

Duncan & Toplis Limited

FRED 82 – Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and other FRSs

Invitation to comment response

Question 1: Disclosure

Do you have any comments on the proposed overall level of disclosure required by FRS 102?

A1a: FRED 82 represents an increased level of disclosure, especially for section 1A adopters with the requirement that previously suggested disclosures will now be mandatory.

The increased disclosures suggested will provide an enhanced level of disclosure across the board. In particular the changes to the treatment of operating leases will represent a significant change. Comments on this are noted below.

There is a clear move to greater transparency for financial reporting and FRED 82 does help to achieve this.

Do you believe that users of financial statements prepared under FRS generally be able to obtain the information they seek? If not, why not?

A1b: Even with the proposed changes per FRED 82 we believe that many users of financial statements will still not be able to obtain the information that they require. For example, the ability for small entities to not have their profit and loss account on public record or the directors' report. However, proposed reforms to Companies House will remove these filing exemptions and therefore in combination with FRED 82 users needs will be further satisfied.

Question 2: Concepts and pervasive principles

The proposed revised Section 2 Concepts and Pervasive Principles of FRS and FRS 105 would broadly align with the IASB's 2018 Conceptual Framework Financial Reporting.

The IASB's Exposure Draft Third edition of the IFRS for SMEs Accounting Standard (IASB/ED/2022/1) contains similar proposals. The FRC considers appropriate that FRS 102 and FRS 105 should be based on the same concepts and pervasive principles as IFRS Accounting Standards including the IFRS SMEs Accounting Standard, given the FRC's aim of developing financial reporting standards that have consistency with global accounting standards.

The FRC has made different decisions from the IASB in some respects developing proposals to align FRS 102 and FRS 105 with the 2018 Conceptual Framework in a proportionate manner.

Do you agree with the proposal to align FRS 102 and FRS 105 with the Conceptual Framework? If not, why not?

A2a: We have no objections to the proposed alignment.

This FRED, and IASB/ED/2022/1, propose to continue using the extant definition of an asset for the purposes of Section 18 Intangible Assets other than Goodwill and the extant definition of a liability for the purposes of Section 21 Provisions Contingencies of FRS 102. This is consistent with the approach taken in IAS Intangible Assets and IAS 37 Provisions, Contingent Liabilities and Contingent Assets which use the definitions of an asset and a liability from the IASB's Framework for the Preparation and Presentation of Financial Statements.

Do you agree with this approach? If not, why not?

A2b: Yes, we have no objections to this.

Do you have any other comments on the proposed revised Section 2?

A2c: No.

Question 3: Fair value

The proposed Section 2A Fair Value Measurement of FRS 102 would align the definition of fair value, and the guidance on fair value measurement, with that in IFRS 13 Fair Value Measurement.

Do you agree with this proposal? If not, why not?

A3a: We have no objections to this. The change will more closely align UK GAAP with international standards.

Do you agree with the proposed consequential amendment to Section 26 Share-based Payment of FRS 102 to retain the extant definition of fair value for the purposes of that section? If not, why not?

A3b: It would be interesting to further understand why the extant definition of fair value has been maintained for this particular area, rather than adopting the proposed approach. However, we have no objection to the proposal.

Question 4: Expected credit loss model

The FRC intends to defer its conclusion as to whether to align FRS 102 with the expected credit loss model of financial asset impairment from IFRS 9 Financial Instruments pending the issue of the IASB's third edition of the IFRS for SMEs Accounting Standard. Any proposals to align with the expected credit loss model will therefore be presented in a later FRED.

Do you agree with this approach? If not, why not?

A4a: Yes. FRED 82 already contains a number of significant amendments that will represent a significant shift for many thousands of businesses. Inclusion of the current expected credit loss model at this stage may place an excessive strain on business.

In IASB/ED/2022/1 the IASB proposes to retain the incurred loss model for trade receivables and contract assets, and introduce an expected credit loss model for other financial assets measured at amortised cost. The FRC's preliminary view is that, in the context of FRS 102, it may be appropriate to require certain entities to apply an expected credit loss model to their financial assets measured at amortised cost, but allow other entities to retain the incurred loss model.

Do you agree with this view? If not, why not?

A4b: Yes, this will be a new and relatively complex requirement for many businesses. A proportional approach should be taken to enhance adherence to the revised requirements.

Based on stakeholder feedback received to date, the FRC does not intend to use the existing definition of a financial institution to define the scope of which entities should apply an expected credit loss model. The FRC's preliminary view is that it may be appropriate to define the scope based on an entity's activities (such as entering into regulated or unregulated credit agreements as lender, or finance leases as lessor), or on whether the entity meets the definition of a public interest entity.

Do you have any comments on which entities should be required to apply an expected credit loss model?

A4c: This would appear to be a reasonable approach. Entities that do not hit the definition of a financial institution may well still engage in activities where it would be appropriate to adopt this model.

Question 5: Other financial instruments issues

When it has reached its conclusion as to whether to align FRS 102 with the expected credit loss model, the FRC intends to remove the option in paragraphs 11.2(b) and 12.2(b) of FRS 102 to follow the recognition and measurement requirements of IAS 39 Financial Instruments: Recognition and Measurement. This intention was communicated in paragraph B11.5 of the Basis of Conclusions to FRS 102 following the Triennial Review 2017. In preparation for the eventual removal of the IAS 39 option, the FRC proposes to prevent an entity from newly adopting this accounting policy.

Do you agree with this proposal? If not, why not?

A5a: Yes, it will ensure consistency across all users of FRS 102.

