



## **Consultation: Guiding the Development of the Charities SORP**

Response from the Association of Charitable Foundations

1 February 2019

### **Summary**

The Association of Charitable Foundations (ACF) is the membership body for UK foundations and grant-making charities, with more than 380 members. We are submitting a response in this capacity and as an observer member of the SORP advisory group.

Our members have a crucial perspective on charity accounts in that they have a dual role:

- They are charities in their own right, with the vast majority required to produce accounts in accordance with the SORP, but distinctive in that the majority have substantial financial assets that they manage.
- They are also organisations that read accounts as part of everyday practice, and need to understand those submitted to them by charities seeking grants or other forms of financial assistance.

In regards to the governance and development of the SORP, this response makes the following observations and recommendations:

- The SORP is complex and long, and is generally regarded as a significant administrative burden for charities, particularly those at the lower end of the income spectrum who are required to comply with it.
- This review might consider how the SORP can, in future, be more proportionate to those it applies to. For charitable foundations in particular, income does not necessarily correlate with staff resources, with many foundations who are required to be compliant with the SORP operating with few or no paid staff.
- We recommend a better balance on the advisory board between those who prepare accounts and those who read them, in particular there should be greater representation of charitable foundations which bring vital experience and expertise. Technical expertise is essential, as is representation from stakeholders with a range of views and insights into the use of charity accounts, including beneficiaries, the public, fundraisers and charity trustees.

- The Committee's more recent development of thematic sub-groups has produced some helpful contributions, and this model could be expanded to examine different aspects of practice with a wider audience.
- We recommend more transparency in the governance of the SORP Committee and its decision-making, for example the process of recruiting and appointing to the advisory board, and the remit of the different roles within it.

We appreciate this opportunity to engage with the review. For more information or to discuss this response in greater detail, please contact [max@acf.org.uk](mailto:max@acf.org.uk)

**Q1. 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.**

ACF is pleased to respond to this consultation on 'Guiding the Development of the Charities SORP'. We have been delighted to support the SORP-making body through our observer status membership on the SORP Committee, and we welcome the regulators' willingness to engage in a consultation on this important matter.

ACF is the membership body for UK foundations and grant-making charities, established in 1989. Driven by a belief that foundations are a vital source for social good, our mission is to support them to be ambitious and effective in the way that they use their resources. We do this through the provision of policy and advocacy, research and information, and a wide-ranging programme of events and learning. Our 380 members collectively hold assets of around £60bn and give more than £3bn each year.

Trusts and foundations, as charities themselves, have always been and will continue to be at the forefront of supporting charitable endeavour, and at the heart of civil society. Trusts and foundations have a direct interest in charity accounts for two main reasons. Firstly, as charities themselves, they are required to produce accounts of their financial activity. Secondly, as funders of other charities, nearly all will rely on charity accounts as a principal source document for undertaking due diligence assessments of applicants and grantees, both when considering a financial or other support for another organisation and for ongoing monitoring of how that support is being utilised.

As the membership body for UK trusts and foundations, ACF has a keen interest in the rules and guidance related to the creation of charity accounts, given how centrally important they are to our members, and in the issue of transparency more broadly. Foundations are increasingly striving to be more open about their own practice – not just through robust accountancy practices and legal compliance, but as sector-leaders in active transparency. Many are doing this because they believe it is both right in principle and as a way to best deliver their charitable missions<sup>1</sup>.

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<sup>1</sup> An example of this are the foundations that helped to support the establishment and development of 360Giving, an online resource that draws upon open source data of foundation giving, which currently has 96 organisations publishing grants data to the 360Giving open data standard. Recently, ACF convened a new working group on Transparency and Engagement, comprised of trust and foundation leaders as part of ACF's

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

We agree with the list of users as set out on page 3 of the consultation document. Most particularly for ACF, we agree with the consultation document's statement that *"Donors and funders...are some of the most active readers and users of charity accounts"*.

Charitable foundations are principally grant-makers, but are increasingly delivering their missions in a variety of other ways in addition, such as in-house policy and research initiatives, convening, social investment and non-financial support. In this capacity, trusts and foundations are likely to use charity accounts in the following ways:

- As part of an initial financial due diligence assessment of a prospective grantee on receipt of a grant application;
- To investigate who else is funding a prospective or current grantee;
- To understand a prospective or current grantee's mission, values and activity;
- To identify potential organisations for a targeted grant for a specific project or activity;
- On at least an annual basis, to monitor a grantee's compliance with charity law, account reporting and to inform checks of financial robustness;
- To ensure a grant was correctly recorded (e.g. as restricted income) in a grantee's accounts.

