VODG Session
Charities SORP 2026
In-depth: Income and Leases

29 January 2026 10.00 – 11.30

Now, for tomorrow

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Webinar overview

Introduction to SORP 2026 & MHA Resources

SORP 2026 – Income recognition

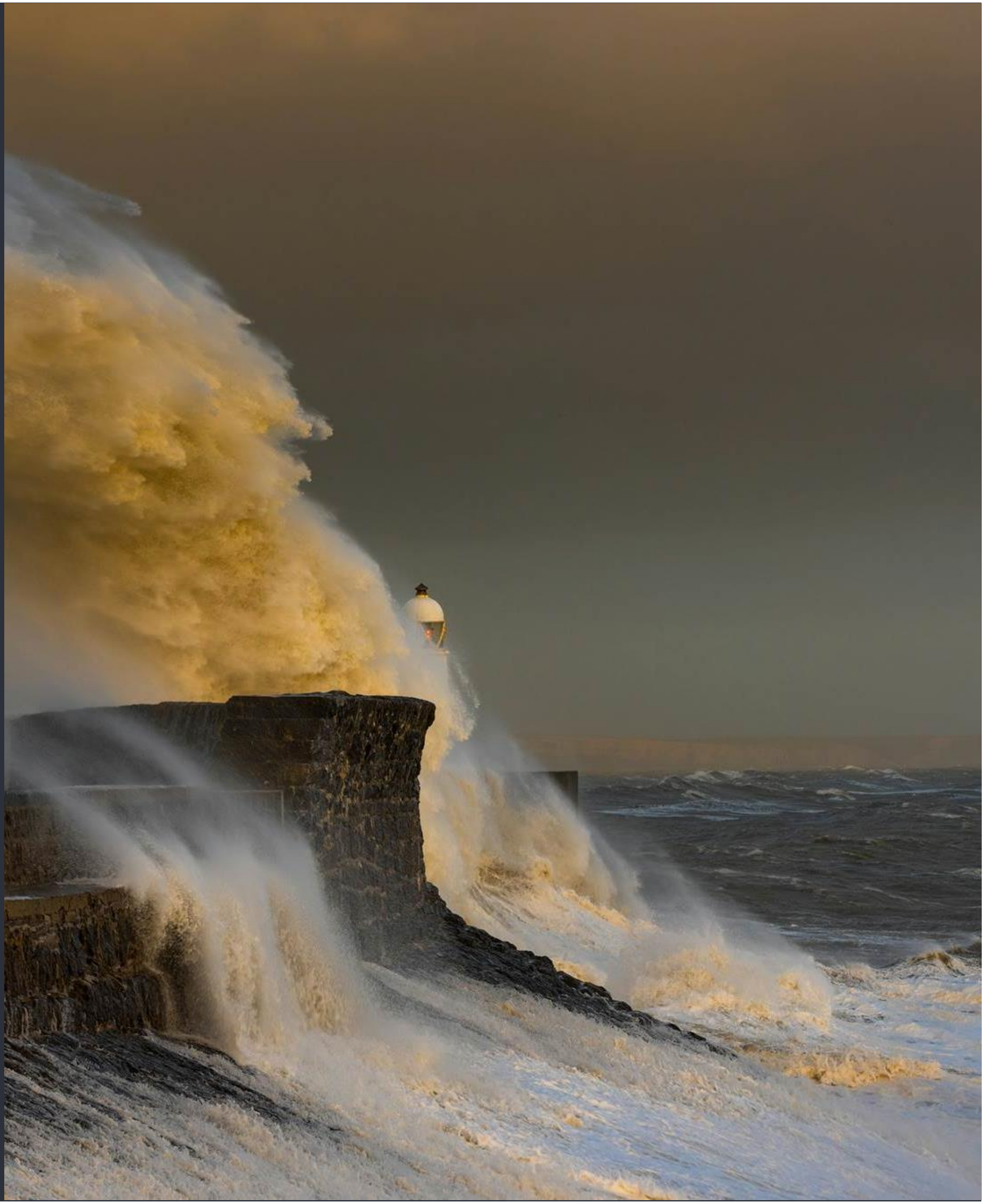
- Understanding the New Requirements
- Comparison with Current Practice
- Worked Examples and Real-Life Scenarios
- Implementation and First-Day Transition

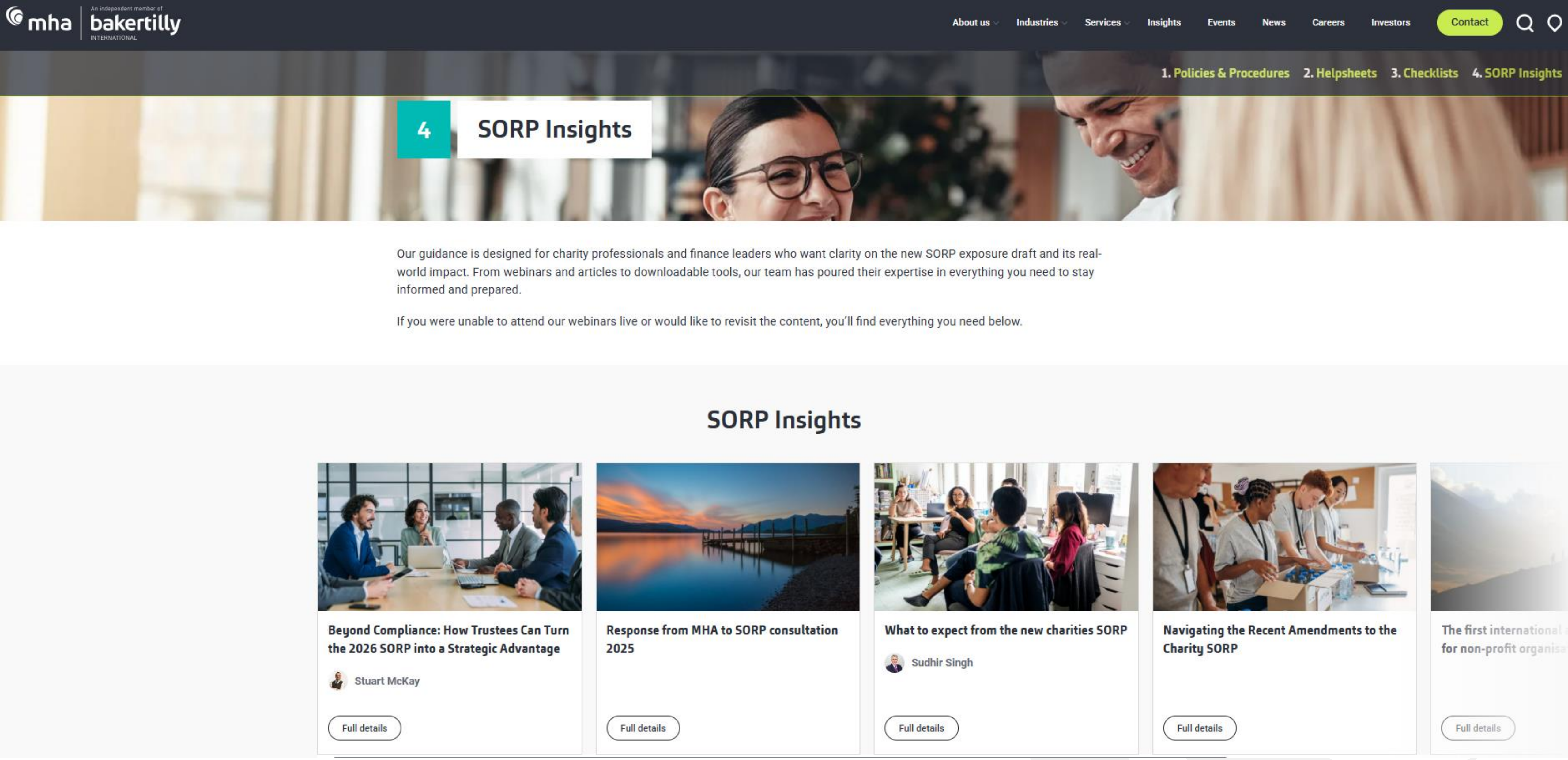
Q&A session

SORP 2026 – Accounting for leases

- Understanding the New Requirements
- Worked Examples and Real-Life Scenarios
- Implementation and First-Day Transition

Q&A session

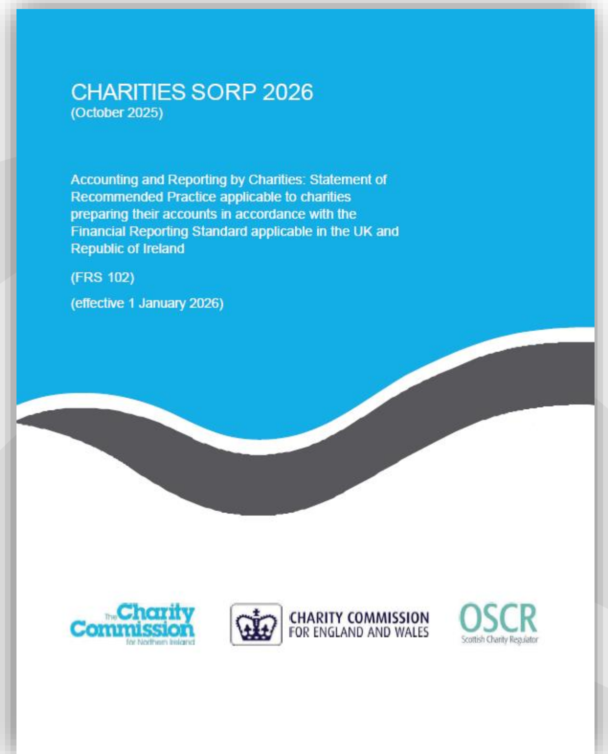




MHA Trustee Hub - https://www.mha.co.uk/spotlight-on/charity-trustee-hub

Recap: Main Sections & Significant Changes

https://www.charitysorp.org/



Module 1 – Trustees Annual Report

- Financial review
- Impact Reporting
- Sustainability Reporting
- Volunteers
- Reserves
- Going concern
- Legacies

Significant Changes to financial statements:

- Module 5 – Recognition of **Income** – 5 step model (only affects exchange transactions)*
- Module 7 – Recognition of **expenses**
- Module 10 - **Leasing** – no distinction between operating and finance leases (flowchart and 2 information sheets)
- Module 14 – Statement of **cashflows** (Tier 1 & 2 exempt)
- Module 18 – **Heritage Assets**
- Module 21 – Accounting for **social investments**

The Tiering System

Company charities – must prepare accruals accounts regardless of size.

Tier 1	All charities applying accruals accounts and with a gross income of **not more than £500,000** (€500,000).
Tier 2	All charities with a gross income falling above the tier 1 threshold and with a gross income of **not more than £15 million** (€15 million*).
Tier 3	All charities with a gross income falling above the tier 2 threshold. (**Above £15m**)

Non-company charities – can opt to produce receipts and payments accounts as long as gross income does not exceed £500,000. (Affects over 5,100 charities)* (per the DCMS announcement)

Tiering only affects these modules of the SORP

There are 29 modules of the SORP - Tiering (where different requirements apply) <u>**only**</u> affect the following modules:

1. **Module 1** – Trustees' Annual Report
2. **Module 4** – Statement of Financial Activities
3. **Module 8** – Allocating costs by activity in the statement of financial activities
4. **Module 9** – Disclosure of trustee and staff remuneration, related party and other transactions
5. **Module 14** – Statement of cash flows

For all other modules in the SORP, **tiering does not apply**, and those modules will be applied in full to all charities, where applicable.

SORP
Financial Statement Changes

- Module 5 – **Recognition of income**

Income

Exchange

Non-Exchange

Income from exchange transactions is received by the charity for goods or services supplied under contract.

