

Policy Proposal: The Future of UK GAAP – consultation paper

1 The Scottish charity sector

- 1.1 In Scotland, around 27% of charities are required to prepare accrued accounts and the demographic is broadly comparable in England and Wales. Therefore a significant number of charities are affected by proposals to change the relevant accounting framework.
- 1.2 A unique feature of the Scottish charity sector is that the content of Receipts and Payments Accounts (eligible to be prepared by unincorporated charities with gross income of less than £100,000) are codified by way of Schedules 2 and 3 of the Charities Accounts (Scotland) Regulations 2006 ('the Accounts Regulations 2006'). The requirements are predicated on the applicable provisions of the SORP for charities below the statutory audit threshold, particularly in relation to the content of the Trustees' Annual Report. Therefore, in Scotland, we have the unique situation that the accounting requirements for even small charities will potentially be impacted by changes to the current arrangements for charities preparing accrued accounts.
- 1.3 The current Charities SORP negates the need to read the separate SSAPs and FRSs and instead provides a comprehensive, 'one-stop shop' guide to preparing accounts; setting out the format of the primary financial statements and explaining the principles and rules that must be applied to income, expenditure, assets and liabilities that are included within the accounts. It contains guidance which focuses on the types of transactions and situations that charities are likely to experience with focused reference to individual sections of the FRSs where necessary. Although the preparation of accounts on an accruals basis does require a level of familiarity with accounting methods, procedures and terms, the current SORP is written in easier to understand language compared to the FRSs - it clearly recognises the needs and skills of the sector it serves.
- 1.4 In line with one of our key functions, OSCR prepares and issues guidance to charities in order to facilitate compliance with the legislative requirements. In the context of accounts, we have published a workpack for those charities who are eligible to prepare receipts and payments accounts – this provides

templates that charities can simply complete and submit to OSCR. In addition, we have recently published guidance on independent examination which is written very much for the non-professional accountant namely in Plain English with practical examples and illustrations to assist the reader.

- 1.5 With the current arrangements therefore, it is possible for charities to prepare their own accounts, to understand the requirements and to source appropriate independent scrutiny. The guidance that is referred to and used by preparers and examiners of charity accounts is the SORP and the benefits of its approach have already been outlined above. If the framework were to move to a situation where the preparer and examiner of accounts was forced to refer to guidance or a standard that did anything other than provide a 'one stop shop' to the requirements in a clear and simple manner, then there can be little doubt that this would result in charities simply being unable to prepare their own accounts unless they have the professional accountancy expertise within their own organization or can afford to buy it in. This would be a financial consideration, but crucially would potentially divorce charity trustees from a real understanding of their responsibilities in relation to accounts; it would also limit the pool of independent examiners. It would damage the culture of transparency and accountability which we have sought to create and protect and which underpins the sector; in our view therefore, these developments would be a retrograde step.

2 Progress since the introduction of the Accounts Regulations 2006

- 2.1 The implementation of the Accounts Regulations 2006 was a major step forward for charity accounting in Scotland as it provided legal status for the Charities SORP. There is little doubt that the quality of reporting has improved considerably over the past 3 years following implementation, not least because there is now a clear set of rules that must be followed and which are laid down in clear language, as well as OSCR's investment in guidance and support for the sector.
- 2.2 Since 2007, OSCR has undertaken thematic studies into the quality of charity accounts and compliance with the relevant requirements. The results of the most recent studies, undertaken in 2008/09 show that there is considerable improvement in compliance rates in relation to smaller charities preparing receipts and payments accounts and also those charities that are required to prepare accrued accounts. For example, the proportion of smaller charities including a trustees' annual report within their receipts and payments accounts in 2007 was approximately 33% - this increased to 80% in 2009. For further information regarding our study on small charity accounts, please refer to our website at

[Comparative Study on Smaller Charities](#) and for details of our study regarding SORP accounts, please refer to [SORP Compliant Accounts Baseline Study](#).