Aside from the financial data (particularly the balance sheet, and the notes on assets, restricted and unrestricted income), the trustees' statement on charitable activities, the financial report for the year, and the reserves policy are the most utilised aspects of charity accounts for most foundations. Many foundations will also produce accounts in accordance with the SORP as charities themselves.

In addition to the list on page 3, we would suggest that the general public and the media are two groups for whom charity accounts matter. In terms of to whom charities are accountable and of demonstrating public benefit, principally this is to those people or communities that the charity serves, its donors, and more broadly the general public. On a statutory basis, they are accountable to the regulator and the legal institutions that have an interest in their practice.

**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?**

Charity accounts, as well as providing clear financial information about assets, income and expenditure, are an opportunity for a charity to report on the extent to which it has delivered its mission in that year, what impact it believes it has had on its beneficiaries and communities of

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Stronger Foundations initiative. This will explore the ways in which foundations seek to be transparent, the benefits and the challenges. A report of the group's enquiries will be published in early 2020, but meeting summaries will be made available throughout 2019.

interest, and how its governance processes and structure are fulfilling its objectives, financial needs and legal obligations. It is an important obligation for all charities that they are required by law to reflect on these matters and report on them publicly each year. The qualitative information in charity accounts, in combination with financial data, is an essential way for readers of accounts to understand the purpose, effort and impact of the charity.

Achieving the right balance of content between data and commentary is key, and this could be improved to ensure greater consistency across charity accounts, where effort is more often focused on the financial data, and less given to the narrative sections (which many general readers will prioritise). As was expressed in a SORP Committee meeting in 2018, referencing a long-held aspiration about charity accounts, *'there should be no data without words and no words without data'*.

It is important to note that, while charity accounts are required of nearly all charities, the vast majority of charities are not required to follow the SORP. According to the Charity Commission for England and Wales' register<sup>2</sup>, around 80% of charities in England and Wales have an income of less than £250,000, and therefore are not usually required to produce accounts that comply with the SORP<sup>3</sup>. This is also the case for a similar proportion of charities in Scotland and Northern Ireland<sup>4</sup>.

90% of charity income in England and Wales is received by the top 7% of charities, fewer than 12,000 charities in total (with 72.5% received by just 2,263, or 1.3% of the total). Therefore, it is reasonable to assert that the SORP is applied to a minority of charities, and is helpful in obligating them to include information that might otherwise not necessarily be presented, and in a way that is comparable both to other years and to other charities.

It seems reasonable that charities with a relatively high income are required to be more detailed in what they report about their activities and financial information. At present, only 20% of charities are required to comply with the SORP, yet there is still a huge range within this group. Nearly two-thirds of those required to use the SORP receive an income of less than £500,000 each year. To require charities with an income of between £250,000-500,000, nearly always with a small volunteer board, to comply with a SORP that is 195 pages in length seems a disproportionate expectation. The result is that many charities will fail to fulfil what is required, inadvertently misreport, or provide a level of detail that is disproportionate to its levels of activity.

A reduction in the burden for these smaller charities would seem more proportionate and still enable robust financial and impact reporting. There is potentially a case to be made that the SORP should only apply to charities with a far higher income (e.g. £500,000).

It is also important to note, particularly in relation to foundations, that income is not necessarily a reliable indicator for capacity of operations. Many grant-makers receive a relatively high income (principally from investment dividends), the majority of which is usually distributed through grants

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<sup>2</sup> <https://www.gov.uk/government/publications/charity-register-statistics/recent-charity-register-statistics-charity-commission>

<sup>3</sup> We estimate that around 40% of ACF's members have an income of less than £250,000.

<sup>4</sup> SCVO State of the Sector 2018 – [webpage](#) on 'Income'; The Charity Commission for Northern Ireland – [online search directory](#)

to others. This is commonly administered by a small staff team, often a single member of staff working part-time. Therefore, it should not be assumed that a charity with an income of more than £500,000, or even one with income in the £millions, has an operation that is automatically proportionate to the demands of the SORP.

In any case, it would be beneficial for the SORP to be substantially reduced in length, to increase both engagement and compliance, and avoid (as is seemingly the case in many instances) the SORP being seen as something to outsource to a technical expert rather than embraced by the charity.

**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?**

We think it is very important that the SORP-making body is supported by an advisory board involving people with expertise who do not work for the regulators.

The SORP Committee has developed some helpful contributions in the last year examining different aspects of practice, such as transparency, proportionality, and tiering.

The establishment of a variety of time-limited sub-groups in between meetings of the Committee seems to have worked well, and seems a useful function to develop and continue with to gain valuable insights and more detailed input.

The answers below address how the current arrangements could be improved and expanded.