The income the charity receives **is approximately equal** in value to the goods or services supplied by the charity to the purchaser

The charity receives value from the donor **without** providing equal value in exchange.

Exchange vs Non-Exchange

Exchange

Exchange transactions:

1. Contracts
2. Membership fees – purchasing right to services or benefits (e.g rights of accessing premises)
3. Royalties
4. Charity shop income
5. Entrance fees
6. Provision of help line on behalf of a 3rd party
7. Care home fees
8. Spot purchases by Government departments

Non-Exchange

Non-Exchange transactions:

1. Donations
2. Grants (including performance related grants)
3. Legacies
4. Gifts of non-cash items – i.e donated goods
5. Membership fees – where substance is a donation

SORP 2019
Current practice

Exchange

Non-Exchange

Income must only be recognised in the accounts of a charity when all of the following criteria are met:

- **Entitlement** – control over the rights or other access to the economic benefit has passed to the charity.
- **Probable** – it is more likely than not that the economic benefits associated with the transaction or gift will flow to the charity.
- **Measurement** – the monetary value or amount of the income can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

SORP 2026
New practice

Income

Exchange | Non-Exchange

Five step model

1. Identify the **presence of a contract** with a third party
2. Identify the **performance obligations** in the contract
3. Determine the **transaction price**
4. **Allocate** the transaction **price** to the **performance** obligations in the contract
5. Recognise income when or as **the charity satisfies** a performance obligation

Non-Exchange:

1. Certainty (probable)
2. Measurement (reliable)

Spot the missing criteria

Entitlement has disappeared!

Exchange

The NEW 5 step model

The new five step model set out in Module 5 is a significant change with a focus on promises, obligations, price and transfer of control.

Central London Property Trust Ltd v High Trees House Ltd [1947]
promissory estoppel

The 5 Steps

STEP 1	A contract exists – 5 criteria have to be satisfied (para 5.14). A contract need not be a written one (para 5.15)
STEP 2	Identify the promised goods and/ or services that comprise the performance obligations (5.20) and whether distinct or a series (para 5.21)
STEP 3	Determine the price for the exchange (5.26) and identify any financing (para 5.29)
STEP 4	Allocate the price across the performance obligations (5.31)
STEP 5	Recognise income on performance as control passes (para 5.42) either over time (para 5.43) or at a point time (para 5.45) as appropriate

STEP 1

Identify the presence of a contract

The new income recognition model is only applied when the following five criteria, which are broadly based on UK contract law, are met:

<table>
<tr><th>Per SORP (2026)</th><th>Per UK contract law</th></tr>
<tr><td rowspan="2">i. The parties to the contract have approved the contract and are committed to performing their respective obligations.</td><td>Offer - A clear, definite promise to be bound on specific terms, made with the intention that it will become binding upon acceptance.</td></tr>
<tr><td>Acceptance - An unqualified assent to the terms of the offer, communicated in the manner prescribed or, if none is prescribed, in a reasonable manner.</td></tr>
<tr><td>ii. The Charity can identify each party's right regarding the goods or services to be transferred can be identified.</td><td rowspan="2">Certainty and Completeness of Terms - The contractual terms must be sufficiently certain and complete to enable the courts to identify the parties' obligations and enforce them.</td></tr>
<tr><td>iii. The Charity can identify the payment terms for the goods and services to be transferred can be identified.</td></tr>
<tr><td>iv. The contract has commercial substance.</td><td>Intention to Create Legal Relations - The parties must intend their agreement to have legal consequences. This is presumed in commercial contexts and rebuttable in domestic or social arrangements.</td></tr>
<tr><td>v. It is probable that the third party will have the ability and intention to pay the consideration to which the Charity will be entitled when it is due.</td><td>Consideration - Something of value given in exchange for the promise (which may be nominal), moving from the promisee. Past consideration is generally insufficient.</td></tr>
</table>

STEP 2

Identify the performance obligations in the contract

"the charity must identify as a performance obligation each promise to transfer to the customer either*:*

a. <u>A distinct</u> good or service (or a distinct bundle of goods or services): or

b. <u>A series of distinct</u> goods or services that are substantially the same and have the same pattern of transfer to the third party."

Distinct

=

customer can benefit from the good or service on its own

\+

entity's promise to transfer good or service is separate from other promises in the contract (if any)

A series of distinct goods or services has the **same pattern** of transfer to the third party if both of the following criteria are met:

- each distinct good or service in the series that the charity promises to transfer to the third party would meet the criteria of a **performance obligation satisfied over time**
- the same method would be used to measure the charity's progress towards complete satisfaction of the performance obligation to transfer each distinct good or service in the series to the third party

STEP 3

Determine the transaction price

Per SORP (2026)

5.32. The **stand-alone selling price** is the price applicable at the inception of the contract for each performance obligation in the contract. It is the **price at which the charity would sell a good or service promised in a contract separately to a third party.**

5.33. Where the contract price is not simply calculated by applying these stand-alone prices to the promised items then, the **allocation made is in proportion to those stand-alone selling prices.**

5.34. If there are **no observable standalone** prices, then these **must be estimated**. Refer to paragraph 5.40 for suitable estimation techniques. When estimating a standalone selling price, a charity must consider all information that is reasonably available to it, including market conditions, charity-specific factors, and information about the third party or class of third party.

5.35. **Discounts** are applied proportionately across all the performance obligations unless a discount applies to a particular obligation only or an alternative method gives a fairer presentation of the amount that the charity expects to be entitled to in exchange for satisfying each performance obligation in the contract.

5.36. **Suitable estimation methods include, but are not limited to**, the adjusted market assessment approach, the expected cost plus a margin approach or the residual approach. The residual approach is rarely appropriate but if neither the adjusted market assessment approach nor the expected cost plus a margin approach are practicable, the residual basis approach can be considered. A charity must apply estimation methods consistently in similar circumstances.

5.37. **The adjusted market assessment approach** – a charity could evaluate the market in which it sells goods or services and estimate the price that a third party in that market would be willing to pay for those goods or services.
5.38. **Expected cost plus a margin approach** – a charity could forecast its expected costs of transferring the good or service promised to a third party and then add an appropriate margin for that good or service.
5.39. **Residual approach** – only if the stand-alone selling price of a good or service is highly variable or uncertain, then a charity may estimate the selling price by reference to the total transaction price less the sum of the observable or estimated stand-alone selling prices or services promised in the contract.

5.40. A charity must allocate any **variable payment (consideration)** to all the performance obligations in the contract on a relative stand-alone selling price basis unless this basis does not depict the amount of consideration to which the charity expects to be entitled in exchange for satisfying each performance obligation in the contract. In that case, the charity must allocate the variable consideration using a method that reflects such an amount (for example, a variable payment may be allocated entirely to one performance obligation in the contract if the terms of that variable payment relate specifically to the charity’s efforts to satisfy that performance obligation).

5.41. **After contract inception**, the charity’s **estimate of the amount of consideration** to which it expects to be entitled in exchange for transferring goods or services **may change**. A change in estimate of the transaction price is allocated across the performance obligations in the contract on the same basis as at contract inception. Amounts allocated to a performance obligation that has been satisfied shall be recognised as income, or as a reduction of income, in the period in which the estimate of the transaction price changes.

STEP 4

Allocate the transaction price to the performance obligations in the contract

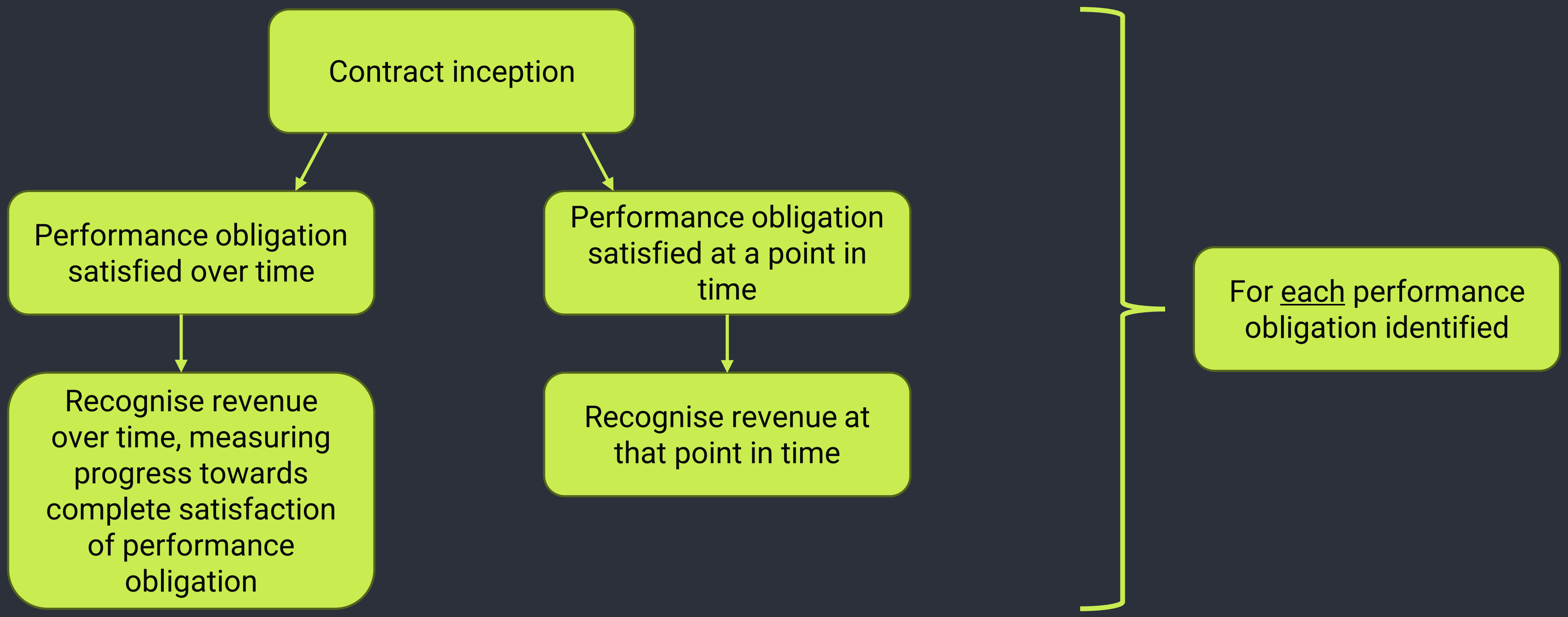
Performance obligation #1	=	£x
Performance obligation #2	=	£y
Performance obligation #3	=	£z
		Transaction price

- Allocate the transaction price to each performance obligation in the contract on a relative *stand-alone selling price* basis.
- The *stand-alone selling price* is the price at which an entity would sell a good or service promised in a contract separately to a customer.
- If a stand-alone selling price is not directly observable, a Charity shall estimate it. Consider all information that is reasonably available, including market conditions, entity-specific factors and information about the customer.
- Again, Charities must reassess these estimates at each reporting period; changes in estimate should be allocated to specific performance obligations within a given contract

- 5.37. The **adjusted market assessment approach** –evaluate the market and estimate the price that a third party in that market would be willing to pay for those goods or services.
- 5.38**. Expected cost plus a margin approach** –forecast its expected costs delivery and then add an appropriate margin for that good or service.
- 5.39. **Residual approach** – only if the stand-alone selling price of a good or service is highly variable or uncertain, then a charity may estimate the selling price by reference to the total transaction price less the sum of the observable or estimated stand-alone selling prices or services promised in the contract.

STEP 5

Recognise revenue when (or as) the Charity satisfies a performance obligation



Satisfaction arises when the promised good/service is transferred to the customer (i.e. when the customer has control of the good/service.

Contract balances at the reporting date should recognised on the Balance Sheet.

