



# Charities SORP Accounting Update



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# Charities SORP Accounting Update



# Our panel



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Audit Senior Manager



# Housekeeping



This webinar is being recorded and will be sent to you later today.

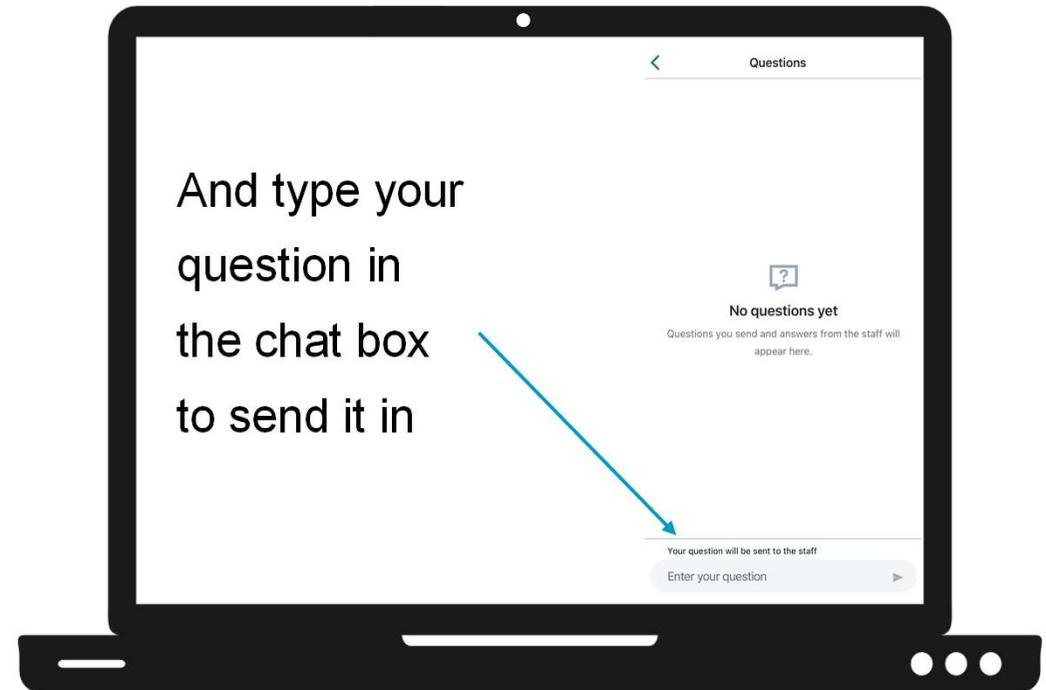
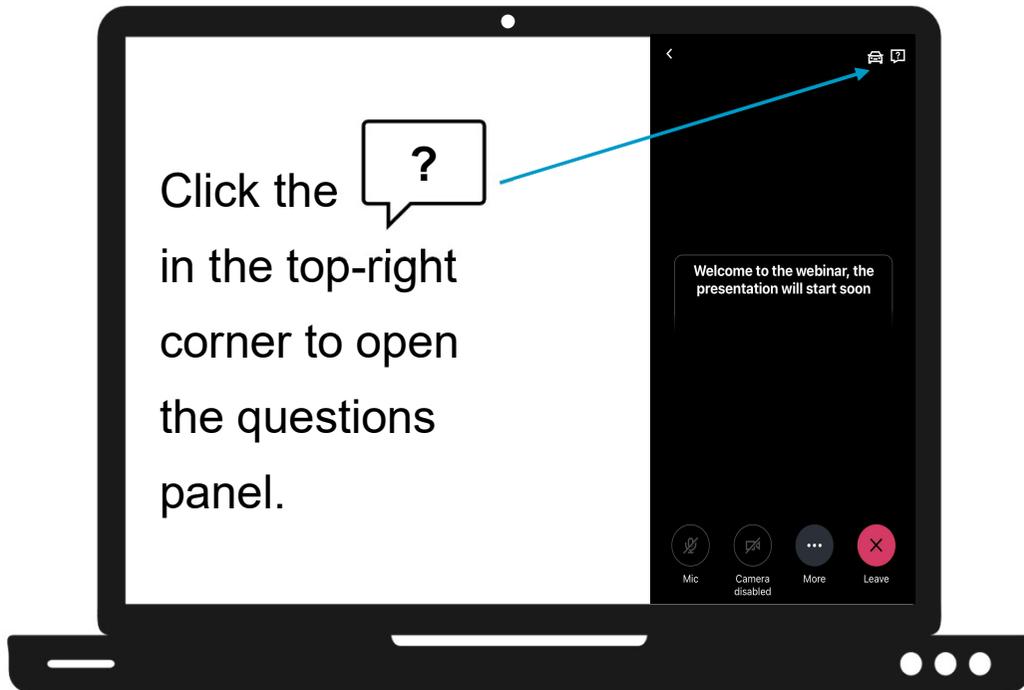


