

The Future of Financial Reporting

in the United Kingdom and Republic of Ireland

The Key Facts

FREDs 46, 47 and 48

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ACCOUNTING STANDARDS BOARD

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1 Introduction

This booklet summarises the Accounting Standards Board's (ASB) revised proposals for the future of financial reporting standards in the UK and Republic of Ireland.

The ASB issued two Financial Reporting Exposure Drafts, FREDs 43 & 44, in October 2010 and a supplementary FRED 45 in March 2011 setting out proposals for a fundamental overhaul of UK and Republic of Ireland financial reporting standards.

Respondents to FRED 43 to 45 were asked to consider whether the proposals would provide the optimal outcome, or whether a different approach would be better. The ASB, following the feedback received, is now issuing FREDs 46 to 48.

The revised proposals are set out in the following three draft Financial Reporting Standards (FRS):

FRED 46 'Application of Financial Reporting Requirements' (draft FRS 100);

FRED 47 'Reduced Disclosure Framework' (draft FRS 101); and

FRED 48 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' (draft FRS 102).

2 What are the revised proposals?

The revised proposals recommend:

- (a) replacing all extant FRSs, Statements of Standard Accounting Practice and Urgent Issues Task Force Abstracts (current FRSs) in the UK and Republic of Ireland with a single FRS;
- (b) introducing a reduced disclosure framework for the financial reporting of certain qualifying entities; and
- (c) retaining the 'Financial Reporting Standard for Smaller Entities' (FRSSE) and updating it following planned changes at EU level to financial reporting requirements for small companies.

The ASB, consistent with its previous proposals, is proposing an adaption of the IFRS for SMEs to replace current FRSs.

3 What do the changes mean for me?

The ASB's proposals aim to be proportionate to the size and complexity of an entity.

This means there are some choices for you.

Currently applying	Options under the revised proposals	Reduced disclosures
FRSSE	No change	
UK Financial Reporting Standards	Draft FRS 102 (FRED 48)	Available for qualifying entities
Opted to apply EU-adopted IFRS	No change or draft FRS 102	
Required to apply EU-adopted IFRS	No change	

Can I apply the reduced disclosures?

You can apply the reduced disclosures as a qualifying entity if your financial reporting is included in consolidated financial statements that give a true and fair view, and are available publicly.

How do I apply the reduced disclosures?

Reduced disclosures are available for qualifying entities applying the recognition and measurement requirements of EU-adopted IFRS. There are also reduced disclosures for qualifying entities applying draft FRS 102.

4 What are the changes from previous proposals?

The main changes from the proposals in FREDs 43 to 45 include:

The elimination of 'public accountability'

FRED 43 proposed three tiers of entity. The first tier, entities with public accountability, would have applied EU-adopted IFRS. The third tier, entities qualifying as small, would have applied the FRSSE. All other entities (the second tier) would apply FRS based on the IFRS for SMEs.

The ASB received feedback that the cost to certain entities of applying EU-adopted IFRS could not be justified by the benefits. The ASB agreed and decided to eliminate the concept of public accountability. Instead, entities previously considered to have public accountability will apply the FRS applicable in the UK and Republic of Ireland. As a result, the application of EU-adopted IFRS is not extended beyond the requirements of the EU's IAS Regulation.

Changing the proposals in FRED 44 (revised FRED 48)

Following its decision to eliminate the concept of entities with public accountability the ASB has had to extend the accounting requirements proposed in FRED 44 to address the needs of a broader group of preparers. This includes areas such as earnings per share, segmental reporting and improving disclosures for financial institutions.

The ASB also received feedback that the proposals in FRED 44 were an oversimplification. Consequently, the ASB has changed its guidelines for when to amend the IFRS for SMEs.

4 What are the changes from previous proposals? ...continued

Effective date

The proposed effective date has been changed to 1 January 2015 and maintains at least 18 months between the expected date of issue of the standards and the effective date.

I was previously considered publicly accountable: do I still have to apply EU-adopted IFRS?

