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Our ref blp/kaf/815

For the attention of Jenny Carter

27 April 2012

Dear Sirs

Revised Financial Reporting Exposure Drafts: The Future of Financial Reporting in the UK and Republic of Ireland

We welcome the opportunity to comment on the Revised Financial Reporting Exposure Drafts: The Future of Financial Reporting in the UK and Republic of Ireland ('the FREDs').

We support the changes to the previous proposals, and consider that the revised proposals are broadly appropriate and proportionate to the needs of preparers and users of financial statements in the UK. However, in order to seek to make the final standards as operational as possible and to achieve minimal diversity in practice, we have a number of detailed observations on the proposals. We set out our responses to the specific questions raised in the FREDs in Appendix 1 to this letter. In Appendices 2 to 4 we set out our detailed comments on the FREDs.

If you wish to discuss any of the points raised, please contact Lynn Pearcy on 0207 694 8075 or Karen Faragher on 0121 232 3874.

Yours faithfully

KPMG LLP

KPMG LLP

Enclosures:
Appendix 1 Responses to specific questions raised in the FRED
Appendix 2 Comments in relation to FRED 46
Appendix 3 Comments in relation to FRED 47
Appendix 4A Key comments in relation to FRED 48
Appendix 4B Other comments in relation to FRED 48

Appendix 1

Responses to specific questions raised in the FREDs

Q 1 The ASB is setting out the proposals in this revised FRED following a prolonged period of consultation. The ASB considers that the proposals in FREDs 46 to FRED 48 achieve its project objective: To enable users of accounts to receive high-quality, understandable financial reporting proportionate to the size and complexity of the entity and users' information needs. Do you agree?

Yes, we agree that the latest proposals achieve the ASB's project objective.

Q 2 The ASB has decided to seek views on whether: As proposed in FRED 47: A qualifying entity that is a financial institution should not be exempt from any of the disclosure requirements in either IFRS 7 or IFRS 13; or Alternatively: A qualifying entity that is a financial institution should be exempt in its individual accounts from all of IFRS 7 except for paragraphs 6, 7, 9(b), 16, 27A, 31, 33, 36, 37, 38, 39, 40 and 41 and from paragraphs 92-99 of IFRS 13 (all disclosure requirements except the disclosure objectives). Which alternative do you prefer and why?

Subject to the comment in the following paragraph, we prefer the approach proposed in FRED 47, as this approach has the advantage of simplicity of application and is consistent with the overall requirement for the financial statements of financial institutions to give a true and fair view. Further, we are not clear that the alternative exemptions suggested in Question 2 above would be consistent with the decisions made when deciding which of the financial instruments disclosure requirements should be included in FRS 102. For instance, we would not expect financial institutions to be exempt from the requirements in paragraphs 8, 20 and 21 of IFRS 7 (which are included in section 11 of FRS 102, and from which qualifying entities applying FRS 102 which are financial institutions are not exempt). Any alternative to that proposed in FRED 47 should be consistent with the approach applied under FRS 102.

We note that the scope of IFRS 13 is wider than financial instruments, for example it includes disclosures in relation to investment property. It appears illogical to provide an exemption from such disclosures for qualifying entities which are property companies (see paragraph 8(e) of draft FRS 101) but not for those which are financial institutions. We therefore suggest that the

Board should consider introducing consistent disclosure exemptions in this regard for financial institutions and non-financial institutions.

Please also see our general comment on FRED 46 in relation to the need for entities to consider the wider requirement for the financial statements to present a true and fair view when considering which disclosure exemptions should be taken advantage of. For example it may not be appropriate for property companies always to take full advantage of the exemption potentially afforded to them under paragraph 8(e) of FRS 101.

Q 3 Do you agree with the proposed scope for the areas cross-referenced to EU-adopted IFRS as set out in section 1 of FRED 48? If not, please state what changes you prefer and why.

Yes, we agree with the proposed scope for the areas cross-referenced to EU-adopted IFRS as set out in section 1 of FRED 48. However, please see our comments on Q5(b) below and in Appendix 4 to this letter regarding the potential inclusion of additional cross-references to IFRIC 12 and IFRIC 4.