We'll be asking you to take part in some polls throughout the presentations.



There will be a pop-up survey at the end of the webinar.

# How to ask a question





## We'll be covering...

-  Trustees' Annual Report
-  Income recognition
-  Lease accounting
-  Provisions, contingent liabilities and contingent assets and funding commitments
-  Groups and mergers

# Poll



# Trustees Annual Report

# SORP new tier system – on or after 1 January 2026

The new SORP sets out a new tier system with the disclosure requirements increasing depending on the size of your charity:



Tier 1 - charities with gross income up to £500,000



Tier 2 - charities with gross income from £500,000 up to £15,000,000



Tier 3 - charities with gross income from £15,000,000



# DCMS Changes – Apply from 1 October 2026 AT THE EARLIEST

Requirement	Current threshold	New threshold from 1 October 2026
Accounts must be independently examined	Income over £25,000	Income over £40,000
Examination must be by a professionally qualified Independent Examiner	Income over £250,000	Income over £500,000
Non-company charities can choose to produce receipts and payments accounts	Income over £250,000	Income below £500,000
Accounts must be audited	Income over £1m or Assets over £3.26m	Income over £1.5m or Gross assets over £5m
Group accounts must be prepared and audited	Aggregate income of group £1m	Aggregate income of group £1.5m

# Poll

# What is gross income?

Depends on jurisdiction and type of accounts:

**Charities Act 2011:** Gross recorded income from all sources

**Charity Commission:** Total income in SoFA, less any endowment received, plus any amount transferred to income from endowment funds

**OSCR:** All income from restricted and unrestricted funds, excluding donated asset receipts in endowment funds



# Purpose of the Trustees' Annual Report



Who are the users of the report?



What are the information needs of users of the report?



Trustees are ultimately responsible



The report should provide a **fair, balanced and understandable** review.



Should tell **your story**

# SORP Language

**‘MUST’ –  
FRS102**



**‘SHOULD’ –  
Good practice**



**‘MAY’ -  
Discretion**



## Objectives and activities



**MUST** - Tier 1 **Volunteers** – Explain input through the scale and nature of activities undertaken.

**MUST** - Tier 1 charities - the review of activities should be **consistent with the analysis of expenditure** within the notes to the accounts.

**MUST** – Tier 2 & 3 - provide the user of the financial statements with a more detailed understanding of the **short and long term aims and objectives**.

Reminder that report must answer:

- Aims and objectives for the year **and how performed against these?**
- Strategies for achieving these?
- Significant activities undertaken and how these contribute to achieving aims and objectives?
- Changes/differences are you seeking to make?
- **Material grant making policy must explain how individuals and institutions are selected**

# Achievements and performance



All charities **MUST** explain how well they carried out activities and extent achieved objectives

**Explain the charity's impact and consider the effect of its activities on beneficiaries and society as a whole in the longer term.**