No, the definition and associated tier system is no longer proposed. However, financial institutions will need to provide additional disclosures if applying draft FRS 102 and are not entitled to the same level of reduced disclosures as other entities. The legal requirement for quoted groups to report under EU-adopted IFRS does, of course, remain.

Where can I find the additional disclosures for financial institutions?

All the requirements for financial institutions are in draft FRS 102. The additional disclosures are in Section 34, Specialised Industries.

5 Why is the ASB making these changes?

Respondents to FREDs 43 to 45 generally supported the ASB's view that current FRSs require a fundamental overhaul. Support for change is evidenced by:

- (a) extensive consultation undertaken by the ASB on the future of financial reporting in the UK and Republic of Ireland;
- (b) the need to update financial reporting for financial instruments: current FRSs permit certain transactions to remain unrecognised that are relevant to the assessment of the financial position of an entity; and
- (c) practical issues associated with maintaining two accounting frameworks, such as the cost associated with training accountants in both IFRS and current FRSs.

6 What is the ASB's objective for this project?

The ASB has identified the following project objective:

To enable users of accounts to receive high-quality, understandable financial reporting proportionate to the size and complexity of the entity and the users' information needs.

In meeting its objective, the ASB will provide succinct financial reporting standards that:

- have consistency with global accounting standards through the application of an IFRS-based solution unless an alternative clearly better meets the overriding objective;
- reflect up-to-date thinking and developments in the way businesses operate and the transactions they undertake;
- balance consistent principles for accounting by all UK and Republic of Ireland entities with pragmatic solutions, based on size, complexity, public interest and users' information needs;
- promote efficiency within groups; and
- are cost-effective to apply.

7 FRED 46 'Application of Financial Reporting Requirements'

FRED 46 provides the revised framework:

- entities required by company law to apply EU-adopted IFRS must do so;
- entities that are not small and are not required to apply EU-adopted IFRS apply the draft Financial Reporting Standard applicable in the UK and Republic of Ireland;
- small entities may apply the FRSSE; and
- qualifying entities may apply the Reduced Disclosure Framework.

FRED 46 also sets out when an entity should comply with a SORP, and certain transition arrangements.

Changes from previous proposals:

The significant change between the proposals in FRED 43 and FRED 46 is the elimination of public accountability as the basis for a differential reporting framework. This would have required all entities with public accountability to apply EU-adopted IFRS, extending it beyond those currently required to do so.

8 FRED 47 'Reduced Disclosure Framework'

FRED 47 sets out a reduced disclosure framework. This allows subsidiaries and ultimate parent entities to prepare financial statements using the recognition and measurement requirements of EU-adopted IFRS but with reduced disclosures.

These entities are required to comply with the formats set out in company law in some instances adjustment may be required to recognition and measurement requirements of EU-adopted IFRS.

Changes from previous proposals:

The changes include:

- extension of the reduced disclosure framework to ultimate parent entities;
- developing principles for determining which disclosures should be reduced as new IFRSs are introduced; and
- prohibiting qualifying entities that are also financial institutions from using the disclosure exemptions relating to IFRS 7 'Financial Instruments' and IFRS 13 'Fair Value Measurement'.

9 FRED 48 ‘The Financial Reporting Standard applicable in the UK and Republic of Ireland’

FRED 48 ‘The Financial Reporting Standard applicable in the UK and Republic of Ireland’ aims to replace all extant financial reporting and accounting standards.

The ASB believes that FRED 48 will provide succinct and understandable financial reporting requirements. Based on the IFRS for SMEs, the draft FRS will move the UK and Republic of Ireland to a single international financial reporting framework.