1. Contract with a third party

A Charity provides training courses, available to the public. The course fee is £5,000 for a 3-month course (with 12 sessions).

1. Upon sign up to the course – course materials are provided.
2. Included in the fee is access to network events held by industry experts (for which the Charity has an arrangement externally)
3. Final assessment to obtain certification for the completion of the course. (CPD certification).

Under SORP 2019:

- Income from the supply of services is recognised with the **delivery of the contracted service,** provided that: the stage of the completion, the costs incurred in delivering the service and the costs to complete the requirements of the contract can **all be measured reliably**.

A charity must **select a method** to measure the **stage of completion** of a service contract that provides the **most reliable estimate** of the right to receive payment for the work performed. Possible methods include:

- the proportion of costs incurred for work performed to date compared with the total estimated costs to completion; or
- surveys of the work performed; or
- completion of a physical proportion of the service contract work.

It may also be appropriate to recognise income based on the time spent in providing a service as a proportion of the total time to be spent to fulfil the contract when this provides the most reliable estimate of a charity's entitlement.

Recognition under SORP 2019:
This will be dependent on the Charity's method selected.
For example, if based on proportion of costs to measure stage of completion, then the Charity would recognise income based on the cost profile. So if 75% of the work has been completed, then 75% of income would be recognised.

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3. Final assessment to obtain certification for the completion of the course. (CPD certification).

SORP 2026

Refer to the 5 criteria of whether a **contract** is in place

STEP 1

- Online sign-up form for the course

Under SORP 2026, the following would need to considered:

- Identify the **promised** goods and/ or services that comprise the **performance obligations**
- Allocate **transaction price** to each
- Recognise income **as each obligation is satisfied**

The contract must be separated into its **performance obligations:**

STEP 2

1. Delivery of the **course materials** at contract inception
2. Delivery of **12 separate training sessions** in the 3-month period
3. Ongoing access to **networking events** throughout the 3-month period
4. **Final assessment plus CPD certification** upon completion

1. Contract with a third party

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1. Upon sign up to the course – course materials are provided.
2. Included in the fee is access to network events held by industry experts (for which the Charity has an arrangement externally)
3. Final assessment to obtain certification for the completion of the course. (CPD certification).

SORP 2026

These **distinct obligations have standalone selling prices as follows:**

Adjusted market assessment approach

Performance obligation	Basis of pricing	Standalone price	Selling price ratio	Allocation of £5,000 fee
Course material	Printed materials at cost to the Charity	£600	11%	£550
Training course	Based on internal staff time to run the session	£4,000	73%	3.650
Networking events	Purchase cost to Charity from third party	£300	5%	£250
Final assessment and CPD certification	Cost to the Charity for the examiner (certification cost is minimal)	£600	11%	£550
TOTAL		**£5,500**	**100%**	**£5,000**

STEP 3

STEP 4

To note – the above is an example of an approach the Charity could take when identifying the transaction price

1. Contract with a third party

A Charity provides training courses, available to the public. The course fee is £5,000 for a 3-month course (with 12 sessions).

1. Upon sign up to the course – course materials are provided.
2. Included in the fee is access to network events held by industry experts (for which the Charity has an arrangement externally)
3. Final assessment to obtain certification for the completion of the course. (CPD certification).

- *What are the timings for when the performance obligations are met?*
- *Does the course end before the accounting year end?*

SORP 2026

- Under SORP 2026, a Charity must recognise the income when the performance obligations have been satisfied by transferring a promised good or service to a third party. A good or service is transferred when the **third party obtains control** of that good or service.

Performance obligation	**Allocation of £5,000 fee**	**Timing of recognition**
Course material	£550	Satisfied at point in time when course materials are sent to participant (i.e. start of the course)
Training course	£3,650	Satisfied over time, being the length of the course – i.e. £3,650 spread over a 3-month period. *[If it straddles the year end then to a proportion of income will be deferred at the year end].*
Networking events	£250	Satisfied over time – i.e. £250 spread over the number of network events held during the 3-month period. *[If it straddles the year end then to a proportion of income will be deferred at the year end].*
Final assessment and CPD certification	£550	Satisfied at point in time when participant completed the final assessment.
TOTAL	**£5,000**	

STEP 5

2. Care contracts

Each VODG member will have different types of income agreements in place.

But they are likely to fall into the following three types

Feature	Spot-purchase	Block contract	Framework agreement
What it is	Care purchased **per individual placement**	Care purchased for a **fixed number of units or capacity**	An **approved provider arrangement** setting terms and rates
Typical use in supported living	**Most common**	Less common; used for specialist or large schemes	Common, but **not income-generating on its own**
How income arises	When an **individual placement starts**	From the **availability of agreed capacity** (subject to terms)	Only when **spot or block placements** are awarded
Volume / occupancy risk	**Charity bears the risk**	Often **shared or transferred** to the local authority	Charity bears the risk until placements occur
Payment profile	Usually **weekly or monthly in arrears**	Fixed periodic payments, sometimes regardless of occupancy	No payment unless placements are made
Is there guaranteed income?	❌ No	✓ Often (subject to contract terms)	❌ No
Typical performance obligation	**Care services to a named beneficiary over time**	**Availability of capacity and/or care services**	None until a placement is agreed
Income recognition under SORP 2026	Recognised **over time** as care is delivered	Recognised **over time**, with judgement on variable consideration	Framework alone creates **no income**
Common accounting risk	Income recognised too early or not stopped promptly	Mis-identifying the performance obligation	Treating framework approval as income entitlement

2. Supported Living

A charity provides Supported Living Services to Mr Bob Smith. There is a contract agreement between the County Council and the Charity the services specified in the agreement include:

- Core Support – Daytime hours £750 per week
- Core support – sleep in £125 per week
- One to one support £240 per week

The contract started in December 20X5 and will be reassessed annually.

The charity has a March 20x6 year end.

SORP 2026

- Under SORP 2026, when a **contract** is in place, each **distinct performance obligation** must be identified and income **allocated** accordingly.

STEP 1

How Income Is Recognised Under SORP 2026

- Identify **distinct performance obligations**
- Allocate **transaction price** to each
- Recognise income **as each obligation is satisfied**

STEP 2

The supported living services are all levied by the performance of the weekly service therefore, whilst there are three distinct performance obligations

These are **distinct obligations delivered at the same time**.

Component	**Standalone Value**
Daytime core support	£750
Sleep in	£125
One to one support	£240
TOTAL	**£1,115 per week**

- December to March there were 16 weeks = £17,840
- All services were performed in accordance with specification

STEP 3

Considerations:

- Disputes over service provision
- Periods of absence
- Amendments

STEP 4

STEP 5

Income from Non-exchange transactions

The key changes under SORP 2026:

For gifts, the income criteria have changed to **only two criteria**: **received/receivable** and **reliably measured** (para 5.86) for legacy gifts or for grants either on performance (para 5.76) or otherwise when received or receivable (para 5.65).

For **legacies** the two criteria approach may affect your accounting policy and in some cases the timing of recognition. **Knowing about a will - i.e. entitlement - is no longer a factor**, instead focus on the **likelihood of benefitting**.
This change is most likely to affect charities using an estimation model that accrues income upon knowing of the death of the donor. Instead await probate or grant of confirmation (para 5.86).
Guidance in respect of life tenants is unchanged from before (para 5.90).

Approach to deferred income (para 5.76) and identification of contingent assets where gift uncertain (para 5.79) and legacies uncertain (para 5.88) is unchanged.

1. Income from performance related grant

A Charity receives a £120,000 grant from a funder to deliver a 12-month support programme.
Grant terms:

- £120,000 total funding
- Charity must:
  - Deliver one workshop per month, and
  - Submit monthly monitoring reports
- If programme finishes early, then the remaining funds are to be returned.

The Charity's year-end is 31 March.
By year-end:

- 9 workshops have been delivered

Under SORP 2019:

Under SORP 2019, Grant funding agreements may contain conditions that specify the services to be performed by a charity in receipt of a grant. Income must only be recognised to the extent that the charity has provided the specified goods or services as **entitlement to the grant only occurs when the performance-related conditions are met.**

Recognition under SORP 2019:

1. Total income received is £120,000 recognised in bank.
2. 9 workshops have been delivered over the 9 month period:
   9 months x (£120,000/12 months) = £90,000 recognised as income.
3. 3 months not yet earned:
   3 x (£120,000/12 months) = £30,000 recognised as deferred income.

On receipt of the funding:

DR Bank	£120,000	
CR Deferred income		£120,000

By year end:

DR Deferred income	£90,000	
CR Grant income		£90,000

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The Charity's year-end is 31 March.
By year-end:

- 9 workshops have been delivered

SORP 2026

Under SORP 2026, grant funding agreements may contain specific conditions that closely specify a level of output or service to be performed by a charity in receipt of a grant. These are performance-related conditions. A grant with performance-related conditions is **recognised in income only when the conditions are met.** If grant funding is received in advance of meeting performance-related conditions, it is accounted for as a liability and shown on the balance sheet as deferred income. Deferred income is released to income on the SoFA when the performance-related conditions are met.

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   9 months x (£120,000/12 months) = £90,000 recognised as income.
3. 3 months not yet earned:
   3 x (£120,000/12 months) = £30,000 recognised as deferred income.

On receipt of the funding:

DR Bank	£120,000	
CR Deferred income		£120,000

By year end:

DR Deferred income	£90,000	
CR Grant income		£90,000

2. Income from legacies

A charity receives a legacy gift in the year ended 31 December 2025. The value of the gift is £150,000.

1. The will is dated 9 September 2021 and names the Charity as being entitled to 1/4th of residual estate.
2. The Charity was informed on 31 December 2024 of the death of the donor.
3. Probate was granted on 12 June 2025.
4. Estate of accounts is dated November 2025 and states the Charity's share of the residual estate is £150,000.

Under SORP 2019:

- Under SORP 2019 (5.29), recognition of the legacy is based on evidence of **entitlement** a legacy exists, **probability** of receipt, and the **ability to measure or estimate with sufficient reliability** the amount receivable.

Legacy income recognition criteria is met when:

- **Entitlement** – named in the Will and probate has been granted → Charity has legal right
- **Probable** – probate has been granted → Executors have confirmed estate sufficiency
- **Reliably measurable –** estate of accounts have been provided and balance due is recorded → Estimated value known from estate

Recognition under SORP 2019:
Meets all three criteria (entitlement/probable/measurement).
As a result, the Charity recognises the £150,000 legacy income in the year ended 31 December 2025.

2. Income from legacies

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SORP 2026

- Under SORP 2026 (5.85), recognition is required when it is **probable** that the legacy will be received and its value can be **measured reliably**.

Unchanged from SORP 2019 - Receipt of legacy income is normally **probable** when:

- any applicable <u>grant of probate</u> or, in Scotland, grant of confirmation, has been made;
- the executors have established that there are <u>sufficient assets in the estate</u>, after settling any liabilities, to pay the legacy; and
- any <u>conditions attached</u> to the legacy are either <u>within the control of the charity or have been met</u>

Legacy income must only be recognised when it can be **reliably measured.** Charities should measure or estimate the fair value of the legacy income receivable based on the information available.

Recognition under SORP 2026 - criteria is met when:

- **Probable** – Executors satisfied and no unresolved conditions as probate is granted on 12 June 2025 → probable that the Charity will receive the legacy.
- **Reliably measured** – estate of accounts have been provided and balance due is recorded → Estimated value known from estate.

As a result, the Charity recognises the £150,000 legacy income in the year ended 31 December 2025.

Income from non-cash gifts

The key changes under SORP 2026:

Module 6 provides that for gifts (non-exchange transactions) the income criteria have changed to only two criteria: received/receivable and reliable measurement (para 6.4) subject to any performance conditions being met (para 6.4). (The entitlement criterion has been dropped).