# Achievements and performance



## IMPACT REPORTING

**SHOULD** - Tier 1 **Infographics, statistics and testimonials are encouraged**

**SHOULD** - Tier 2 & 3 **Impact stories on society or individual level**

**Outputs achieved should be explained and compared with any set targets**

### MIGHT LOOK LIKE:

- Summary of performance measures used (**including environmental or social issues**)
- Information on achievement of objectives by activities, outputs, outcomes and impact contributions
- Both positive and negative factors covered and implications on future plans
- Employee, service user, beneficiary or funder relationships and wider community

# Impact Reporting

Describe your journey and illustrate the evidence that shows you are making the correct decisions

## **Now required for charities in Tier 2 and 3**

- You need to describe not only what you do, but also the impact it creates. This will be a journey that develops over time
- How do you assess the effects and influence of your activities on beneficiaries and on wider society, both now and in the future?
- Maintain consistent language throughout the report and financial statements
- It's about more than achievements, and more than simply spending money



# Financial Review



## New **MUST** disclosures - Tier 1



Ensure the information aligns with the figures reported in the accounts



Identify and explain any material designated funds or committed amounts, including the expected timing of the related expenditure



The reserves balance should match the accounts or, a reconciliation must be provided



Where reserves are negative or nil, provide an explanation of how the charity remains a going concern



Any material uncertainties regarding the charity's ability to continue as a going concern must also be disclosed



You must compare the reserves held against the charity's reserves policy and explain actions being taken to bring the two into alignment

(Was previously a should for large charities)

# What are free reserves ?

**Reserves definition in Glossary:** Funds freely available to spend. Exclude restricted, permanent and expendable endowment funds.

Not freely available:

Fixed assets

Investments held for charitable purposes

Committed designated funds

Unprovided commitments



# Do you need a reserves reconciliation?

You must explain any material adjustments, designated funds, and committed expenditure as part of the reserves policy.

Many charities now use target ranges rather than a single reserves figure, and increasingly analyse free reserves into sub-categories or specific pots.

Unrestricted funds at the balance sheet date	X
Less: Designated funds	
- Fixed assets used by charity	(X)
- Investments used for charity purposes	(X)
- Other designated and committed spending	(X)
- Other adjustments explained	(X)
Free reserves	X

# Financial Review



## New **MUST** disclosures – Tier 2 & 3

Must explain the charity's principal income sources and how those funds have been used (previously a 'should' requirement).

The disclosure of principal risks must now also include environmental and cyber risks.

The investment policy must set out the extent to which social, environmental and ethical considerations influence investment decisions.



## New **Should** disclosures – Tier 2 & 3

Any material legacy income recognised in debtors and indicate the expected timing of receipt to help explain the availability of funds.

# Plans for the Future



## New **MUST** and **MAY** disclosures – Tier 1

Must provide summary of future plans

May be helpful to include commentary on reserves and going concern where relevant

## **MUST** – Tiers 2 and 3

Report must provide a summary of the charity's plans for the future, including its aims, objectives and details of any activities planned to achieve them and should explain the Trustee's perspective of the future direction of the charity.

It should explain where relevant, how experienced, gained or lessons learned from past or current activities have influenced future plans, decisions about allocating reserves to their best effect.

# Sustainability



Tier 1 & 2

**May** describe how the charity is responding to and managing these matters, and providing such disclosure is encouraged.



Tier 3

**Must** provide a summary of how the charity is responding to and managing environmental, governance and social matters.



## Next Steps

Don't panic—the process will develop and your report will evolve over time. Already doing this just not in the prescribed sections of new SORP



Begin the planning process now—don't wait for the next reporting cycle



Review your current Trustees' Annual Report and identify any missing information.



Determine whether you already have this information or whether it needs to be created or collated.



Assess how you currently track whether you are doing the right things.



Consider whether it is more effective to refine your existing approach



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# Lease accounting

# Overview

Charity SORP 2026 mandates most leases be recognised on balance sheet.