Q 4 Do you agree with the definition of a financial institution? If not, please provide your reasons and suggest how the definition might be improved.

We broadly agree with the proposed definition of a financial institution, subject to the following points of detail:

- The definition of a bank appears to be consistent with that in the glossary to the FSA Handbook, which is different from the definition of a banking company in section 1164 of the Companies Act 2006. The latter definition is potentially wider than the FSA definition, as it does not require a company to be a credit institution in order to be a banking company. We suggest that consideration should be given to whether this is expected to present an issue in practice (we are not aware that this will be the case).
- “Credit institution” and “full credit institution” are not defined in parts (a)(i) and (a)(ii) of the proposed definition. A definition of a credit institution is given in section 1173(1) of the Companies Act 2006 and the glossary to the FSA Handbook includes a definition of a full credit institution; if these definitions are intended to apply they should be referred to in the definition of a financial institution.
- Part (c) refers to an entity that undertakes the business of “effecting or carrying out” insurance contracts. It is unclear whether this is intended to be wider than the definition of an insurance company in section 1165 of the Companies Act 2006, and hence capture entities which act as insurance agents or entities which issue contracts that meet the IFRS 4 definition of insurance contracts (for example roadside assistance, some utility services and certain warranty companies); this should be clarified in the final standard.
- Part (d) refers to a “stockbroker”. It is unclear how this is defined and whether it includes broker-dealers.

- The definition does not make any reference to principal activities (or similar wording). This suggests that an entity which is involved to any extent in any of the activities listed is caught by the definition. If this is the case, it may be helpful to clarify this within the definition.

Please also see our comments in Appendix 4 to this letter in relation to the lack of a definition of a financial institution group and how the definition of a financial institution interacts with the financial instrument disclosures set out in Section 34 of draft FRS 102.

> Q 5 In relation to the proposals for specialist activities, the ASB would welcome views on:
> (a) Whether and, if so, why the proposals for agriculture activities are considered unduly arduous? What alternatives should be proposed?
> (b) Whether the proposals for service concession arrangements are sufficient to meet the needs of preparers?

(a) Agriculture activities

Whilst we acknowledge the inconsistency between the treatment of inventories under section 13 of draft FRS 102 and the treatment of biological assets and agricultural produce at the point of harvest under section 34 of the draft standard, this inconsistency is also present under full EU-IFRS. We do not comment on the availability of fair values for biological assets and agricultural produce at the point of harvest.

(b) Service concession arrangements

As we noted in our response to FREDs 43 and 44, in our view the proposals for service concession arrangements are insufficiently clear as drafted. Our experience in the application of IFRIC 12 under EU-adopted IFRSs indicates that in practice the entire scope guidance of IFRIC 12 needs to be considered carefully when determining whether arrangements with government bodies fall within its scope. From applying this detailed guidance, it is evident that only certain restricted types of arrangements are intended to be accounted for under IFRIC 12. The omission of this detailed scope guidance from FRS 102 may therefore result in a lack of clarity over the arrangements falling within the scope of this section of the standard. We repeat our previous comments for reference:

It is unclear whether the application of paragraphs 34.12 to 34.16 will necessarily result in consistent application of scope or accounting treatment when compared with IFRIC 12, particularly for entities that are not currently familiar with IFRIC 12. For example:

- There is no acknowledgement of the public service nature of the obligations undertaken by the operator in a service concession arrangement to distinguish it from normal trading with public bodies;
- It is unclear whether the scope of these paragraphs is the same as IFRIC 12 – there is no equivalent paragraph in draft FRS 102 to IFRIC 12.6, which refers to arrangements where

the infrastructure is used in a public-to-private concession arrangement for its entire useful life;

- Whilst the guidance indicates that a financial asset and/or intangible asset should be recognised it is unclear as to whether the initial recognition of either or both type of asset is revenue-generating or how the difference between fair value and cost should be recognised. Although paragraph 34.16 requires revenue to be recognised by the operator for the services it performs, it is unclear whether the recognition of a financial or intangible asset is considered to be a service under this paragraph; and

- No guidance is provided regarding the use of the grantor's existing infrastructure in the arrangement.