Changes from previous proposals

The changes include:

- broadening the scope of the draft FRS:
to address the needs of a broader group of entities (i.e. those entities that under the previous proposal would have had ‘public accountability’), for example in relation to earnings per share, interim reporting and improving disclosures for financial institutions;
- widening the guideline for amending the IFRS for SMEs:
following feedback on its previous proposals, certain accounting treatments have been introduced that are consistent with current FRS and EU-adopted IFRS, such as: revaluation of tangible and intangible fixed assets, and capitalisation of borrowing costs and carrying forward certain development costs; and
- fitting the requirements more closely with company law:
the majority of the presentation requirements for the income statement and balance sheet are replaced with formats set out in company law. To improve consistency the formats are extended to all reporting entities.
- other changes in response to feedback on FRED 44 include:
 - o revised proposals for accounting for taxation;
 - o updating the consolidation requirements and providing some relief from consolidation for investments in subsidiaries held as part of an investment portfolio;
 - o introducing an option to recognise grant income on a systematic basis over the life of the grant; and
 - o introducing accounting requirements for retirement benefit plans.

10 Public benefit entities

FRED 45, which included requirements specific to public benefit entities, has been incorporated into FRED 48. Areas that apply only to public benefit entities are identified by the prefix “PBE”.

Changes from previous proposals

- Clarification is provided on the recognition of income from donations of goods or services (incoming resources for non-exchange transactions).

Recognition should include consideration of whether the resources can be reliably measured and whether the benefit of recognition outweighs the costs.

- An extension to all entities of the following proposals:
 - o property held for the provision of social benefits;
 - o impairment of assets held for service potential, to be measured using a value in use based on the present value of future service potential; and
 - o funding commitments.

11 Small entities

The ASB is proposing to retain the FRSSE and to consult again on how to update it following the European Commission's planned changes to the accounting requirements for smaller entities.

The European Commission is proposing a new Accounting Directive, which will:

- (a) raise the thresholds for defining small companies; and
- (b) reduce the mandatory information provided in small company financial statements, but require specific disclosures of commitments, borrowings and arrangements not included in the balance sheet.

In addition, agreement has been reached on legislation to give Member States an option to treat micro-entities as a separate category of company and to exempt them from certain accounting requirements. This will be integrated into the new Accounting Directive.

The ASB will consequently need to consult on how best to amend the FRSSE to accommodate the above changes.

12 Statements of Recommended Practice

The ASB is proposing the SORPs be updated as follows:

SORP	ASB recommendation
Financial reports of pension funds	Update for the draft FRS 102 (FRED 48)
Accounting for oil & gas	
Limited liability partnerships	
Investment companies	
Authorised funds	
Accounting by registered social housing providers	
Accounting and reporting by charities	
Accounting for further and higher education	
Accounting for insurance business	A separate consultation is being undertaken on the future of this SORP.
Leasing	Withdraw when the proposals in the FREDs become effective.
Banking segments	

13 Impact of the proposals

In making its revised proposals the ASB has carefully considered the comments received in previous consultations. It believes the resultant changes will:

- reduce the costs of its proposals because the elimination of the ‘public accountability’ definition avoids extending the application of EU-adopted IFRS; and
- permit currently available accounting treatments, thereby reducing the cost of transition.

Benefits of proposals

The ASB considers the proposals will give rise to the following benefits:

- The reduced disclosure framework will allow consistency within groups, reducing disclosure requirements and therefore costs.
- FRED 48:
 - o is a proportionate solution written specifically for smaller and medium-sized entities whilst maintain the quality of financial reporting; and
 - o will improve accounting for financial instruments.
- The move to an internationally based framework should assist in the education, training and intellectual mobility of accountants.

Costs of proposals

The ASB has carefully considered the costs of its proposals and has sought to find solutions that are cost effective whilst maintaining the quality of financial reporting.

The most significant costs of applying the proposed framework are likely to be incurred by entities that have a significant number of complex transactions (particularly financial instruments), but had previously applied neither EU-adopted IFRS, nor FRS 26.

14 Request for comments

The ASB **welcomes comments** on any aspect of the proposals.

A full explanation of the proposals and a number of **specific questions** are set out in the FREDs.

Comment letters should be received by **30 April 2012**

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