- 2.3 In spring/summer 2009, the Scottish Government consulted on proposed changes to the Accounts Regulations 2006, the responses to which have recently been published - refer to the Scottish Government website at [Consultation Responses](#).
- 2.4 A common theme in the responses is that the introduction of these Regulations has resulted in a positive impact on the sector and the information that is now made available by Scottish charities. Furthermore, there was little appetite noted for change to the regime as it was felt that the sector was now becoming more familiar and comfortable with the current rules and that there was no point in change for changes sake – better to allow the regime to bed in fully in its present form before considering any change.
- 2.5 OSCR has taken extensive soundings from the Scottish charity sector both before and since the Scottish Government consultation in the course of its day to day work and it is abundantly clear that the sector desires, and indeed needs, stability and, where possible, simplification of the applicable rules. To that end, while any opportunity for change can be positive, it is essential in our view that the resulting regime is one that is at least as straightforward as the current one. To confuse the sector or to add undue complexity to the current arrangements would potentially have an adverse effect and undermine the progress made in the first 4 years of effective charity regulation in Scotland. Again, it must be recognised that any changes to SORP may have an indirect impact on the requirements for the entire sector in Scotland owing to the influence of SORP on the content of receipts and payments accounts

3 Users of charity accounts

In considering the future of accounting in a charity context, the needs of those who use charity accounts must be seriously considered. Essentially, there are a number of users of a set of charity accounts:

- The charity itself (including the charity trustees)
- Beneficiaries of the charity
- Funders and donors
- The relevant charity regulator(s)
- The general public

We have already seen that the charity sector in Scotland is dominated by smaller charities and it is equally important that such organisations are able to understand how to prepare their accounts and what these accounts actually tell the reader about the charity. In our response therefore, we are mindful of the end user of charity accounts and the need to ensure that any change to the accounting requirements will have some value for end users, including charities themselves. Other users of accounts also need to be considered in terms of the usefulness and comprehension of a set of charity accounts by funders/donors. This strengthens the importance of having appropriate input and perspective in the development of the relevant rules and requirements.

4 Issues identified

Against this background, OSCR has identified a number of issues arising from the consultation proposals which we wish to highlight to the ASB. These are listed below and supplemented by detailed comment thereafter:

- The need to consider the use of the term ‘public benefit’ entity
- The need to ensure that the product that will be used by preparers of charity accounts (not limited to professional accountants) is:
 - Prepared on a ‘stand-alone’ basis to minimise the need for further accounting regulations
 - Written in non-technical language
 - Developed with adequate sector and charity regulator representation and input in order to ensure that it addresses the needs of the sector and impact on regulators, including the unique situations and transactions that often occur (a point already made at the meeting with ASB)
- The timeframe in which the proposals will be implemented

4.1 The language issue – ‘public benefit’

It is interesting to compare the definition of ‘public benefit’ entities per the consultation document in light of the requirements and guidance on the subject of ‘public benefit’ issued by both OSCR and the Charity Commission for England & Wales. It may be argued that the ASB definition is more akin to that of a social enterprise and certainly has the potential to cause confusion if it differs materially from the charity law definition which in Scotland is contained within the Charities and

Trustee Investment (Scotland) Act 2005. Whilst we acknowledge that the terminology used attempts to clearly differentiate special types of not for profit organisation, we would highlight our concern about the potential for confusion regarding the use of the term 'public benefit' in this context.

4.2 The end product – what preparers of charity accounts will use

4.2.1 We have already highlighted the positive aspects of the current framework for charity accounting in the UK in terms of having a SORP that is relatively simple to follow and that is focused on the charity sector. In considering what a future framework may look like, it is crucially important to focus on who will need to refer to a standard or guidance in preparing a set of charity accounts and therefore how the needs of preparers can best be served.

4.2.2 At present, the consultation document outlines possible options for the bases on which a public benefit standard or framework might be developed. We foresee difficulties with these options.