The basis for conclusions of the IFRS for SMEs does not suggest that different accounting treatment for service concession arrangements under the IFRS for SMEs was the intention of the IASB. Given that there is no requirement to look to full EU-adopted IFRSs in developing a suitable accounting policy, we consider that the current drafting of this section may result in diversity in practice in the UK. Therefore, we suggest either including fuller guidance consistent with IFRIC 12 in FRS 102, to include clear principles, or the inclusion of a footnote cross-referring to IFRIC 12 as a source of guidance in developing accounting policies in relation to service concession arrangements.

Q 6 The ASB is requesting comment on the proposals for the financial statements of retirement benefit plans, including:
(a) Do you consider that the proposals provide sufficient guidance?
(b) Do you agree with the proposed disclosures about the liability to pay pension benefits?

(a) The requirements for retirement benefit plans in draft FRS 102 are drawn largely from IAS 26 and include a number of requirements for non-financial information to be included either in the financial statements or in a report alongside the financial statements. These requirements appear out of place compared with the approach taken elsewhere in the standard for the financial statements of other entities and it is unclear what authority an accounting standard carries in relation to reports that do not form part of the financial statements.

In the UK most of this information is required by law to be disclosed in a trustees' report and therefore it is not necessary for it to be included in FRS 102. In addition, it is currently dealt with in the pension SORP and we assume that this will continue to be the case. We would therefore recommend that all references to disclosure of non-financial information are removed from the final standard.

Please also see our comments on section 34 of draft FRS 102 in Appendix 4 to this letter.

(b) The disclosure requirements about the liability to pay pension benefits are largely drawn from IAS 26 with some tailoring to recognise existing reporting of actuarial information in UK pension plans as recommended by the current pensions SORP. However, the current drafting is not wholly consistent with either IAS 26 or current UK practice, which recommends disclosing the annual Summary Funding Statement (SFS) which is sent to all members and comments on the relationship between plan assets and liabilities on an ongoing and buy-out basis. There are also differences between disclosures under IAS 26 and the SFS. For example IAS 26 requires the disclosure of vested and non-vested benefits (please see our comments on section 34 of draft FRS 102 in Appendix 4 to this letter) yet this is not required for SFS, and the SFS includes liabilities on a buy-out, or wind up, basis, and this is not required under IAS 26. We therefore recommend that FRS 102 should simply require pension liability information to be provided either in the notes to the financial statements or in a separate report alongside the financial statements (without setting out detailed requirements for that disclosure), and that the pension SORP should explain how a plan should or might meet the requirements of FRS 102.

Q 7 Do you consider that the related party disclosure requirements in section 33 of FRED 48 are sufficient to meet the needs of preparers and users?

Subject to the following comment, we agree that the related party disclosure requirements in section 33 are sufficient to meet the needs of preparers and users.

We note that the wording of the exemption from disclosure of certain intra-group transactions is not consistent between paragraph 22(m) of FRED 46 (proposed amendments to the FRSSE), paragraph 8(l) of FRED 47 and paragraph 33.1A of FRED 48. The wording in FREDs 46 and 48 is based on the legal wording of the exemption, whereas that in FRED 47 is based on current FRS 8. Whilst the former is technically accurate, it does not provide clarity over the scope of the exemption. The exemption should be clearly and consistently worded to avoid uncertainty in practice over the appropriate application of the exemption. For example, it is unclear what “by such a member” is intended to mean (for example, is the subsidiary required to be wholly owned by the company which is the counterparty to the transaction or simply by any group company?). If the wording of the exemption remains as currently drafted, a straight reading of the exemption would lead, for example, to the conclusion that transactions between two fellow subsidiaries owned by the same parent entity would be disclosable. This would be a change from the widely held interpretation of the current exemption in FRS 8; if this is the Board’s intention, it should be explained.

Q 8 Do you agree with the effective date? If not, what alternative date would you prefer and why?

We agree with the proposed mandatory effective date.

As regards early adoption:

- We note that the wording of the preamble to question 8 in the document *Part One: Explanation* has been revised in the online version of that document to clarify that early adoption of draft FRS 101 is permitted subject to the same conditions as apply to the early adoption of draft FRS 102.

