

Introduction to SORP 2005

The Statement of Recommended Practice: Reporting and Accounting (SORP) is updated on a regular basis and a new version was published in March 2005. Charities have to implement this for accounting periods commencing after 1 April 2005. This revised version is available from <http://www.charitycommission.gov.uk>

Confirmation of fundamentals

The underlying principles of charity accounting are unchanged – this revised SORP is not overturning the fundamental tenets of charity accounting as set out in SORP 2000. It updates the SORP for new developments and also deals with some issues raised in the Strategy Unit report and the CFDG report *Inputs Matter*.

One of the principles it reinforces is that charity reporting should be activity-based. The revised SORP is more consistent in recommending that charities should describe the costs of their activities, and how the funding links to those activities. This should tie in with the trustees' annual report, which describes the activities of the charity in narrative.

The overall theme of this SORP is improved accountability – and so this is consistent with the Standard Information Return (see website www.charitycommission.gov.uk/enhancingcharities/sirintro.asp) and the Strategy Unit report.

Trustees' annual report

The narrative section is more structured, with five sections and clearer requirements. The narrative report is an opportunity for charities to explain their aims and their work – to their supporters and the public generally. A recent report by the Charity Commission 'RS8 Transparency and Accountability' reveals that many charities do not report adequately in line with the current SORP. Charities will now be asked to set out clearly what they are trying to do, and provide information on their performance.

One of the issues raised in the CFDG report was that of valuing volunteers. The revised SORP does not go as far as including the value of volunteer time in the statement of financial activities, but it does recommend that the trustees' annual report should give full information so that readers can understand the role and contribution of volunteers. This could include an estimate of the hours, and an indicative value of that time.

Trustees' annual report

- **Structure, governance and management**
 - Nature of governing document
 - How trustees are recruited and appointed
 - Policies and procedures for induction and training of trustees
 - Organisational structure and how decisions are made
 - Connections to a wider network
 - Related parties
- **Objectives and activities**
 - Objects of the charity
 - Charity's aims
 - Objectives for the year
 - Charity's strategies
 - Significant activities
 - Volunteer help
- **Achievements and performance**
 - Performance achieved against objectives set
 - Fundraising performance
 - Investment performance
 - Factors affecting performance
- **Financial review**
 - Reserves policy
 - Principal funding sources, and how expenditure has supported key objectives
 - Any funds in deficit
 - Investment policy and ethical policies if relevant
- **Plans for future periods**
 - Key objectives for the future

Statement of financial activities

One of the problems of implementation of SORP 2000 was that it was still difficult to interpret, and that users found it difficult to know which income and expense categories to use. In addition, charity accounts were sufficiently transparent and it was difficult to see how costs had been allocated to different cost categories. The revised SORP is more consistent in its approach, with a better explanation of how charities should focus on the activities and attribute costs to those, matching to income received.

Main changes in the statement of financial activities (SoFA)

For both income and expenditure headings, charities are encouraged to insert additional sub-headings and use more specific descriptions so that these relate to their activities. Headings only have to be used where there is an entry to be made.

Incoming resources

- 'Donations, legacies and similar income' – removed
- New heading of 'voluntary income' – for donations
- 'Activities for generating funds' – clarity that this heading to be used for trading, fundraising events etc
- 'Incoming resources from charitable activities' – to be used for fees and grants provided to charity to provide services

Resources expended

- Costs of generating voluntary income – the fundraising costs or raising the income shown under voluntary income
- Fundraising costs for events, trading etc should be shown to match to income heading of 'activities to generate funds'
- 'Charitable activities' is retained, but charities should add sub-headings to describe the activities
- Grants payable no longer have to be shown on the face of the SoFA, but should be included within the activity cost, with analysis in notes
- Support costs no longer to be shown on the face of the SoFA, but included within the activity cost.
- Notes to the accounts have to show the main components of support costs.
- 'Governance costs' is introduced as a new heading, with 'management and administration costs' removed. Greater clarity on what should be included.
- Accounting policies need to state the methods used to allocate costs.

Where a charity is receiving income under contracts, or grants where there is a very specific service requirement, it needs to consider whether it can take all that income into the statement of financial activities, or whether some income should be deferred. Deferral will be necessary if the charity has not completely delivered all the services required by the funding – thus the recognition of income should be matched to 'performance' under the contract or grant.

Allocating costs

Charities will need to develop a structure for allocating costs that will ensure that fundraising and governance contain a fair proportion of the staff costs and general overheads. In addition, charities

will need to identify the support costs and then show how these have been apportioned to charitable activities. The notes to the accounts should provide details of the total support costs, giving an analysis of the main components. Where support costs are material, the notes should explain how support costs have been apportioned to the charitable activities. This may be achieved either by providing a breakdown in the notes to the accounts, or by providing the method and percentage basis for the apportionments.

Balance sheet

Very few changes to the balance sheet presentation, as one might expect. The main change here is that a new definition of 'heritage assets' has been introduced to bring the SORP into line with current practice elsewhere. Heritage assets are those assets held for preservation or conservation purposes. Hence, assets given to charities with restrictive covenants which prevent the charity from disposing of the asset (known as inalienable assets) do not now fall within this definition. In addition, historic buildings occupied by charities as offices, schools, places of worship, but not held to fulfil their preservation objects, do not fall within the definition. In practice, this means that these assets have to be shown under the fixed assets of the charity and depreciated. Newly acquired heritage assets should also be shown in the balance sheet and depreciated in a separate category. Heritage assets previously acquired where it is difficult or costly to obtain a value can still be omitted from the balance sheet.