If a standard is developed that purely addresses areas where different accounting rules are required for public benefit entities, this will result in users having to refer to more than one document. A single reference document has been one of the clear plus points of the current SORP, as recent research has shown. There is also the issue of whether this standard would be written in the most appropriate style for the user and whether the development would include adequate input from relevant sector stakeholders. If a standard were developed on a standalone basis, the timeframe for development could potentially be significantly longer than would appear has been anticipated.

4.2.3 On the basis of the perceived difficulties with the options outlined in the consultation document, we strongly suggest that an alternative be considered. OSCR believes that the most effective way in which to arrive at a product which meets the needs of preparers of charity accounts is likely to be by way of a public benefit standard developed on a relatively conceptual basis. This would then require supplementing by way of guidance in some form. It would appear that the most efficient and effective manner in which this could be achieved would be to **retain the existing SORP framework** whereby the SORP provides a focused and practical interpretation of the PBE standard for the charity sector.

- The ASB already has a Policy and Code of Practice in place for SORPs and therefore the mechanism exists for the recognition of SORP making bodies and the development of SORPs. This would negate the need to develop a new process for the development of

additional guidance material which would undoubtedly be a time consuming exercise

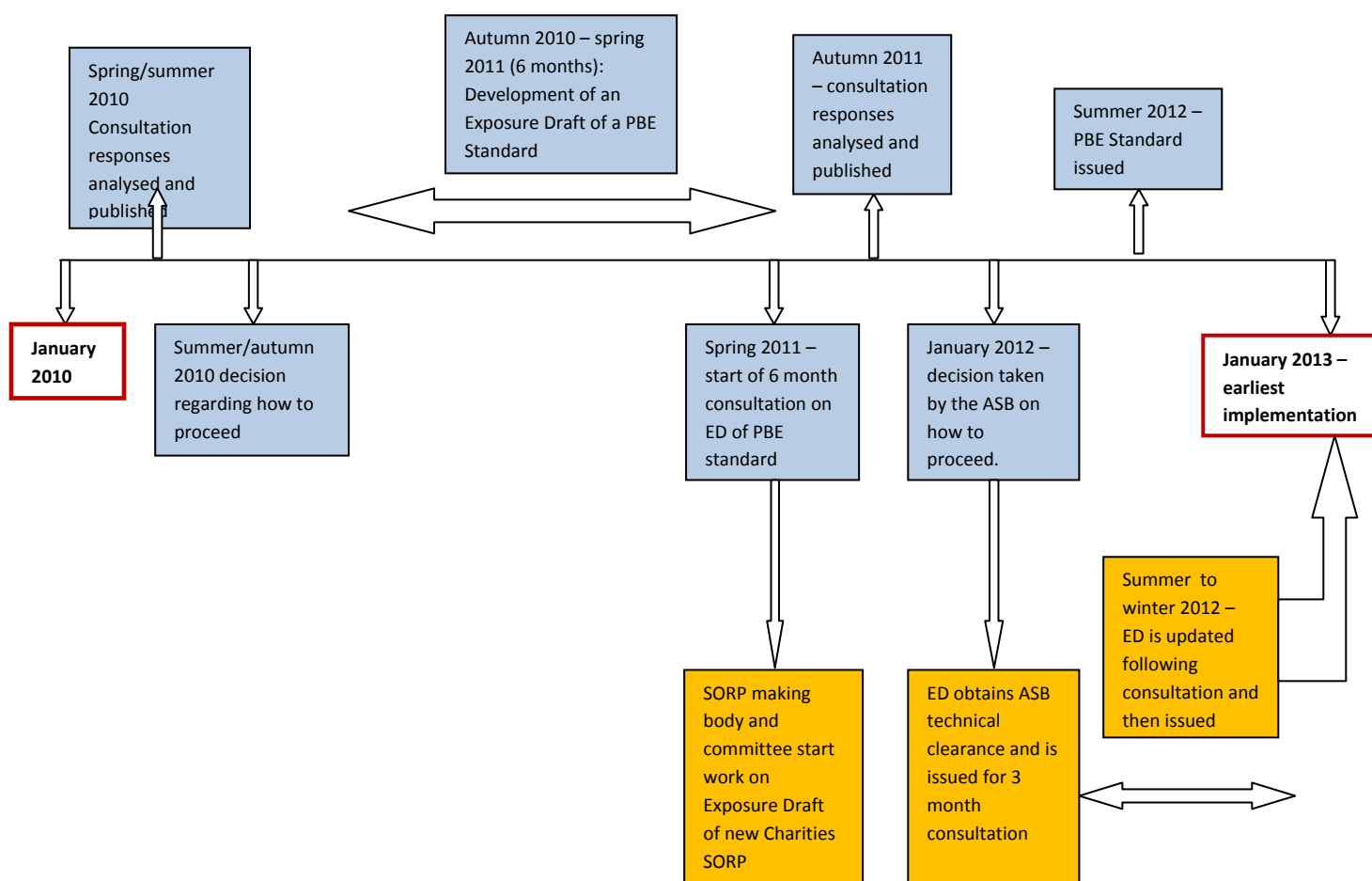
- The current Charities SORP making body and SORP Committee has representation from the sector in terms of regulatory knowledge and experience as well as those working within charities and as professional advisors and auditors. In 2006, the Committee was refocused and expanded to ensure more extensive representation. Arguably, the body and the supporting committee are best placed to understand the needs of the sector and to therefore develop material that is relevant and useful for its constituents