- We consider that it would be appropriate to permit early adoption for accounting periods ending (rather than beginning) on or after the date of issue of the final standards.
- It is unclear why it is necessary for early adoption by a PBE to be subject to an additional requirement that it must apply a PBE SORP developed under the new standards as we would not expect such an entity to wish to apply the standards in the absence of such a SORP. If the reference to SORPs is retained, we note the following:
  - We suggest that references to “a” public benefit entity SORP (for example in paragraph 1.14 of FRED 48) should be to “any relevant” SORP to make it clearer that the entity should apply only the SORP relevant to its circumstances.
  - Consideration should also be given to widening the reference to SORPs developed in accordance with draft FRSs 100, 101 and 102 to *any* entity within the scope of a SORP, rather than limiting this to public benefit entities.

Q 9 Do you support the alternative view, or any individual aspect of it?

We do not support the alternative view, or any individual aspect of it.

Appendix 2

Comments in relation to FRED 46

Key comments

- Paragraph 22(j) refers to the useful life of goodwill and intangible assets being five years when a "reliable estimate" cannot be made of the useful life of the asset. We note that the term "reliable estimate" does not appear in the applicable EU Accounting Directive, and that the Directive refers to a maximum life of five years except when the useful life of goodwill exceeds this and is appropriately disclosed. No such legal restriction is imposed on other intangible assets. It would appear that the wording of the amendment to the FRSSE is more onerous than required by law and also makes no reference to a <u>maximum</u> of five years. Consideration should be given to aligning the wording more closely with the legal requirement. Please see also our comments on sections 18 and 19 of FRED 48 in this respect.
- Consideration should be given to including a requirement for entities to consider the overriding requirement for financial statements to give a true and fair view when considering which of the disclosure exemptions of draft FRSs 101 and 102 to apply. For example, it might be considered inappropriate for a subsidiary treasury company always to take full advantage of the financial instrument disclosure exemptions potentially available to it.

Other comments

- Paragraph 2 could usefully clarify that FRS 100 does not apply to financial statements of public sector entities (as defined).
- It would be preferable to include definitions in only one location in this standard (preferably in its glossary) to avoid the risk of differences between the definitions (please see next comment). For example the definitions of a financial institution, qualifying entity and public benefit entity appear in both the glossary and the body of the standard.
- The definition of a qualifying entity in paragraph 4:
  - is inconsistent with that given in the glossary to FRED 46. Paragraph 4 refers to financial statements "which are intended to give a true and fair view", whereas the glossary states "which give a true and fair view". A consistent definition should be used, which in our view should be that given in paragraph 4 in order to make it clear that a modification of an audit opinion on the consolidated financial statements in question does not result in the disclosure exemptions being unavailable to group entities.
  - does not specify the meaning of "in which that member is consolidated": it is unclear whether this should be full consolidation or whether, under frameworks (including FRS 102) that permit such approaches, proportional consolidation, equity accounting, or recognition as a single asset at fair value would be sufficient. We note that the terminology used is not consistent with either s474 of the Companies Act 2006 (which

defines "included in the consolidation" explicitly as full consolidation) or the more expansive "dealt with on a consolidated basis" in the Partnership (Accounts) Regulations 2008 (which would include proportional consolidation and equity accounting). Further, it is unclear whether the criteria would be met if no consolidated financial statements were prepared because all subsidiaries were eligible to be excluded from consolidation and included at fair value through profit or loss.

- in order to clarify that the parent of the "group" rather than the "member" is required to prepare publicly available consolidated financial statements, might instead be worded (subject to the preceding comment):

  "A qualifying entity is a member of a group, where the parent of that group prepares publicly available consolidated financial statements, which are intended to give a true and fair view, in which that member is consolidated."