New category of right-of-use assets within tangible fixed assets



Lease liabilities to be calculated



Enhanced disclosure requirements



No change for lessors



## Right of use asset value

$$\begin{aligned} & \text{Lease liability} + \text{Initial direct costs} + \text{Costs to remove or restore} + \text{Payments made at or before commencement} - \text{Lease incentives received} + \text{Value of social donation} \\ & = \text{Right of use asset value} \end{aligned}$$

# Lease liability



## Lease liability

- Lease payments for each month / quarter
- Must exclude non lease elements such as cleaning, catering or office related services
- Liability should be calculated for the lease term
- Discounted at appropriate rate

## Lease term

- Begins at the commencement date
- Includes any rent-free periods
- Is the aggregate of:
  - non-cancellable period; and
  - periods covered by option to extend if **lessee** is reasonably certain to exercise that option; and
  - periods covered by the option to terminate the lease if the **lessee** is reasonably certain not to exercise that option.

# Lease term considerations



## Non-cancellable period of a lease

- When you as the charity lessee do not have an option to terminate to the lease

## The period for which the contract is enforceable

- A lease is no longer enforceable when the lessee and the lessor each has the right to terminate the lease without permission from the other party with no more than an insignificant penalty.

## Break clauses

- Area of judgement
- If lessee is reasonably certain to extend beyond the minimum notice period, then include full term of the lease.
- If expect to cancel, then only use period up to break clause.

# Peppercorn and below market leases



## Value of social donation

- Consider information from lessor about the discount given
- Consider information available for value of similar leases
- Donation value is the fair value difference between the market value of the ROU asset and the actual lease liability

- Peppercorn leases are non-exchange transactions – recognise as a donated right of use asset

DR Right of Use Asset

CR Donations

- Below market leases have a lease and a donation component

DR Right of Use Asset

CR Lease liability

CR Donations

# Discount rate

This is set at commencement and is not changed during lease term to reflect changes to interest rates.

Discount rate will be:

- Interest rate implicit in the lease

If this is not available then the charity can choose from:

- Obtainable borrowing rate OR
- Incremental borrowing rate

For public benefit entities only, if neither of the above apply, must then use:

- Rate of interest earned on deposits held with financial institutions





## Exemption for low value assets

Based on value of the ASSET not the lease liability.

An asset is considered low value if:

- Its value when new is low
- The lessee can benefit from the asset on its own or together with other readily available resources
- The asset is not highly dependent on, or interrelated with, other assets

Impact:

- Continue to treat as operating leases
- Expense lease payments directly to SOFA
- Must disclose exemption being taken
- Must disclose operating lease obligations falling due

## Exemption for short term leases



- Any lease with term < 12 months at lease commencement date
- Any lease with < 12 months remaining on transition date
- Must not contain any purchase option
- Must be applied to an entire class of leased assets with similar character
- Continue to treat as operating leases
- Expense lease payments directly to SOFA
- Must disclose exemption being taken
- Must disclose operating lease obligations falling due within the next 12 months

# Revised Charity SORP and leases - example

Example					
Asset description	Start date	End date	Lease term (years)	Paid in year	Annual rent commitment
Land and Buildings	01/08/2019	31/07/2044	25	93,439	93,061
Vehicle Hire	01/06/2025	31/05/2026	1	6,288	6,288
Vehicle Hire	01/06/2025	31/05/2028	3	6,288	6,288
Photocopiers and Printers	01/04/2025	31/03/2026	1	551	551
Photocopiers and Printers	01/01/2024	31/12/2026	2	151	151
Audio Equipment	01/08/2020	31/07/2027	7	60,000	60,000
Treatment					
Asset description	Start date	End date	Low value?	Short term?	Treatment
Land and Buildings	01/08/2019	31/07/2044	×	×	Recognise a right of use asset and lease liability on SOFA
Vehicle Hire	01/06/2025	31/05/2026	×	✓	Expense to SOFA
Vehicle Hire	01/06/2025	31/05/2028	×	×	Recognise a right of use asset and lease liability on SOFA
Photocopiers and Printers	01/04/2025	31/03/2026	✓	✓	Expense to SOFA
Photocopiers and Printers	01/01/2024	31/12/2026	✓	×	Expense to SOFA
Audio Equipment	01/08/2020	31/07/2027	×	×	Recognise a right of use asset and lease liability on SOFA

# Transition

- Do not need to restate prior year balance sheet
- Instead, full impact on opening fund balances for the cumulative effect when bringing the Right of Use assets and the Lease Liabilities on balance sheet.
- Accounting policies need to state what exemptions are taken and judgements and assumptions that have been made.