- The regulatory landscape for charities in the UK and Republic of Ireland is currently changing– there is already a new regulator in Northern Ireland and there will shortly also be one in the Republic of Ireland; in time, there may also be changes to the regime in the Isle of Man and the Channel Islands. By having a mechanism (SORP making body and SORP Committee) to allow these other jurisdictions to input and contribute to the development of the accounting rules, there is a greater chance of developing a set of rules that is suited both to the needs of the organisations concerned and those who will be preparing the accounts of charities in these newly regulated jurisdictions. This would be expected to result in high quality, relevant financial reporting going forward and reduce the risk of differing requirements and expectations (of particular interest for those in multiple jurisdictions).

4.3 Timeframe

Within the consultation document, the ASB states that it is planning a 'change' date for financial years starting on or after 1 January 2012. However, it has already been recognised in the course of recent consultation events that this is an overly ambitious timetable for change, taking into account the necessary steps to move from the current position to an anticipated future point.

For example, if the ASB's favoured option for a PBE standard is taken forward, there will still be the need for supplementary guidance for the charity sector (whether this is prepared on a conceptual basis or whether it outlines where different accounting is required for public benefit entities). Assuming this would utilise the existing SORP mechanism, the likely timeframe might look as the diagram below shows.



A more realistic timeframe for future development of a PBE standard indicates an implementation date of early 2013. If the timescale slips further beyond this date, there will be a strong argument in favour of updating the current Charities SORP in order to better meet the needs of smaller charities, a key theme emerging from the recent research undertaken by the SORP making body and the SORP Committee.

5 Closing comments

In summary, we have outlined here our comments on the proposals in relation to public benefit entities, focusing particularly on how these would be likely to impact on the charity sector and therefore the real need that we perceive to actively consider the user of accounting standards and supplementary guidance as well as the user of charity accounts. We consider there to be a significant need to consider the large proportion of non-accountancy professionals who are involved with the charity sector and how any such changes might impact on the sector as a whole. In addition, we would again, stress the need to avoid any changes that may be perceived as adding complexity to the current arrangements for preparers of charity accounts or making the accounts themselves more difficult to comprehend. Instead, we advocate changes that bring simplification for the sector and a positive response from users of the accounts. To that end, we would welcome further opportunity to discuss our views with the ASB, particularly as part of the joint SORP-making body.