**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.**

The current composition of the SORP Committee involves representatives from some charities, infrastructure bodies, and technical experts (primarily staff employed by accountancy firms). At present, the vast majority of the members are those who are directly responsible for the preparation of accounts, which limits the Committee's ability to reflect on and share direct experience of their use.

In our view, the advisory board would be improved if it were represented by at least as many people who read and use charity accounts as those who prepare them. For example, there is no representation from funders or donors (other than ACF as a membership body, and only in an observer capacity), who are possibly the most frequent users of charity accounts.

In addition to ACF's involvement, which we would very much like to maintain, we recommend a greater representation of funders, particularly institutional philanthropy (e.g. a cross-section of grant-making charitable foundations).

There is currently no representation from fundraisers (who could be represented by a fundraising infrastructure organisation), charity beneficiaries, or the wider public interest (e.g. sector specialist trade media), all of whom have a direct interest in, and insight into, the use of charity accounts.

There is no specific representation from trustees of charities (i.e. those with legal responsibility for the preparation of the accounts) except in an indirect way (in that some members are themselves trustees of charities, but who are not attending the Committee in that capacity). This could be addressed in part by ensuring representation from charity chairs and/or trustees.

Currently, the recruitment and appointment process is unclear and not sufficiently transparent, and this should be addressed even if the current arrangement and process is unchanged.

**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?**

While the nature of the task is inherently technical, its interpretation and application is intended to be undertaken by trustees who will usually be informed non-experts (only rarely will trustees be professional accountants or charity lawyers). It is therefore essential that the technical work is grounded in the real experience of those who are tasked with preparing, owning (in the sense of being legally responsible for), reading, interpreting and responding to accounts. Rebalancing the group as per our answer to question 5, and enabling it to determine priority areas of focus, would be a good place to start to determine potential changes to the current approach.

**Q.7 Do you have any other comments on the structure, size or membership of the SORP Committee?**

It is not obvious why, at present, some attendees are 'members' and others 'observer members', or what practical difference this entails. We recommend that these points are either made explicit and explained, or that observer status is removed.

The membership of the group seems to be large enough (yet not too large to achieve the business of the day). The innovation of sub-groups perhaps lends itself well to the involvement of a greater number of people beyond this for a time-limited, specific contribution on a particular issue, such as through a one-off roundtable with key stakeholders to inform discussions and recommendations.

**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?**

In order to secure interest and contributions from users of charity accounts, consideration could be given to tailoring aspects of consultations to particular audiences, rather than inviting everyone to respond to all aspects, which can seem overwhelming and therefore off-putting. For example, if there are questions about transparency, small charities, or executive pay, it may be beneficial to

package these questions up as a specific feature for audiences with a specific interest. This could be achieved through more outward-facing work by the sub-groups.

Although SORP guidance affects a significant number of charities, very few have the time or resources to work on such technical policy issues, and therefore more engagement (e.g. events, more outreach, and short surveys) might make it easier to engage with rather than a full written consultation.

Following this, a 'testing phase' might be beneficial, where charities of different sizes pilot the new guidance. A similar process could be undertaken with readers of accounts to determine what format and content they find most helpful.

**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?**

Our answer to question 5 and the suggestions given are also applicable to this question.

**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?**

This list of groups in the question is useful in terms of not only those who should not only be consulted, but who might be represented in the SORP Committee itself.

It is not obvious how the views of different groups could be differentially weighted. However, an equal weighting between preparers and users of accounts would seem reasonable, as it would on the Committee itself. As noted above, we agree that foundations are a key audience for engagement, as well as for direct involvement in the advisory committee.

**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?) and **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?)

There may be charities and others for whom a written response is challenging, which is another reason that the regulators should ensure that there are other ways for stakeholders to engage.

**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?**

We think it is useful and expedient to limit the SORP to financial reporting required by charity law, primarily to ensure a greater degree of consistency and limit the burden on charities to what is legally required. Limiting what is mandated in this way does not prevent charities from including additional information, and charities could be reminded this is possible and permitted.

**Q.14 If you think 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?**

A short guide to the general purposes of charity accounts, who reads them and why they matter (perhaps along with some examples of the potential additional information that can be included) would be helpful to some. However, this may be better coming from the regulators (ideally in collaboration with key infrastructure bodies including ACF) rather than the SORP Committee, which on its own has a very limited reach.

**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?) and **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?)

We appreciate the efforts that the SORP-making body in running this consultation, and for its engagement to date with ACF and the foundation sector. We are grateful for the opportunity to feed in to this review, and will be pleased to provide further detail if required.

For further information or clarification, please contact Max Rutherford, Head of Policy, [Max@acf.org.uk](mailto:Max@acf.org.uk)

**END**