- Paragraph 6 and the glossary to FRED 46 include a definition of a public benefit entity. We make the following comments in this respect:
  - As noted in our response to FRED 45, it would be helpful to include examples of the types of entity caught by this definition, for example, charities, registered social landlords and higher and further education institutions.
  - The draft application guidance on the definition of a public benefit entity included in FRED 45 has not been included in FRED 46; such guidance may be useful.
  - It is unclear whether a Community Interest Company would fall automatically fall within the definition of a public benefit entity. CICs may pay dividends subject to a cap set by the CIC Regulator.
  - It would be useful to clarify whether subsidiaries of a PBE parent would also be considered to be PBEs or whether it is the status of the individual entity alone that is relevant. This is relevant in considering, for example, the accounting for concessionary loans, whereby the accounting treatment may differ between a PBE parent and its trading subsidiary.
  - Similarly, it is unclear how transactions of a PBE subsidiary should be accounted for in the consolidated accounts of a non-PBE parent, if those transactions are accounted for under the PBE-specific requirements of FRS 102.
- The footnote to paragraph 7 regarding the financial statements of charities should also refer to s403(3) of the Companies Act 2006, which states that a charity's group accounts must be Companies Act group accounts. This reference is already included in paragraph A2.12.
- Paragraph 16(d) refers to the transitional arrangements "set out in the FRSSE". It is unclear what these arrangements are since the FRSSE does not include any specific transitional arrangements. This requirement should be clarified.

- Consideration should be given to defining the "date of transition" as referred to in paragraph 17 – presumably this is intended to have the same meaning as in IFRS 1 and FRS 102, although this is not clear.
- It is unclear why the references to UITF Abstracts have been deleted from paragraphs 22(b), (d), (f) and (g) but not from paragraph 22(e). If new UITF Abstracts may be issued in the future, these references should be retained throughout. If not, then all references should be deleted consistently.
- It is unclear why the text "when preparing financial statements intended to give a true and fair view of the financial position and profit and loss of the entity" has been deleted from the end of paragraph 22(f).
- It is unclear why the final paragraph in paragraph 22(g) does not refer to FRS 101 for completeness.
- Please see our comments on Question 7 in Appendix 1 to this letter in relation to paragraph 22(m).
- It is unclear why the exemption from disclosing in consolidated financial statements those related party transactions which have been eliminated on consolidation has been deleted from the FRSSE by paragraph 22(n).
- Paragraph AG 2 states that FRS 101 permits exemptions from disclosure "where equivalent disclosures are included…". Not all of the proposed disclosure exemptions require equivalent disclosures to be made hence this should presumably read "…permits exemptions from disclosure, in some cases subject to equivalent disclosures being included …".
- Paragraphs AG2 and AG8 should clarify that equivalence is also relevant to accounts prepared under FRS 102.
- AG 8 and 9 could usefully discuss whether the consideration of equivalence applies only to the disclosures made in the consolidated financial statements, regardless of the recognition and measurement requirements applied to the transactions in question.
- It would be helpful if AG10 clarified whether transactions which eliminate on consolidation which might be within the scope of the disclosure exemptions are exempt from disclosure in the financial statements of a qualifying subsidiary if the consolidated financial statements of the parent include similar disclosures in relation to different transactions (for example intra-group disposals or acquisitions of businesses).
- Similarly, we assume that the disclosure exemption is not available if the disclosures in question are material to the individual group entity but are not material to the group and therefore equivalent disclosures are not given in the consolidated financial statements; this should be clarified.
- A1.2 states that separate financial statements are a type of individual accounts. However, neither term is defined in this glossary. We also note that the cross-reference to IFRS (which should be to EU-adopted IFRS) in relation to separate financial statements should refer to the

definition given in the glossary to FRS 102. The same comments apply in relation to the reference to individual accounts in the glossary to draft FRS 102 (the location of the latter within that glossary should also be reconsidered; it should be presented either in alphabetical order or within the definition of separate financial statements rather than being included at the end of the glossary).