In detail:

- **Donated goods for resale** at fair value on receipt (para 6.26) as stock where practical (para 6.29) or on sale (para 6.12)
- **Donated goods for distribution** at fair value on receipt as stock (para 6.23) or on distribution (para 6.12)
- **Donated facilities and services** on receipt or when receivable (para 6.14) at value to the charity (para 6.15)
- **General volunteers** not measured (para 6.18)
- **Fixed asset** related capitalised (para 6.21) or if lease related included in right of use asset (para 6.20)

Donated goods for distribution

SORP 2019	SORP 2026
6.23. Donated goods held by the charity for distribution to its beneficiaries **should be recognised as stock**, with the corresponding income recognised within donations and measured at its fair value.	6.23. Donated goods held by the charity for distribution to its beneficiaries **must be recognised as stock**, with the corresponding income recognised within donations and measured at their fair value.
6.24. It may be necessary when valuing the donation to consider any restriction on the sale of the asset or the factors that may reduce the fair value of the asset, such as proximity to a product expiry date or the availability of lower-cost substitutes for the donated item, for example a generic version of a drug. Donated goods held in stock for distribution must be assessed for impairment at the reporting date.	6.24. It may be necessary when valuing the donation to consider any restriction on the sale of the asset or the factors that may reduce the fair value of the asset, such as proximity to a product expiry date or the availability of lower-cost substitutes for the donated item, for example a generic version of a drug. Donated goods held in stock for distribution must be assessed for impairment at the reporting date **following the requirements outlined in paragraph 6.22.**
6.25. In the reporting period in which the stocks are distributed, they are recognised as an expense **and appropriately analysed as expenditure** in the SoFA**.** The expense recognised is the carrying amount of the stocks at the point of distribution.	6.25. In the reporting period in which the stocks are distributed, they are recognised as an expense in the SoFA. The expense recognised is the carrying amount of the stocks at the point of distribution.
6.26. **If it is impractical to assess** the value of donated stock held for distribution at the time of receipt, or if the costs involved in undertaking the valuation of donated stock outweigh the benefit to users of the accounts and to the charity of having this financial information, the value to the charity of the gift must be recognised as a component of donations when it is distributed, with an equivalent amount recognised as charitable expenditure.	**6.12**. If it is impracticable to measure the fair value of goods donated for resale or distribution at the point the goods are received, the donated goods must be recognised as income when they are sold or distributed.

Donated facilities and services

Measurement of a **donated asset** is at **fair value** and a **donated facility or service** is at **value to the charity**, in line with the requirements of FRS 102 and this remains **unchanged.**

To note - Minor updates have been made to Module 6 to reflect the new lease accounting requirements within SORP module 10B ‘Lease accounting’ so that charities are clear on how to account for the **non-exchange component** of a lease arrangement where the **lease arrangement also contains a donation**.

> *Lease arrangements where the payments are below market rent but are higher than a nominal amount as a result of the lessor choosing to accept a lower rent for the philanthropic intention of providing a benefit to the lessee are social donation leases. A charity may enter into a social donation lease either as a lessee or lessor.*

The definition of **peppercorn arrangements** has also been updated within Module 10B as well as in the glossary to this SORP to be clearer as to the arrangements this applies to.

> *Peppercorn arrangements – in this SORP such arrangements are considered to have the form of a lease, but any consideration paid lacks economic substance (nil or nominal amounts) meaning the arrangements are unlikely to meet the FRS 102 definition of a lease but are considered to be a form of non-exchange transaction.*

Implementation and First-Day Transition

Charities must apply this SORP for accounting periods beginning on or after 1 January 2026.

Under the Charity SORP 2026 – Charities must refer to Section 1 of FRS 102 for guidance on the transition.

FRS102 notes that when an entity first applies the Periodic Review 2024 amendments it shall apply the amendments **retrospectively,** in accordance with paragraph 10.12, except as specified in paragraphs 1.40 to 1.68.

Section 1.61 – 1.64 specifically refers to the exceptions for *Revenue from contracts with customers*, whereby transition can be:

(a) ***retrospectively with the cumulative effect*** *of initially applying that section recognised as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate a)* ***at the date of initial application;***

(a) ***shall not restate comparative*** *information;*

(b) shall apply that section retrospectively only to ***contracts that are not completed contracts*** *at the date of initial application; and*

(c) may use the practical expedients described in paragraphs 1.65(b) and (c).

Or

(b) retrospectively in accordance with paragraph 10.12.

- *Para 10.2 - When a change in accounting policy is applied retrospectively in accordance with paragraph 10.11, the entity shall* ***apply the new accounting policy to comparative information for prior periods to the earliest date for which it is practicable****, as if the new accounting policy had always been applied.*

This approach is referred to as a 'modified retrospective approach', which is also used for leases.

Charity Name

Year ended [REPORTING DATE]

	Endowment Funds	Restricted Funds	Unrestricted Funds	Total Funds
Balance at [START OF PRIOR PERIOD] (as previously reported)	XX,XXX	XX,XXX	XX,XXX	XXX,XXX
Effect of change in accounting policy *(see note X)*	-	-	XX,XXX	XXX,XXX
Balance at [START OF PRIOR PERIOD] (restated)	XX,XXX	XX,XXX	XX,XXX	XXX,XXX

Practical tips to prepare for these changes

- ❑ **Assess income streams and contracts**
  - Conduct a **detailed review** of your charity's income streams to identify those with performance conditions.
  - Pay particular attention to agreements that span **multiple accounting periods**.
  - For each income stream, document any **performance obligations** and their associated **transaction values** per the contract. This will help in determining when income should be recognised under the new rules.

- ❑ Complications arise with mixed goods and service bundles, bundled items, variable amounts payable including discounts, penalties and refunds. **A pricing policy is essential**. (The entitlement to raise an invoice is now a matter of cash-flow and has no direct effect to recognition.)

- ❑ **Strengthen financial reporting processes**
  - Ensure that your organisation is **collecting the necessary data**, such as performance metrics for contractual income.
  - Provide **training** for finance staff and trustees to understand the upcoming changes and their implications.

- ❑ **Engage early with professional advisors**
  - Consult with your auditors and advisors **early** to understand how the changes may affect your charity's specific circumstances.
  - For example by **modelling potential scenarios** to ascertain how asset and liability values might be impacted by the changes and understand potential knock-on effects.

Any questions?

2026 SORP
Lease Accounting

29 January 2026

Now, for tomorrow

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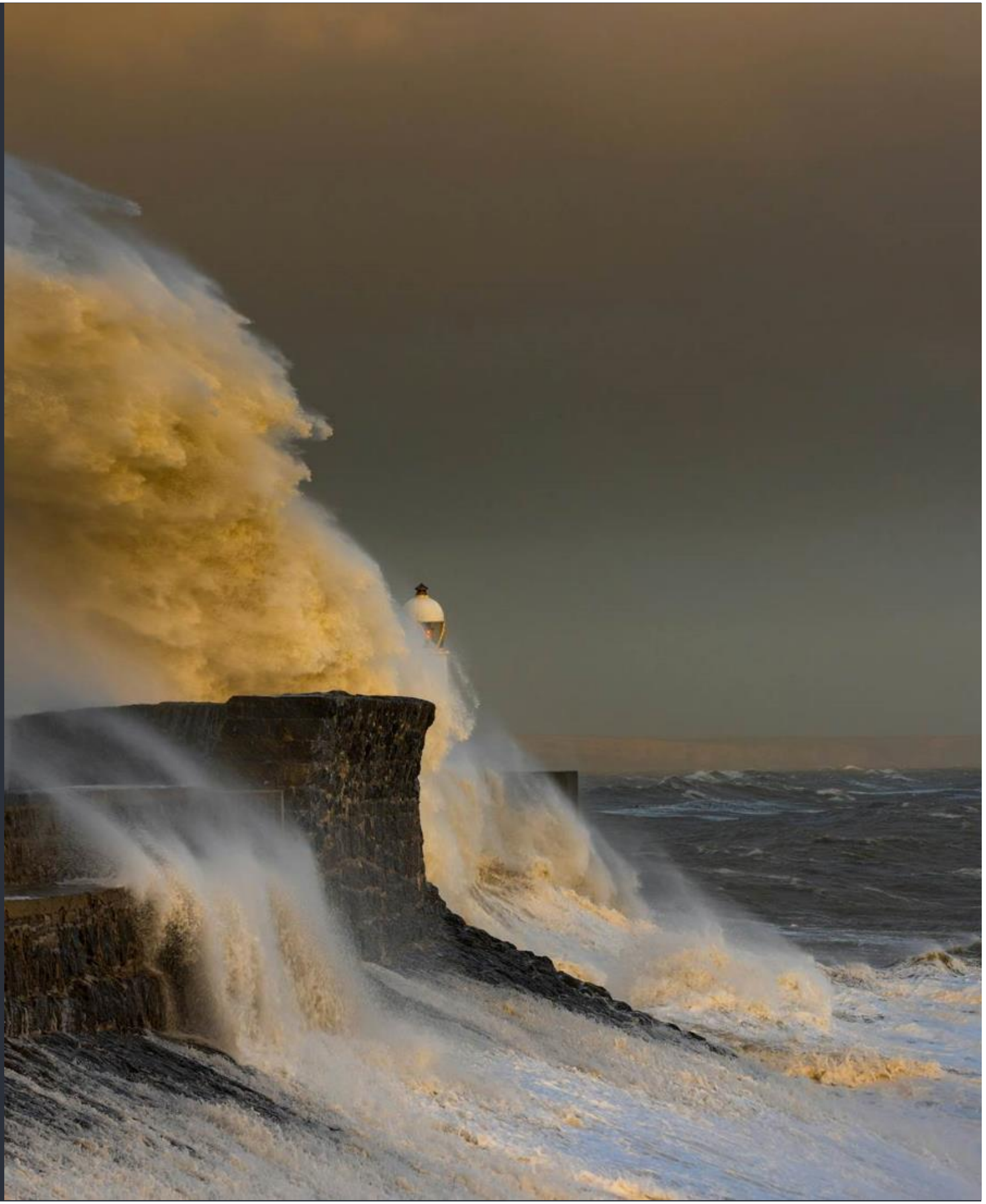
Transition to SORP 2026 and worked examples

Webinar overview

SORP 2026 –Leases – Module 10

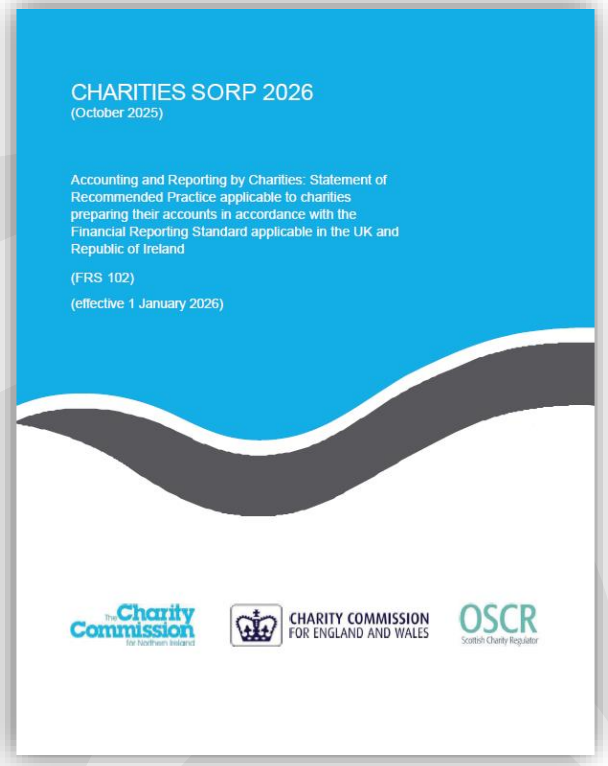
- Understanding the New Requirements
- Comparison with Current Practice
- Step-by-Step Implementation Guidance
- Transitioning to Your First Accounting Period
- Worked Examples and Real-Life Scenarios

Q & A session



Recap: Main sections & significant changes

https://www.charitysorp.org/



Module 1 – Trustees Annual Report

- Financial review
- Impact Reporting
- Sustainability Reporting
- Volunteers
- Reserves
- Going concern
- Legacies

Significant Changes to financial statements:

- Module 5 - **Revenue** recognition – 5 step model (only affects exchange transactions)
- Module 7 – Recognition of **expenses**
- Module 10 - **Leasing** – no distinction between operating and finance leases (flowchart and 2 information sheets)*
- Module 14 – Statement of **cashflows** (Tier 1 & 2 exempt)
- Module 18 – **Heritage Assets**
- Module 21 – Accounting for **social investments**

***Note – Tiering does not apply to Module 10 (and other modules)**

Some reminders

- The Charities SORP 2026 is not one-stop guidance
- Must consider other relevant guidance – FRS 102, statutes and regulations in each Nation e.g. Charities Acts 2011, 2016, 2022, Accounts Regulations 2008 etc
- Also consider legal form – e.g. Company Law
- The SORP is modular

SORP
Financial Statement Changes

- Module 10 – **Leasing**

Key change: Lease accounting

Accounting for lessors is unchanged but for lessees the distinction between an operating and finance leases is gone (para 10B.6). Unless an exemption applies all leases are ‘on balance sheet’ with a more complex accounting treatment required. Not all rented items count as leased eg intangible asset licenses (FRS102 section 20 para 20.1).