Temporary amendments were made to FRS 102 in December 2019 and December 2020 in relation to interest rate benchmark reform (IBOR reform). The FRC intends to consider, alongside the future consideration of the expected credit loss model, whether these temporary amendments have now served their purpose and could be removed.

Do you support the deletion of these temporary amendments? If so, when do you think they should be deleted? If not, why not?

A5b: Yes. We have no comment on timing.

Question 6: Leases

FRED 82 proposes to revise the lease accounting requirements in FRS 102 to reflect the on-balance sheet model from IFRS 16 Leases, with largely-optional simplifications aimed at ensuring the lease accounting requirements in FRS 102 remain cost-effective to apply. An entity electing not to take these proposed simplifications will follow requirements closely aligned to those of IFRS 16, which is expected to promote efficiency within groups.

Do you agree with the proposals to revise Section 20 of FRS 102 to reflect the on-balance sheet lease accounting model from IFRS 16, with simplifications? If not, why not?

A6a: Overall, we have concerns over the benefit of adopting this approach, especially for smaller entities.

We understand that for certain entities and industries the on-balance sheet approach for operating leases will lead to greater comparability (for example the air-line industry) but for many businesses where there are relatively few users of the financial statements we believe that the cost of the additional accounting required will be significantly greater than the benefit to the users or the entity.

It will be a hard sell to smaller business owners that they will need to recognise on their balance sheets, 'assets' that they do not own. It does feel like this will add significant complexity for relatively little gain.

We would like to see a greater level of exemptions for entities utilising 1A, perhaps even a complete exemption / accounting policy choice in this area.

Have you identified any further simplifications or additional guidance that you consider would be necessary or beneficial?

A6b: As noted above.

Question 7: Revenue

FRED 82 proposes to revise the revenue recognition requirements in FRS 102 and FRS 105 to reflect the revenue recognition model from IFRS 15 Revenue from Contracts with Customers. The revised requirements are based on the five-step model for revenue recognition in IFRS 15, with simplifications aimed at ensuring the requirements for revenue in FRS 102 and FRS 105 remain cost-effective to apply. Consequential amendments are also proposed to FRS 103 and its accompanying Implementation Guidance for alignment with the principles of the proposed revised Section 23 of FRS 102.

Do you agree with the proposals to revise Section 23 of FRS 102 and Section 18 of FRS 105 to reflect the revenue recognition model from IFRS 15, with simplifications? If not, why not?

A7a: Yes, no objections. We believe that introduction of the revised recognition requirements will help to improve consistency in revenue recognition and make clearer to the users of financial statements when revenue is recognised for the different products and services offered by and entity.

Have you identified any further simplifications or additional guidance that you consider would be necessary or beneficial?

A7b: We have not further comments to add.

Question 8: Effective date and transitional provisions

The proposed effective date for the amendments set out in FRED 82 is accounting periods beginning on or after 1 January 2025, with early application permitted provided all amendments are applied at the same time.

Do you agree with this proposal? If not, why not?

A8a: We have no objections to the proposed effective date.

FRED 82 proposes transitional provisions (see paragraphs 1.35 to 1.60 of FRS 102 and paragraph 1.11 of FRS 105).

In respect of leases, FRED 82 proposes to permit an entity to use, as its opening balances, carrying amounts previously determined in accordance with IFRS 16. This is expected to provide a simplification for entities that have previously reported amounts in accordance with IFRS 16 for consolidation purposes, promoting efficiency within groups.

Do you agree with this proposal? If not, why not?

A8b: We have no objections to this proposal.

Otherwise, FRED 82 proposes to require the calculation of lease liabilities and right-of-use assets on a modified retrospective basis at the date of initial application.

Do you agree with this proposal? If not, why not?

A8c: We have no objections to this proposal.

In respect of revenue, FRED 82 proposes to permit an entity to apply the revised Section 23 of FRS 102 on a modified retrospective basis with the cumulative effect of initially applying the revised section recognised in the year of initial application. This is expected to ease the burden of applying the new revenue recognition requirements retrospectively by removing the need to restate comparative period information. Unlike IASB/ED/2022/1, to ensure comparability between current and future reporting periods, FRED 82 does not propose to permit the revised Section 23 of FRS 102 to be applied on a prospective basis. However, FRED 82 proposes to require micro-entities to apply the revised Section 18 of FRS 105 on a prospective basis.

Do you agree with these proposals? If not, why not?

A8d: The proposals appear reasonable and will ensure comparability moving into future periods.

Do you have any other comments on the transitional provisions proposed in FRED 82?

A8e: We would suggest that clear, worked examples are provided to assist users of the FRS with the transition to the amendments set out in FRED82. This will help to ensure consistent application of the standards.

Have you identified any additional transitional provisions that you consider would be necessary or beneficial? Please provide details and the reasons why.

A8f: We have no further suggestions.

Question 9: Other comments

Do you have any other comments on the proposed amendments set out in FRED 82?

A9a: We have no further suggestions.

Question 10: Consultation stage impact assessment

Do you have any comments on the consultation stage impact assessment, including those relating to assumptions, sources of relevant data, and the costs and benefits that have been identified and assessed? Please provide evidence to support your views.

In particular, feedback is invited on the assumptions used for quantifying costs under each of the proposed options (Section 3 of the consultation stage impact assessment); any evidence which might help the FRC quantify the benefits identified or any benefit which might arise from the options proposed which the FRC has not identified (Section 4 of the consultation stage impact assessment); and appropriate data sources to use to refine the assumption of the prevalence of leases by entity size (Table 23 of the consultation stage impact assessment).

A10a: We have no comments to make on any of the points raised within question 10.