- Paragraph A2.4 refers to the IAS Regulation. The inclusion of the word "broadly" in the footnote suggests a wider application of the Regulation than the group accounts of entities with securities listed on a regulated market, which is not the case. If this is meant to capture, for example, AIM companies, we suggest that a fuller explanation should be given in A2.4, i.e. that certain exchanges also require group accounts to be prepared in accordance with full EU-IFRSs.
- Paragraphs A2.5 and A2.7 refer to entities being "permitted" and "electing" to apply the small companies regime. This should instead refer to entities being "subject to" the small companies regime since there is no election to be made.
- The reference to "for reasons of public interest" should be deleted from paragraph A2.9 since the reason for the exclusion of these entities from the small companies regime is not given in the Companies Act 2006.
- Paragraph A2.14(c) does not accurately reflect the requirements of s407(5) of the Companies Act 2006. The Act permits inconsistency in this situation only between the individual accounts of the parent and those of its subsidiaries; the consistency requirement still applies to the individual accounts of the subsidiaries.
- Paragraph A2.14 should also clarify that the consistency rule does not apply to the individual accounts of subsidiaries that are not prepared under the Companies Act 2006 (e.g. certain partnerships, overseas companies) (see section 403(3) of the Act).
- Paragraph A2.17 should also list section 236 (disclosure of qualifying indemnity provisions) of the Companies Act 2006.
- It is unclear why the table in A2.19 does not refer to the pension scheme SORP in the same way that the Charities SORP is referred to. Also, we note that the Charities Act 2011 supersedes the Charities Acts 1993 and 2006 with effect from 14 March 2012; we suggest that the text of A2.19 should be updated to reflect this. The same comments apply to paragraph A3.30 of FRED 48.

Appendix 3

Comments in relation to FRED 47

Key comment

- Paragraph 7(c)(i) requires precise paragraph references to the relevant standard to be disclosed when taking advantage of the disclosure exemptions. We question whether this is of benefit to the user of the financial statements or whether it serves only to add clutter. We suggest that disclosure of the nature of the exemptions taken might be more appropriate. The same comment applies to paragraph 1.14(c) of FRED 48.

Other comments

- Neither "qualifying entity" nor "financial institution" appears to be defined in this standard. We suggest that paragraph 4 is expanded to cross-refer to the relevant definitions included in FRS 100.
- The disclosures required by paragraph 36(4) of Schedule 1 of the Regulations are based on IFRSs endorsed by the EU on or before 5 September 2006, hence it is unclear why requirements of IFRS 7 which were endorsed after that date are included in paragraph 4 of draft FRS 101. Also, since the disclosures under IFRS 7.27B are not required to be given, it is unclear why reference to IFRS 7.27A is included in this paragraph.
- A cross-reference from paragraph 5 to paragraph 7 might be helpful in order to clarify that financial institutions must meet the same criteria as other entities in order to be eligible for the reduced disclosure framework.
- It appears from paragraphs 5 and 8(g) that financial institutions which are qualifying entities may be exempt from the capital disclosures required under IAS 1.134 to 136. We do not consider such an exemption to be appropriate, particularly for banks and insurers.
- As noted in our response to FREDs 43 and 44, paragraph 7(a) of FRS 101 should provide more detail on the required process as regards shareholder consent for the application of the reduced disclosure framework. There is no indication given of whether there is a specified timeframe in which the shareholders in question may object, and it is not clear whether a formal indication that they do not object is sufficient, or whether a nil response can be taken to indicate acceptance.
- Paragraph 7(b) might more usefully read "…it otherwise applies <u>as its financial reporting framework</u> the recognition, measurement and disclosure requirements of EU-adopted IFRS…" to avoid any uncertainty over the applicability of the reduced disclosure framework in the event that the financial statements did not in fact comply with one or more of the requirements of EU-adopted IFRSs.