For lessees, the new approach requires trustees to:

1. Consider the new terminology (para 10B.8) and work through the flow chart (Diagram 1)
2. Identify each agreement that has characteristics of a lease (para 10B.21)
3. Identify if any exemption applies (para 10B.16) - short term or low value lease
4. Identify if peppercorn or nominal or zero payment due (paras 10B.75 and 10B.76)
5. Otherwise for each lease the commencement date (para 10B.35), lease term (para 10B.36) and non-cancellable period (para 10B.37)
6. Calculate the right of use asset (paragraph 10B.49) and related lease liability (paragraph 10B.51)
7. Identify the financing element of the lease payment (para 10B.54)
8. Identify the accounting policy and depreciation of the right of use asset (para 10B.58)
9. ‘Social donation leases’ identify the gift element on initial recognition (para 10B.42) and add to right of use asset value (para 10B.83)
10. (Approach to lessor accounting as now treat either as finance lease (10B.113) or operational lease (para 10B.119). Note treatment where a social donation lease (paras 10B.125 to 10B.127).)

Lease or rental expense

No-exemptions

Agreement for use of an asset is a lease

N → Keep calm and carry on

Y

A lease is a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.

Exemptions

Keep calm and carry on

1. Current operating lease recognition in SOFA on straight line basis

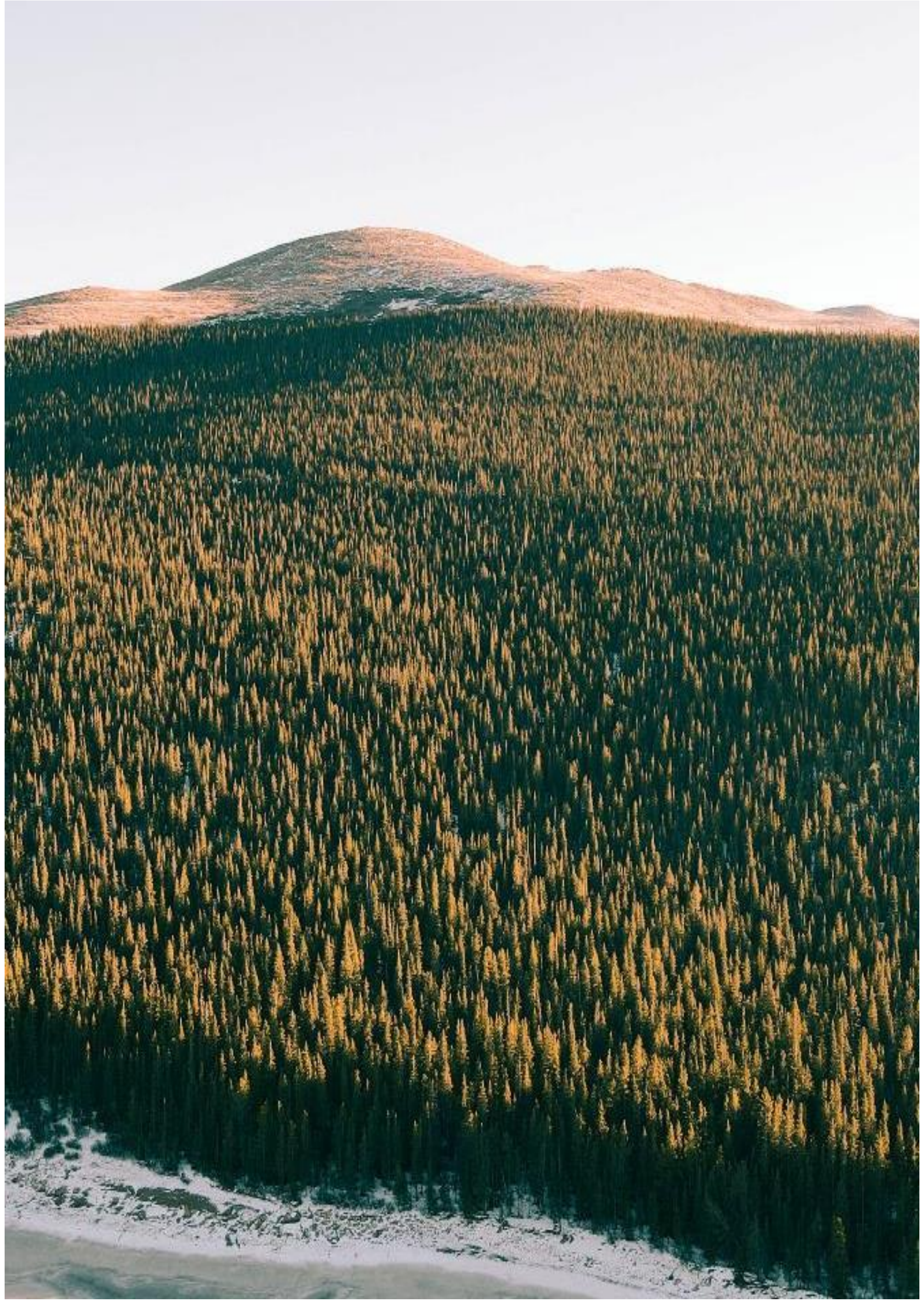
There are no substantive changes to how (exempt) leases are recognised

Lease accounting - exemptions

Section 20 of FRS 102 provides recognition **exemptions** for those leases that meet the definition of:

- **Short term** – applicable to classes of asset – on commencement term of 12 months or less (cannot have purchase option)

- **Low value** – applicable on an asset by asset basis – must be separable – (excludes Cars, Lorries, land and buildings) – includes computers, small office furnishings, telephones



Lease or rental expense

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A lease is a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.

Keep calm and carry on

1. Current operating lease recognition in SOFA on straight line basis

There are no substantive changes to how (exempt) leases are recognised

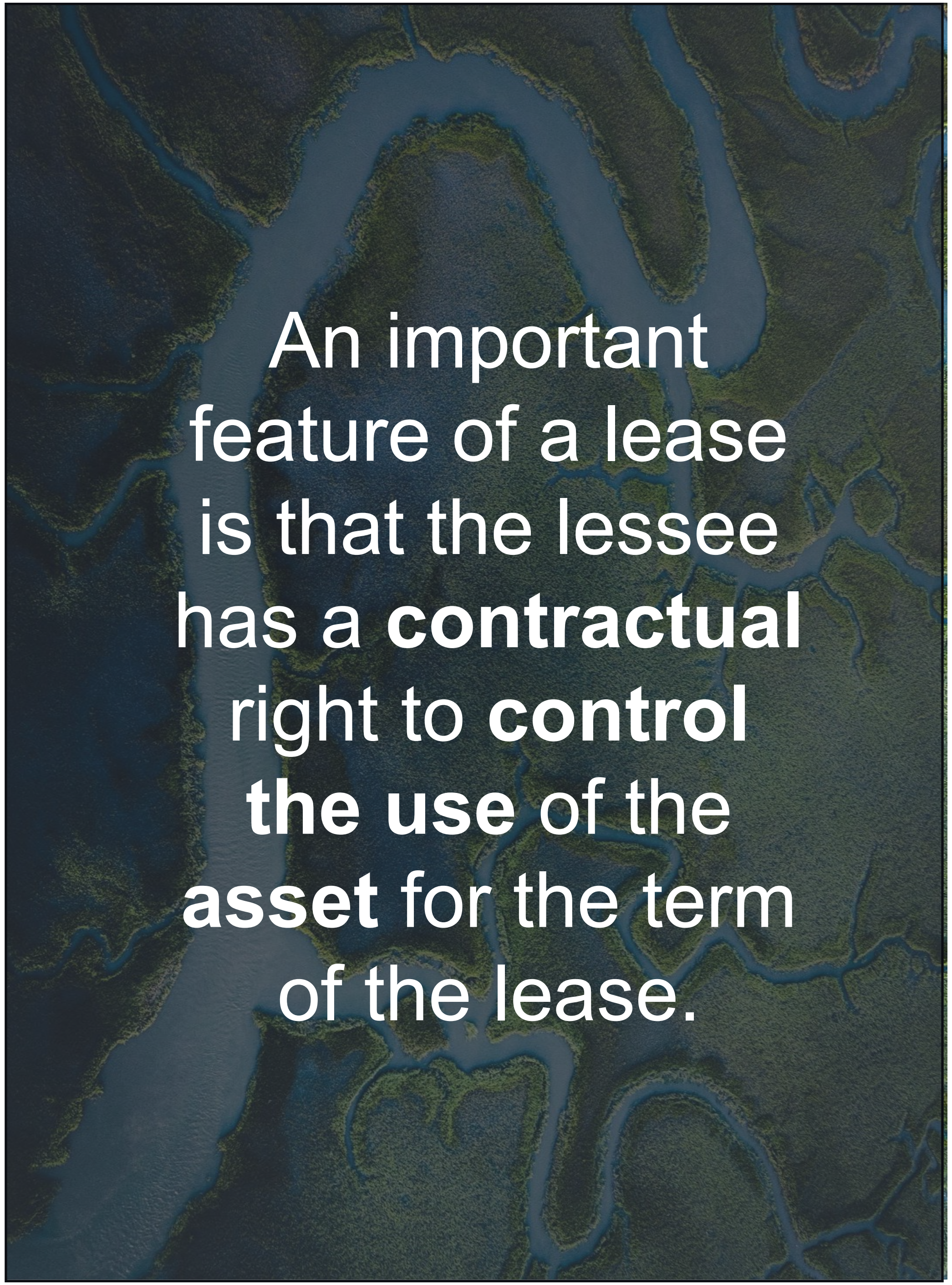
Lease accounting – what is a lease?