## Action required



Compile a full list of all of the charity's operating leases



Collate copies of all of your lease agreements



What break clauses / extension options are there and are these likely to be taken?



Can any leases be fairly classified as low value / short term under FRS102?



What discount rate will be used by the charity? Obtainable or incremental borrowing rate? Or rate of interest obtainable on deposits if no borrowing?



Does your finance team understand the adjustments that will be required?



What will be the impact on any loan covenants of bringing the operating leases onto the balance sheet?

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Income recognition

# Income recognition - overview

**Income from exchange transactions**

5 step model for income

**Income from non-exchange transactions**

When received / receivable  
**or**  
when performance conditions are met  
**and**  
when can be reliably measured

# Exchange vs Non-exchange transactions

Exchange transactions under contracts	Non-exchange transactions
Must have offer and acceptance	Gift / donation freely given by the donor / funder
Must have consideration (unless structured as a deed)	May state to be used for a specific purpose ("restricted")
Subject to contract law	Subject to trust law
Remedy for failure – damages for breach of contract	Remedy for failure – repayment / claw back

# Income from exchange transactions



Exchange transactions involve goods or services provided under a contract or enforceable service level agreement



Must apply 5 step model for income from exchange transactions



Does not change the total value of income recognised over the period



May change the timing of when this income is recognised

## Example income streams

Course fees in exchange for delivering a training course



Income in respect of provision of serviced residential accommodation to beneficiaries



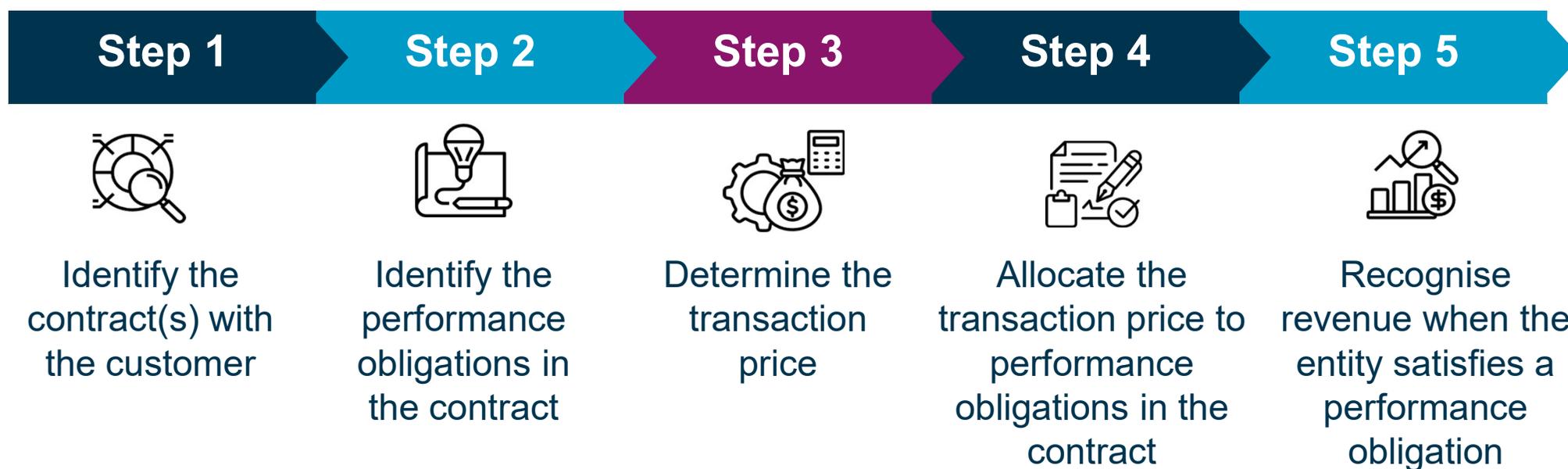
Sale of bought in goods or items made by beneficiaries



