the estate.

If a charity receives numerous legacies and has detailed historical information regarding settlement, it may apply an estimation technique in measuring the value of legacies to be recognised. This portfolio approach only applies to immaterial legacies – material legacies should be considered individually.

Legacy income due to be received after 12 months may, if material, be discounted to its net present value using an interest rate for a comparable deposit.

DONATED GOODS AND SERVICES

Where practicable to do so, donated goods should be recognised at fair value at the time of receipt – if this is not practicable, the goods should be recognised at the point of sale or distribution.

In determining fair value, factors to consider include the cost of the item to the donor or the estimated resale price less costs to sell.

Charities receiving goods for resale under the UK retail gift aid scheme are acting as agent on behalf of the donor and are only entitled by law to an administration fee until such time as the donor waives their entitlement to the sales proceeds. Charities with historical data may use an estimation technique to determine the likely value of donations receivable in the form of administration fees and resale proceeds. Such a technique must include consideration of an adjustment to reflect the risk that not all donors will grant the sales proceeds to the charity.

Donated services should be recognised if the charity would otherwise have to pay for them and be measured at the value the charity would pay on the open market.

Charities must not recognise the value of the contribution of volunteers in the accounts, but instead provide an indication of the nature of their contribution.

GOVERNANCE COSTS

These are no longer shown separately on the face of the SOFA, but are included as a category within support costs and allocated across the different activities.

GRANTS PAYABLE

Grants payable should be recognised once there is an obligation to make a payment, the payment is probable, and the payment can be measured reliably.

If there is no legal obligation to make a payment or provide services, there may be a constructive obligation if a promise has been made, this has been communicated to the recipient, and there is an established pattern of practice indicating the charity will meet its commitment.

Grants payable over a period of more than 12 months should be recognised in full unless future payments are subject to review by the donor that allows it not to make the payment. Balances due for payment after 12 months must be discounted to their net present value using a comparable interest rate to borrow.

Any contingent liabilities for grants payable must be disclosed, including the time-frame of the commitment, any performance related conditions, and how the commitment will be funded.

Grants payable can be disclosed in a separate document outside of the accounts, as long as this list is published on the charity's website and the web address is disclosed in a note to the accounts.

SALARIES

All charities must disclose the total remuneration paid to key management personnel as well as providing the number of employees earning in excess of £60,000 in bands of £10,000.

Charities may choose to disclose details of remuneration paid to the Chief Executive Officer or highest paid member of staff, or disclose remuneration paid to key management personnel on an individual basis.

Larger charities must disclose the remuneration policy for senior staff in the Trustees' Report.

HOLIDAY PAY

Holiday pay earned but not yet taken must be recognised, if material, where carried forward from one accounting period to the next.

DEFINED BENEFIT MULTI-EMPLOYER PENSION PLANS

These can be still be accounted for as defined contribution plans, but if the charity has entered into an agreement to clear any deficit relating to past service then such a liability must be recognised.

RELATED PARTY TRANSACTIONS

The definition has been extended to include key management personnel and their close family.

INTANGIBLE ASSETS – DEVELOPMENT COSTS

Databases can be capitalised if purchased and if strict criteria are satisfied. Capitalisation is likely to be rare – the technical and financial feasibility of the development asset must be demonstrated.

GOODWILL

Unless the useful life can reliably estimated, the default amortisation period has reduced from 20 years to 5 years.

FINANCIAL INSTRUMENTS

Basic financial instruments include trade debtors/creditors, simple overdrafts and loans, and investments in shares. These are valued at amortised cost using an effective interest rate (under FRS 102 this means market rate).

Other financial instruments include all items not classed as basic, such as interest swaps, forward contracts and hedging instruments. These are measured using fair value accounting.

Balances due for receipt after more than 12 months must be discounted to present value, if the time value of money is material.

CONCESSIONARY LOANS

These are loans made to or received by a charity to further its purposes and any interest charged is below the prevailing market rates. Such loans can either be measured at the amount paid adjusted for accrued interest, or by measuring at amortised cost using the effective interest method.

INVESTMENT PROPERTIES

These are initially recognised at cost and subsequently at market value (if market value is not available, they can no longer be shown at depreciated cost).

MIXED USE PROPERTY

Such property should now be split between the part used for investment (investment properties) and the part used for day-to-day operations (tangible fixed assets).

If a charity cannot measure the fair value of the investment element, the entire property should be held within tangible fixed assets.

SOCIAL INVESTMENTS

Programme-related investments are held to further a charity's objectives. Income is included within other income, and expenditure within expenditure on charitable activities. Gains on disposal are included within other income.

Mixed motive investments are held partly to achieve a financial return. Any impairment and any gains/losses on disposal, are included within gains/losses on investments.

LEASES

Lease incentives are now spread over the full period of the lease.

Finance leases are those where substantially all risks and rewards of ownership are transferred - the 90% rule has disappeared.

ABOUT GOODMAN JONES CHARITY GROUP

We help charities and social businesses by providing advice, support and reassurance that all the financial aspects are well-managed, allowing you to focus on your important work.

By keeping up to date with the ever-changing, ever-demanding requirements in the sector, we are able to keep our advice cost-effective by having solutions at our fingertips. Our online accounting system also keeps time and paperwork down to a minimum.

We have recently been lecturing, by invitation, on the SORP.

We regularly blog on this and other issues affecting the sector, please visit the website or follow us on LinkedIn or Twitter to be kept up to date

If you would like us to review your accounts in light of the new SORP requirements, please contact Martin Bailey on martin.bailey@goodmanjones.com or on 020 7388 2444