10B.23. The identifying features of a lease contract are:

- A contractual agreement is agreed by the parties for the identified asset.
- The contract may specifically identify the asset or the asset may be implicit when it is made available for use by the lessee
- The agreement gives the lessee the right to control the use of an identified asset. The agreement does this when the lessee has both the right to:
  - direct the use of the identified asset, and
  - obtain substantially all the economic benefits from that use
- There will be a commencement date when the lessee obtains the right of control over the asset from the lessor
- There will be a period of use specified when the lessee has the right of control over the asset. This can be viewed in terms of time or amount of use of an identified asset. For example, where an identified asset is a piece of equipment the amount of use could be the number of units of a product that the asset will be used to produce.
- There are payments due by the lessee to the lessor for the right of control over the asset

Lease accounting

- Commencement date is the date on which a lessor makes an underlying asset available for use by a lessee.
- Lease liability is the liability recognised at the commencement date by a lessee measured at the present value of the lease payments that are not paid at that date discounted using the interest rate applicable to that lease.
- Right-of-use asset is an asset that represents a lessee's right to use an underlying asset for the lease term.
- Interest rate implicit in the lease is the rate of interest that causes the present value of the lease payments and the unguaranteed residual value, to equal the sum of the fair value of the underlying asset and any indirect costs of the lessor.
- Lease term is the aggregate of: (a) the non-cancellable period of a lease; (b) periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option; and (c) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option.
- Licence agreement is a term used in this SORP to describe an arrangement that allows temporary (a period of 12 months or less), non-exclusive, use of an asset.
- Low value asset is where in a lease arrangement, the underlying asset is of low value on an absolute basis, regardless of whether such leases would be material to the lessee. The value of lease payments has no bearing on the assessment of whether an underlying asset is of low value.
- Social donation lease is defined in this SORP as a lease where the lessor chooses to accept a lower rent for the philanthropic intention of providing a benefit to a public benefit entity.
- Short-term lease is a lease that, at the commencement date, has a lease term of 12 months or less. (A lease that contains a purchase option is not a short-term lease.)
- Peppercorn arrangements – in this SORP such arrangements are considered to have the legal form of a lease, but with nil or nominal consideration and are unlikely to meet the FRS 102 definition of a lease but are considered therefore to be a form of non-exchange transaction.

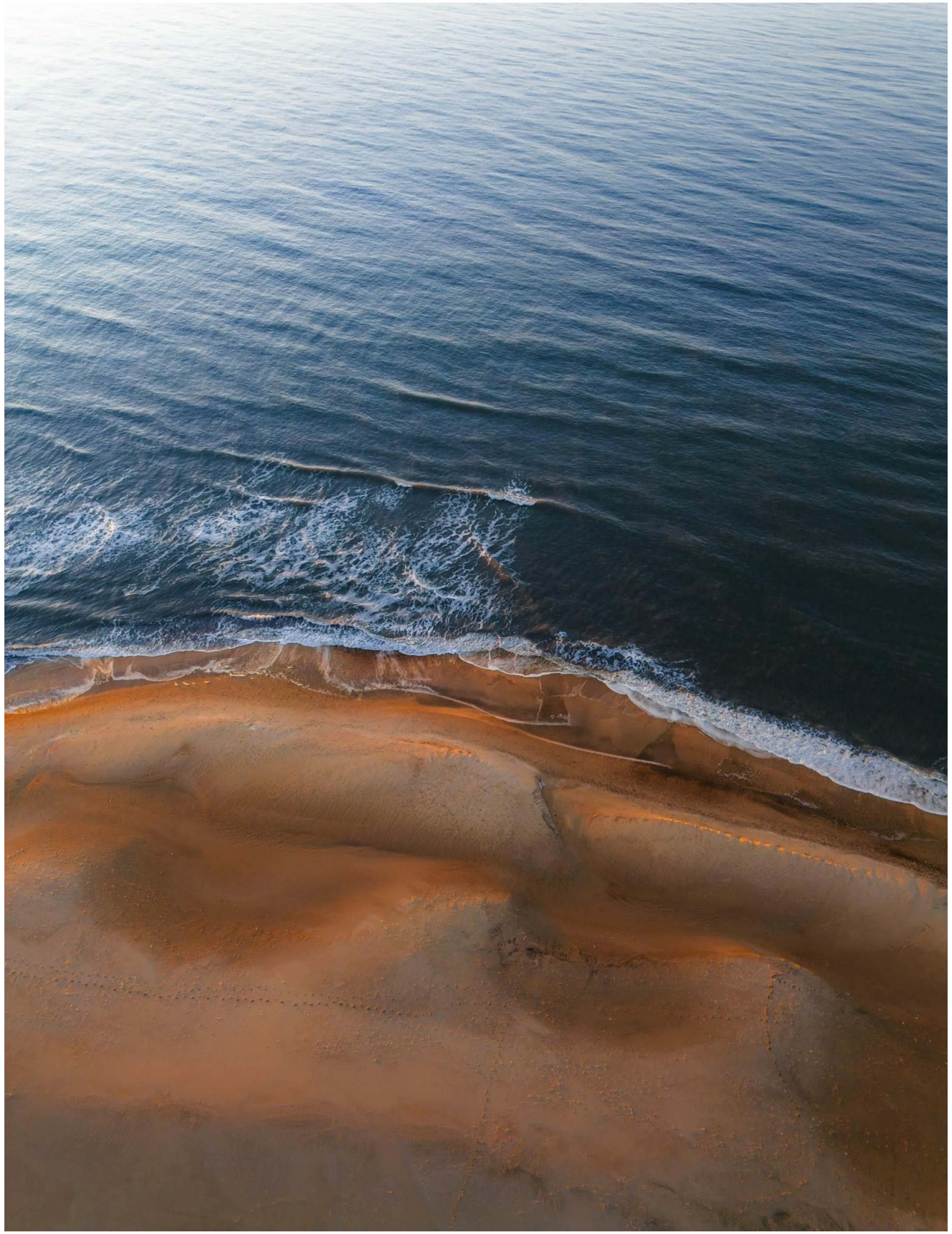


Lease accounting – steps

1. **Identify a lease agreement**
2. **Identify asset**
3. **Establish the right to control the use of the asset**
4. **Identify the commencement date and lease term**
5. **Separate the components of an agreement (cleaning, catering etc.)**

Measure the right-of use asset at cost and measure the lease liability (including interest element of lease and discounted for time value of money)

Present value of the lease payments



Lease accounting – example

Community Support Charity

- *Charity leases an office building used entirely for charitable activities*
- *Lease commenced: **1 April 2026***
- *Lease term: **5 years**, no break clauses*
- *Lease payments: **£50,000 per annum**, payable annually **in arrears***
- *No lease incentives*
- *No dilapidation provision*
- *Asset not low-value, lease not short-term*
- *Charity has **no external borrowing***
- *Charity holds surplus cash on deposit earning **5%***

Accounting under SORP 2019 (Old Treatment)

- Lease classified as an operating lease
- No balance sheet recognition
- Lease expense recognised straight-line in the SoFA

Dr / (Cr)	**£**
Charitable activities – premises costs	50,000
Cash or liabilities	(50,000)

Lease accounting – example

Community Support Charity

- *Charity leases an office building used entirely for charitable activities*
- *Lease commenced: **1 April 2026***
- *Lease term: **5 years**, no break clauses*
- *Lease payments: **£50,000 per annum**, payable annually **in arrears***
- *No lease incentives*
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- *Asset not low-value, lease not short-term*
- *Charity has **no external borrowing***
- *Charity holds surplus cash on deposit earning **5%***

Accounting under SORP 2026 (New Treatment)

Step 1 – Determine the Discount Rate
Step 2 – Measure the Lease Liability at Commencement
Step 3 – Measure the Right-of-Use Asset
Step 4 – Subsequent Measurement

Lease accounting – example

Step 1 – Determine the Discount Rate

The charity has:

- No borrowing
- Cash deposits earning **5%**

Under FRS 102 / SORP 2026, a **reasonable proxy for the incremental borrowing rate** is acceptable.

Assumption:
➞ Discount rate = **5%**

“No debt does not mean no discount rate.”

Lease accounting – example

Step 2 – Measure the Lease Liability at Commencement

Lease payments: £50,000 annually in arrears for 5 years

Discount rate: 5%

Present value factor of annuity at 5% for 5 years ≈ **4.329**

Lease liability at commencement:
£50,000 × 4.329 = **£216,450**

Present value factor = $\frac{1-(1+r)^{-n}}{r}$

Where r is the interest rate per period (0.05) and n is the number of periods (5 years).

Lease accounting – example

Step 3 – Measure the Right-of-Use Asset (ROU)

ROU asset initially equals:

- Lease liability
- plus any initial direct costs (none here)
- less incentives (none)

ROU asset = £216,450

Opening Journal (1 April 2026)

Dr / (Cr)	**£**
Leasehold– property	216,450
Lease liability	(216,450)

Split lease liability between current and non-current

Lease accounting – example

Step 4 – Subsequent Measurement

(4a) Depreciation of ROU Asset
Lease term = 5 years
Straight-line depreciation:
£216,450 ÷ 5 = **£43,290 per annum**

Dr / (Cr)	£
Charitable activities – depreciation	43,290
Accumulated depreciation – leasehold asset	(43,290)

(b) Interest on Lease Liability (Year 1)
Opening liability: £216,450
Interest at 5%: **£10,823**
Payment made at year-end: £50,000

Closing liability year 1:
£216,450 + £10,823 interest – £50,000 payment
= **£177,273**

Dr / (Cr)	£
Interest expense (SoFA)	10,823
Lease liability	39,177
Cash / creditors	(50,000)

Balance Sheet
Fixed assets
•Leasehold asset (NBV):
£216,450 – £43,290 = **£173,160**

Liabilities
•Lease liability: £177,273

SoFA Impact (Year 1)

Item	£
Depreciation	43,290
Interest	10,823
Total charge to SoFA	**54,113**

Lease accounting – example

5 year summary

Liability

Year	Opening Lease Liability (£)	Interest @ 5% (£)	Lease Payment (£)	Capital Repayment (£)	Closing Lease Liability (£)
1	216,450	10,823	(50,000)	39,177	177,273
2	177,273	8,864	(50,000)	41,136	136,137
3	136,137	6,807	(50,000)	43,193	92,944
4	92,944	4,647	(50,000)	45,353	47,591
5	47,591	2,379	(50,000)	47,621	**0**

Asset

Liabilities are higher than assets

Year	Opening ROU Asset (£)	Depreciation (£)	Closing ROU Asset (£)
1	216,450	(43,290)	173,160
2	173,160	(43,290)	129,870
3	129,870	(43,290)	86,580
4	86,580	(43,290)	43,290
5	43,290	(43,290)	**0**

Lease accounting – lessons

- **This is not optional**
  Operating lease accounting for lessees disappears under SORP 2026.

- **Balance sheets will grow (gross)**
  Many charities will show material new assets and liabilities for the first time.

- **Discount rate judgement matters**
  Deposit rates are often the best available proxy in the absence of borrowing.

- **SoFA volatility increases**
  Depreciation + interest ≠ straight-line rent.

- **Reserves calculations are affected**
  Lease liabilities may materially reduce “free reserves”.

