Financial Reporting Council

December 2019

Impact Assessment and Feedback Statement

Amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*

Interest rate benchmark reform

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Overview

(i) In December 2019, FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* was amended by *Amendments to FRS 102 – Interest rate benchmark reform*. This Impact Assessment and Feedback Statement accompanies those amendments, which were in relation to specific hedge accounting requirements and provide relief that will avoid unnecessary discontinuation of hedge accounting during the period of uncertainty as interest rate benchmarks are being reformed.

(ii) The Impact Assessment and Feedback Statement:

(a) sets out the Impact Assessment for these amendments, after taking account of respondents' comments on the Consultation stage impact assessment; and

(b) summarises the ten responses received to FRED 72 *Draft amendments to FRS 102 – Interest rate benchmark reform* and the FRC's response to them.

Impact Assessment

Introduction

1 The Financial Reporting Council (FRC) is committed to a proportionate approach to the use of its powers, making effective use of impact assessments and having regard to the impact of regulation on small enterprises.

Amendments to FRS 102

2 These amendments will only affect entities that choose to apply hedge accounting.

3 Interest rate benchmarks such as the London Interbank Offered Rate (LIBOR) are being reformed, and it is anticipated that LIBOR will not be available after 2021. There is increasing uncertainty about the long-term viability of some interest rate benchmarks and this gives rise to issues affecting financial reporting in the period before the reform, particularly in relation to hedge accounting.

4 Interest rate benchmark reform will affect some entities applying FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. In relation to financial instruments, FRS 102 permits entities an accounting policy choice to apply the recognition and measurement requirements of Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*, IFRS 9 *Financial Instruments* or IAS 39 *Financial Instruments: Recognition and Measurement*. The IASB has made amendments to IFRS 9 and IAS 39 in response to the reform of interest rate benchmarks.

5 The amendments to Section 12 avoid the discontinuation of hedge accounting solely due to uncertainties about interest rate benchmark reform before its economic effects are known. There should be no costs associated with the amendments, as they permit existing hedge accounting to continue and the disclosure requirements are straightforward and minimal. The benefits associated with the amendments include avoiding the costs and disruption of early discontinuation of hedge accounting; discontinuation in these circumstances would:

(a) not provide useful information to users; and

(b) not maintain consistency with IFRS 9 (given that the hedge accounting requirements of FRS 102 are based on IFRS 9).

Conclusion

6 Overall, the FRC believes that the amendments to FRS 102 will have a positive impact on financial reporting.

Feedback Statement

7 The purpose of this Feedback Statement is to summarise the comments received in response to FRED 72 *Draft amendments to FRS 102 – Interest rate benchmark reform*. FRED 72 was issued in July 2019 and the comment period closed on 20 September 2019.

8 The table below shows the number of respondents and analyses them by category.

Table 1: Respondents by category

	No. of respondents
Accountancy firms	6
Accounting professional bodies	3
Other	1
	10

9 FRED 72 posed two questions, and the feedback and FRC response to them are summarised below.

Question 1

> Do you agree with the proposed amendments to FRS 102? If not, why not?

Table 2: Respondents' views on Question 1

	No. of respondents
Agreed	9
Agreed with reservations	–
Disagreed	1
	10

10 The proposals in FRED 72 were based on similar proposals made by the IASB. The majority of respondents agreed with the proposals in FRED 72, although many raised suggestions for detailed improvements, including referencing changes the IASB had indicated that it would make in finalising its proposals, which should also be reflected in the amendments to FRS 102 (as FRED 72 suggested they would). Respondents particularly welcomed the timely response to the issue and agreed with the approach of consulting on the basis of the IASB's Exposure Draft of amendments to IFRS 9.

11 A number of respondents also referred to the need to address the issues that will arise when an interest rate benchmark is replaced with an alternative interest rate (also known as Phase 2 issues). The IASB has started a Phase 2 project, and some respondents suggested the FRC should expedite its own Phase 2 issues, rather than waiting for the IASB to issue an Exposure Draft on Phase 2 before a FRED is developed.

12 The respondent that disagreed with the proposals considered that the primary accounting challenge in relation to interest rate benchmark reform is developing the guidance that supports the transition from existing interest rate benchmarks to alternatives in a manner that prevents disruption to existing hedge relationships and eliminates financial statement volatility when that is not reflective of the economics of the transaction. That respondent suggested identifying overarching principles to address this.

FRC response

13 The FRC confirmed that its approach to this issue is an IFRS-based solution with suitable changes, including simplifications, for entities applying FRS 102. Therefore, a number of changes have been made to the proposals in FRED 72 in finalising the amendments to reflect the changes the IASB made to its proposals in finalising them, as well as respondents' detailed comments on FRED 72.

14 In relation to Phase 2 issues, the FRC again expects to be able to use amendments to IFRS as a suitable basis for the development of amendments to FRS 102 and is likely to adopt a similar approach as it did to these amendments, with a FRED being developed once the IASB has issued an Exposure Draft.

Question 2

> In relation to the Consultation stage impact assessment, do you have any comments on the costs and benefits identified? Please provide evidence to support your views.

Table 3: Respondents' views on Question 2

	No. of respondents
Agreed	6
Disagreed	–
Did not comment[1]	4
	10

15 All of the respondents commenting agreed that the amendments will have a positive impact on financial reporting because discontinuing hedge accounting solely due to uncertainties about interest rate benchmark reform before its economic effects are known would:

(a) not provide useful information to users;

(b) be disruptive and increase the complexity, and therefore the costs, of preparing and using the financial statements; and

(c) not maintain consistency with IFRS 9 (when the hedge accounting requirements of FRS 102 are based on IFRS 9).

FRC response

16 The costs and benefits of these amendments have been included in the Impact Assessment. Overall, the amendments to FRS 102 will have a positive impact on the financial reporting.

[1] Includes those respondents that stated that they had no comments in relation to Question 2 and those that did not address Question 2.

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