Corporate sponsorship



# 5 step model for income from exchange transactions



## 5 step model - example



Museum annual membership subscription benefits:

- Half price entry fees for the year
- Quarterly newsletter

- Spread expected discounts over the year
- Recognise quarterly

# Non-exchange transactions - donations

The donor or grant maker does not directly receive equal value in exchange: eg donations and certain grants



## No conditions

If no specified future performance related conditions, recognise when received or receivable. Restriction on use does not prevent recognition



## Conditions

If future performance obligations, recognise only when these are satisfied. Performance obligation may impact the timing of recognition but does not make it an exchange transaction



## Measurement

Only recognise when income can be measured reliably



## Non-exchange transactions - legacies

No substantial change to recognition criteria – when probable and can be measured reliably

Restriction on use does not prevent recognition

Financial review should disclose material amounts accrued but not received

Disclose contingent asset for amounts not yet recognised



### **Probable**

When probate has been granted

Sufficient assets less liabilities to pay legacy

Conditions are either within control of the charity or have been met



### **Measurement**

Only recognise when income can be measured reliably

Consider whether post year end evidence is an adjusting event

If significant number of legacies - may apply estimate to portfolio



## Action required



Document the split of charity income between exchange and non-exchange transactions.



Do you have any income contracts that include multiple goods / services provided by the charity? If so, these will need to be unbundled and if you have different contract terms for different services provided, you will need to ensure that the right income recognition policy is applied to each service element.



Does your finance team understand the five-step model that needs to be applied for exchange transactions?



Non-exchange transactions – consider separate performance obligations and attribute consideration to when these are met.



Additional disclosures re accrued legacies in TAR.



Update accounting policies and key judgements



# Provisions, contingent liabilities and contingent assets and funding commitments

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## New module 10A

Area	SORP 2019	SORP 2026
Dedicated provisions module	✗ No	✓ Yes – <b>Module 10A</b>
Funding commitments	✗ Limited guidance	✓ Explicit charity-specific guidance
Alignment with FRS 102 (2024 update)	✗ Based on earlier version	✓ Fully aligned and updated
Disclosure requirements	General, FRS 102-based	More structured, more detailed
Clarity and examples	Limited	Significantly improved

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# Groups and mergers

# Groups and mergers

## Groups

Requirement for consolidated accounts in module 23 still then references to Appendix III which, as it stands, is £1million threshold for consolidated accounts.

The groups module is effectively applicable for all tiers.

## Mergers

Important restriction:

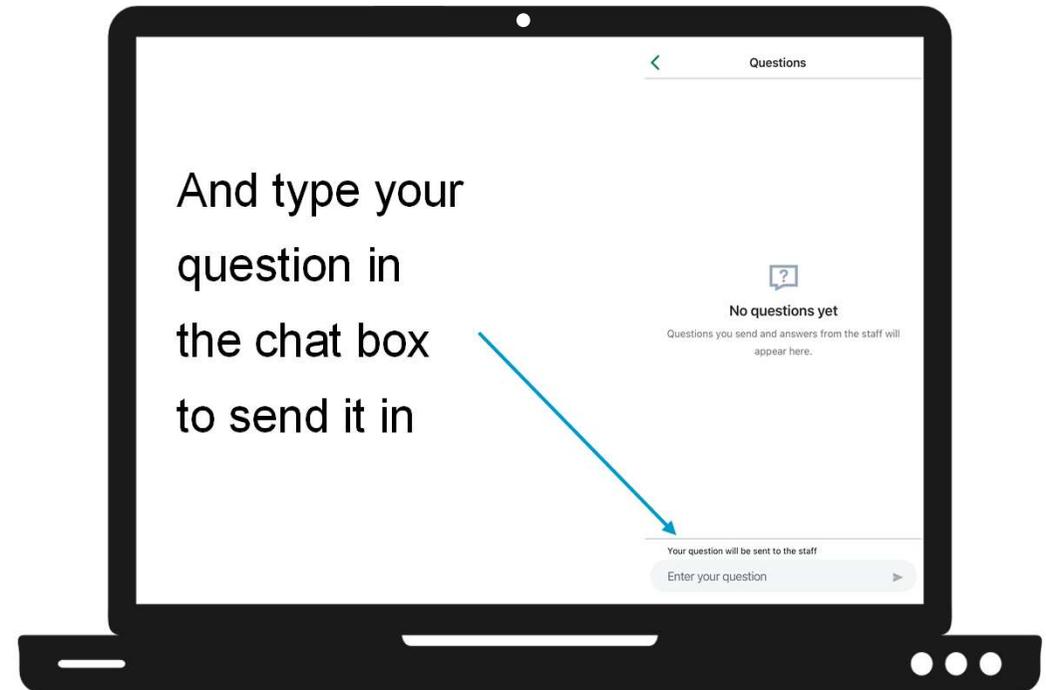
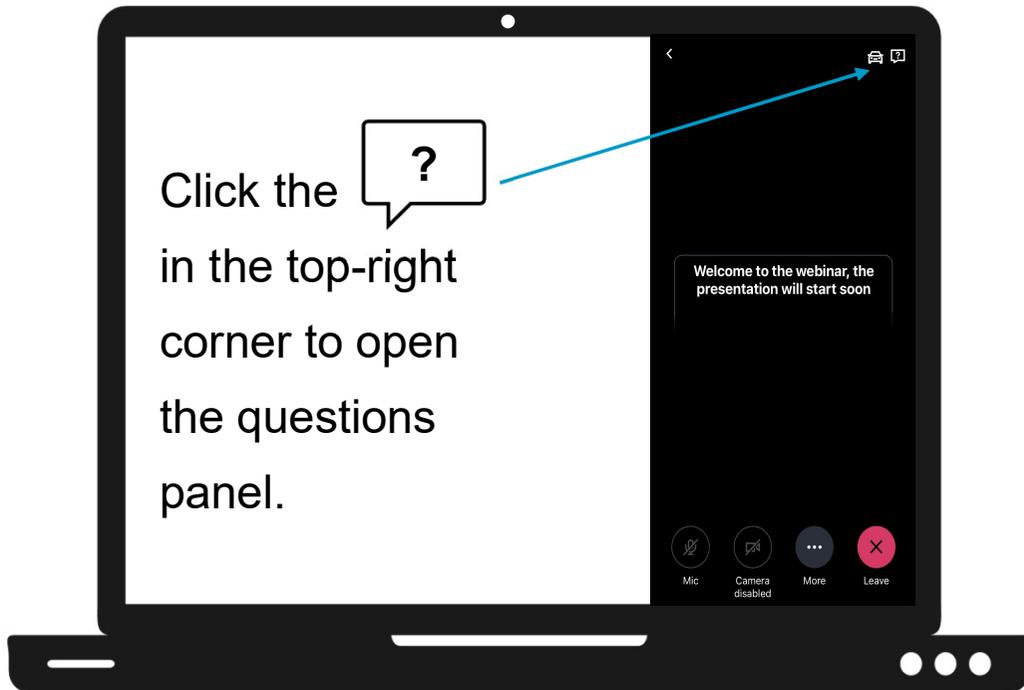
UK charitable companies that enter into business combinations with a third party can no longer apply merger accounting, due to changes in UK company law.

Unincorporated charities, CIOs, and non-UK companies may still apply merger accounting if other criteria are met.



# Poll

# How to ask a question





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