- It is unclear what arrangements are intended to be caught by the reference in paragraph 8(a) to "group arrangements". This term is not defined in IFRS 2 (paragraphs 43A-D of that standard refer to "arrangements amongst group entities"). Also paragraph 8(a) refers to "a group arrangement…of an entity other than the parent"; it is unclear whether the reference to "parent" is to the entity's ultimate parent, immediate parent or any parent. The fact that the exemption is conditional on the provision of equivalent disclosures in the consolidated financial statements might imply that "parent" in this case means the parent which heads the consolidated group in question but this is unclear and we suggest that the wording of this exemption should be clarified.
- It is unclear why paragraph 8(a) provides an exemption from disclosure of the total share-based payment expense under IFRS 2.51(a).
- Paragraph 8(h) should also, for completeness, refer to paragraphs 10(d) and 111 of IAS 1 in relation to cash flow statements.
- Please see our comments on Question 7 in Appendix 1 to this letter in relation to paragraph 8(l). Paragraph A2.5 of FRED 47 may also need to be updated accordingly.
- It is unclear how the revisions to IFRS 1.D17 set out in AG 1(b) might apply to a qualifying entity that is a parent since it will not have prepared consolidated financial statements in accordance with FRS 101 (since that standard applies only to individual financial statements). If the references to consolidated financial statements are intended to be to any consolidated financial statements prepared by the entity under full EU-IFRSs, this should be stated.
- Paragraph AG1(o) might provide more clarity if the final part of the sentence was retained but revised to specifically state that grants <u>are not deducted</u> in reporting the related expense.
- Paragraph A1.3 should repeat the items included in A2.17 of FRS 100, or include a cross-reference to that paragraph.
- Paragraph A1.8 could helpfully clarify that in the case of conflict, the presentation requirements of the Companies Act take precedence over those of EU-adopted IFRSs. It would be helpful also to clarify whether IFRS terminology may be used in place of Companies Act terminology (for example: revenue rather than turnover; receivables rather than debtors; inventories rather than stocks). Consideration might also be given to including in FRS 101 an amendment to IAS 1 dis-applying the format requirements of IAS 1 (consistent with the approach applied in FRS 102).

Appendix 4A

Key comments in relation to FRED 48

Section 3 – Financial statement presentation

- As noted in our comments on FRED 44, paragraph 3.2 refers to the "fair presentation" of the financial statements. We suggest that a footnote should be added, or the definition of "fair presentation" in the glossary expanded, to clarify that for UK entities "fair presentation" is considered to be the same as a "true and fair view". Consideration should also be given to retaining the Appendix to the Foreword to Accounting Standards dealing with the true and fair requirement and the true and fair requirement revisited, perhaps as an appendix to FRS 100.
- Paragraph 3.8 refers to management being required to consider going concern for at least twelve months from the reporting date. In our view, it would be preferable to retain the current FRS 18 reference to "foreseeable future" as a minimum, or to refer to twelve months from the date of approval of the financial statements, rather than introducing a specific minimum period which is less than the period required to be considered under International Standards on Auditing (UK and Ireland).

Sections 4 and 5 – Statement of financial position and statement of comprehensive income and income statement

- As noted in our comments on paragraph A1.8 of FRED 47, it is unclear whether FRS 102 terminology for individual line items may be used in place of Companies Act terminology (for example: revenue rather than turnover; receivables rather than debtors; inventories rather than stocks). We note that the Appendix to section 5 uses Companies Act terminology for the individual line items; it would be helpful to clarify whether this approach is mandatory and, if so, it would be helpful to align the terminology in FRS 102 with that in the Act (or, as a minimum, include a cross-reference to Appendix II to the standard within section 3 (and/or sections 4 and 5) of the standard).
- We suggest that the Companies Act accounts formats should be included as an Appendix to the standard for ease of reference for non-Companies Act entities which will be required to apply these formats (with which they may not be familiar) under paragraph 4.2 of the standard.
- Paragraph 4.7 should clarify that the unconditional right should exist as at the reporting date (as FRS 25.50A) in order to avoid this being read as permitting a liability renegotiated after the reporting date to be classified as non-current.

Section 7 – Statement of cash flows

- Paragraph 7.10 discusses the gross presentation of cash flows. By not including an equivalent to IAS 7.22 to 24 regarding when netting of cash flows is permitted, the effect of this paragraph is not to allow any netting. This is a stricter approach than that adopted under IAS 7 and may give rise to problems for some entities e.g. those financial institutions that rely upon the exemptions from gross presentation given in IAS 7.24.

- We note that the requirement in FRS 1.36 for insurance companies and groups other than mutual life assurance companies not to include cash flows relating to their long-term business in a cash flow statement, other than transfers into and out of the long-term funds, has not been retained. We suggest that, given the retention of the exemption for mutual life assurance companies from the requirement to present a cash flow statement in FRS 1, it would be appropriate to also retain the requirement of FRS 1.36.