Lease accounting – charity considerations

Nominal or below market rate leases – need to establish the intentions of the lessor – if for social purposes – "**social donation lease**"

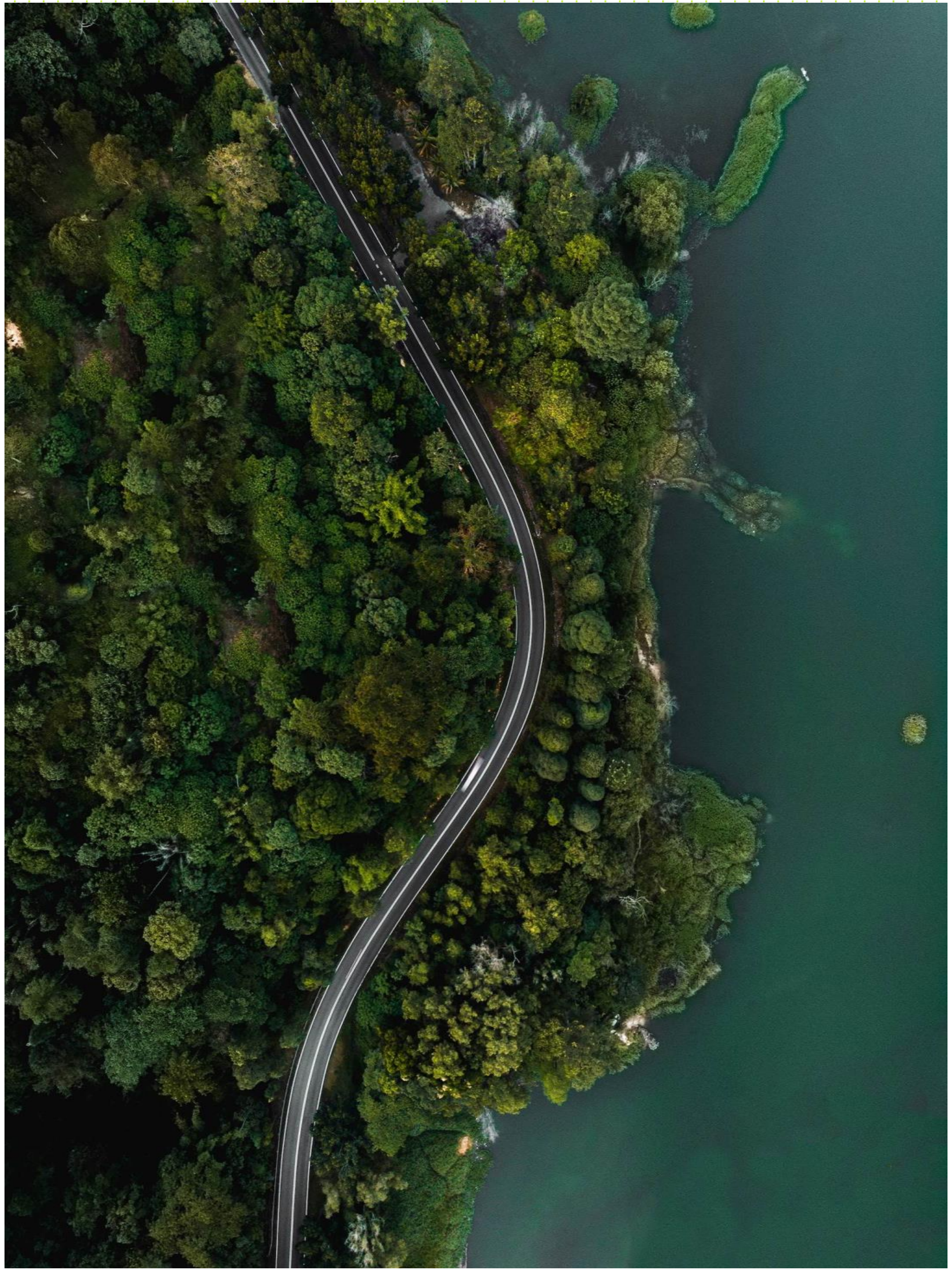
Nominal or peppercorn arrangements – these are not leases and therefore accounted for as donated services (eg each year income and expense to SOFA)

Dilapidations form part of the cost of a lease – but liability goes as a provision (not in lease liability)

Discounting – rate of interest on deposits can be used if no borrowing

Lease incentives – effect is to reduce the consideration paid for the lease which is reflected in the value of the right-of-use asset and in the calculation of the lease liability

Don't forget – the term of the lease includes options to extend where it is **reasonably certain** the option will be exercised.



Lease accounting – options to extend

Example

Charity agrees to lease a building for 25 years

- Options to terminate at end of years 10 and 20
- Opportunity to extend for a further 5 years

Non-cancellable period if the first 10 years.

What are the trustees reasonably certain of?

Judgment involved and importance of documenting trustee decisions

Rolling lease agreements

Consider period the lease is enforceable for and what the non-cancellable period is.

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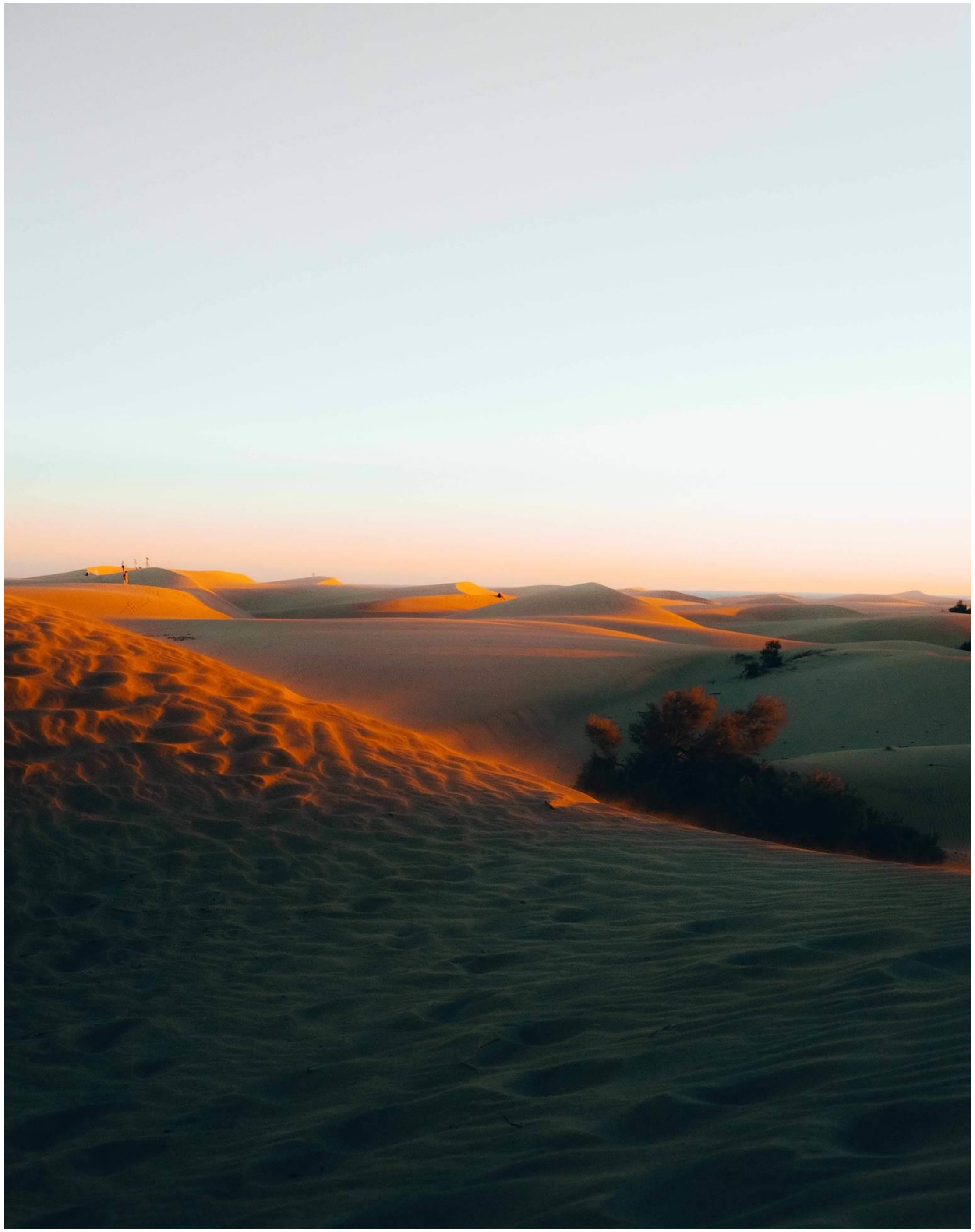
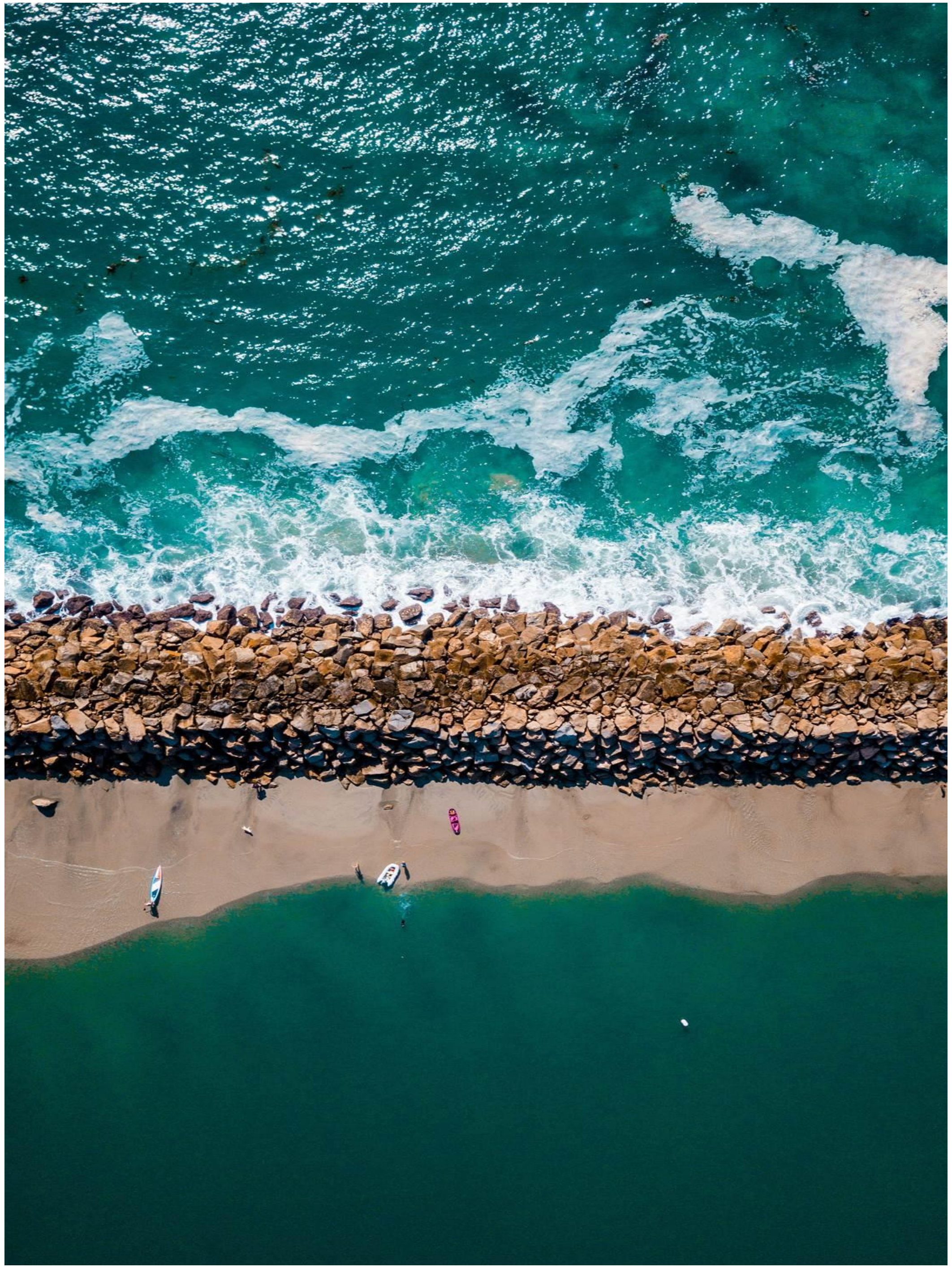


Lease accounting – Social donation lease

Social donation lease (payments are below market rate but higher than nominal/peppercorn) – where the discount is a 'social' contribution

- The value of the incoming resources from the non-exchange component is recognised as part of the cost of the right-of-use asset
- The charity recognises the related income at the same time
- The depreciation charges for the right of use asset will be greater than they would otherwise have been if the non-exchange component had not been recognised
- The initial lease liability is consequently lower than the initial value of the right-of-use asset.



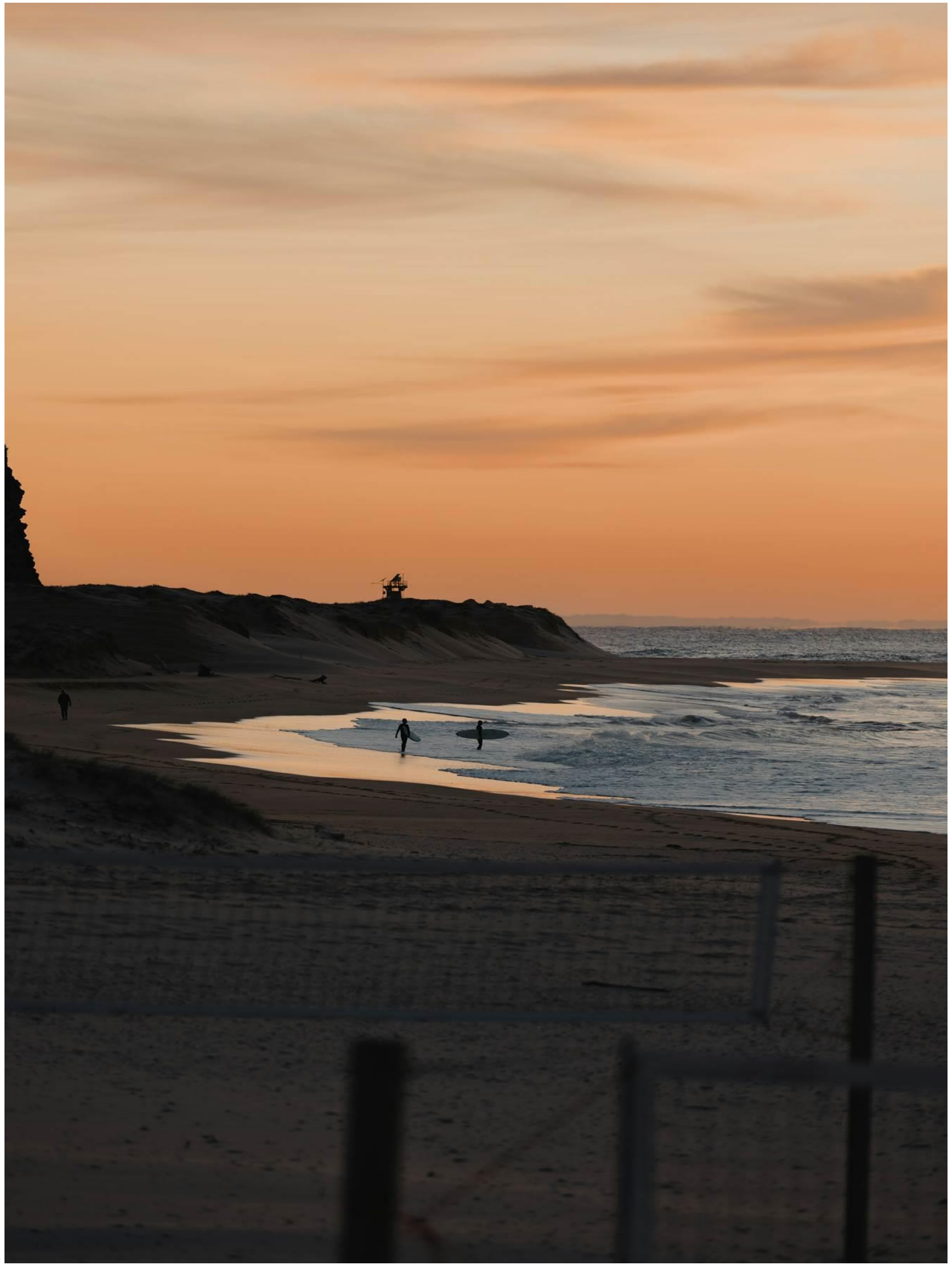
Social donation lease example

The example given:

- A charity enters into an agreement to use one floor of a five-storey office building for three years. The other four floors are occupied by the lessor, a commercial business. The market rent for this floor is **£120,000/year**.

- The lessor states that as part of its corporate social responsibility activities, it will give the charity a **50% discount** on the office space, so the **charity will pay £60,000/year instead**.

- If the arrangement not been available, the charity **expected to pay £72,000/year** for office space **elsewhere**.



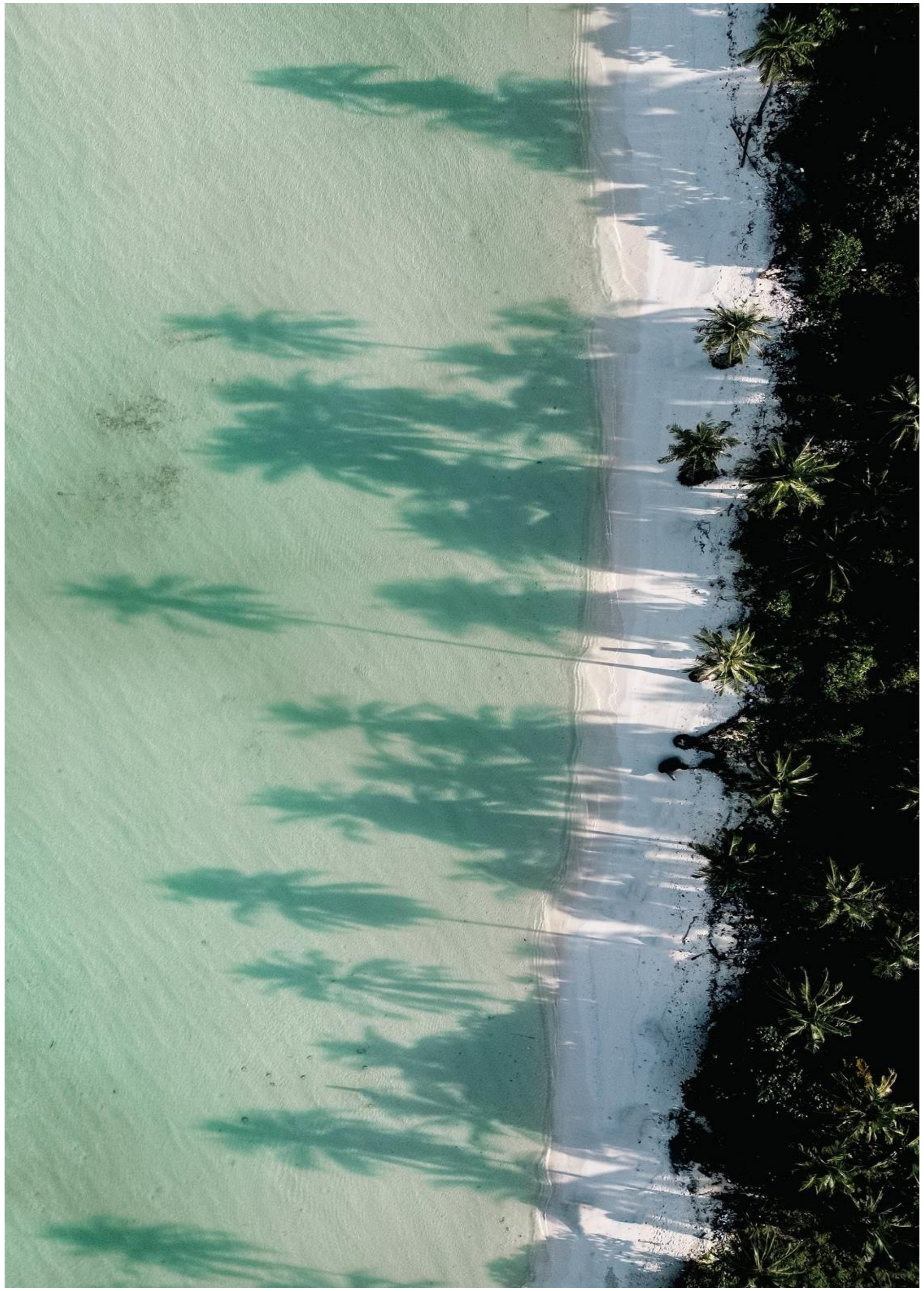
Social donation lease example solution

Solution:

- It is the value to the charity of the office space that is important
- The non-exchange element is £72,000 minus £60,000 = £12k a year
- Ignoring any discounting
- Depreciation over 3 year straight line

In Year 1
DR: Asset = (60,000 + 12,000) x 3 = 216,000
CR: Lease obligation (60,000 x 3) = 180,000
CR: Deferred Income – (12,000 x 3) = 36,000

DR Depreciation SOFA = £72,000
CR Asset Depreciation = £72,000
CR Bank = £60,000
DR Lease obligation £60,000
CR income - £12,000 grant
DR deferred income £12,000



Implementation and first-day transition

- Charities must apply this SORP for accounting periods beginning on or after 1 January 2026.

- When a charity first applies the *Periodic Review 2024 amendments*, it shall apply the revised Section 20 *Leases* of FRS 102:

  - Retrospectively with the cumulative effect of initially applying that section recognised as an adjustment to the opening balance of reserves at the date of initial application; or
  - An entity shall not restate comparatives

  This approach is referred to as a ‘modified retrospective approach’.

Implementation and First-Day Transition (continued)

The SORP references FRS102, which provides more detail:

- For leases previously classified as an operating lease:
  - Recognised a lease liability at the date of the 'initial application' of the new SORP/FRS102
    - Measure at the present value of the remaining discounted lease payments
  - Recognised a right-of-use asset at the date of the initial application
    - Measure at an amount equal to the lease liability, less any prepaid or accrued lease payments
  - Consider whether a social donation was present in the lease at the commencement/modification date, and consider impairment at the date of the initial application
  - Low-value leases need not be adjusted for, nor do leases where the term ends within 12 months of the initial application

- For leases previously classified as a finance lease:
  - Recognise a lease liability and right-of-use asset at the date of the initial application at the carrying amount of the leased asset.

Disclosures

- Charities MUST provide a general description of its significant leasing arrangements – accounting policies.

- If necessary for significant leasing arrangements, must disclose as a minimum:
  - Future cash flows (not already reflected in lease liabilities)
  - Restrictions or covenants
  - Discount rates
  - Sale and leaseback transactions

- Social donation leases or peppercorn arrangements

- MUST disclose following amounts (more common):
  - Interest expense on lease liabilities
  - Expenses associated with short term leases or low value assets and commitments
  - Total cash outflow for leases
  - ROU asset – gross carrying amount and accumulated depreciation, separate disclosure of additions, disposals, depreciation etc.

Practical tips to prepare for these changes

- ❑ **Analyse lease commitments:** create a comprehensive inventory of all current leases, categorising them as operating or finance leases under the current framework and listing the terms and conditions of the lease agreement. Estimate how the new lease accounting standards might affect your balance sheet and Statement of Financial Activities (e.g. increased depreciation, reduced rental costs). Also consider the impact of the changing recognition, for example for bank covenants, or on whether the charity breaches the asset-related audit threshold.

- ❑ Finance teams must identify the appropriate borrowing rate for each lease and determine the lease term, considering any extension or termination options that are reasonably certain to be exercised.

- ❑ **Strengthen financial reporting processes:** ensure that your organisation is collecting the necessary data, such as detailed lease terms. Provide training for finance staff and trustees to understand the upcoming changes and their implications.

- ❑ **Engage early with professional advisors**: consult with your auditors and advisors early to understand how the changes may affect your charity's specific circumstances, for example by modelling potential scenarios to ascertain how asset and liability values might be impacted by the changes and understand potential knock-on effects.

Any questions?

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