Section 9 – Consolidated and separate financial statements

- The wording of paragraphs 9.2 and 9.3 does not identify all circumstances in which a consolidation may not be required to be prepared under the Companies Act. For example, the exemption available to small groups (as defined in the Act) is not mentioned. We suggest that all exemptions should be dealt with in this section in order to avoid the situation whereby the requirements of the standard are more onerous than those of the Act.

- We note that the wording of paragraph 9.9A could result in this paragraph applying to certain interests in subsidiaries held by pension plans preparing accounts under FRS 102. (This comment applies also to paragraphs 14.4B and 15.9B regarding associates and joint ventures, respectively.) We are unclear whether this was the intention of the Board but believe that this would be the appropriate treatment where the subsidiary is held for investment purposes, as most such subsidiaries would be. If so, it would be helpful to cross-refer to this paragraph from the retirement benefit plan financial statement requirements in section 34.

- It is unclear from paragraph 9.19 how an investment in an associate or a jointly controlled entity is measured when the investment arises following a partial disposal of an interest in a former subsidiary. The paragraph refers only to the initial measurement of a financial asset remaining following such a disposal.

- Paragraph 9.25 requires an entity that is not a parent to apply paragraphs 2.53 to 2.55 to ESOPs. No equivalent requirement is given for the separate financial statements of an entity that is a parent; in our view the same requirement should apply regardless of whether or not the entity is a parent.

- It is unclear why the accounting policy choices available in respect of accounting for interests in associates and jointly controlled entities differ between the separate financial statements of a parent (paragraph 9.26) and the accounts of an entity that is not a parent (paragraphs 9.25, 14.4 and 15.9), i.e. why fair value through profit or loss is not available to non-parents but is available in the separate financial statements of parent entities. The accounting policy choices should be aligned or an explanation given for the difference.

Section 11 – Basic financial instruments

- Paragraph 11.6(d) states that commitments to make a loan to another entity are within the scope of section 12, i.e. measured at fair value. This would be a change to current practice for financial institutions, since most commitments to receive and make loans are usually excluded from IAS 39. We suggest that this requirement should be reconsidered given that some financial institutions will now be within the scope of draft FRS 102.

- As currently worded, paragraph 11.8(d) would also include investments in preference shares that are classified as debt instruments by the issuer. It is therefore unclear whether the holder should consider such investments under paragraph 11.9 or under paragraph 11.14(c). It would be logical to have no difference in the accounting treatment between, say, a fixed-term fixed-rate preference share and a bond with the same features. However, this would require updating the wording of paragraph 11.8(d) to exclude debt instruments from that paragraph. If the intention is to treat investments in such preference shares under 11.14(c), then the implication would be that they would generally need to be fair valued through profit or loss, as we would expect their fair value to be reliably measurable.
- It is also unclear how the issuer should account for preference shares that are classified as debt instruments under section 22, i.e. whether these would fall under the requirements of 11.8(b). This would result in fair value measurement for preference shares that fail any of the four conditions under 11.9, for example preference shares where the coupon is linked to the issuer's profits. This would represent a difference to the requirements of IFRS 9 and result in the recognition of fair value movements due to changes in own credit risk.
- Paragraph 11.12 deals with the initial recognition of financial assets and liabilities. We note that settlement date accounting for regular way purchase or sale of financial assets is not discussed in draft FRS 102, and hence we assume that the standard requires trade date accounting. This should be reconsidered now that some financial institutions will be within the scope of the standard since IAS 39 permits a choice of trade or settlement date accounting.

Section 12 – Other financial instruments issues

- Paragraph 12.18(a) – for the sentence to make sense, the word 'for' needs to be inserted between 'or' and 'a' at the end of the second line. We also assume that the semi-colon after "financial asset" should be positioned after "financial liability" as all hedging instruments should be expected to be highly effective in offsetting the hedged risk. Further, consideration should be given as to whether the reference to a "financial asset" or a "financial liability" in relation to the hedge of a foreign exchange risk in a net investment in a foreign operation is sufficiently precise; the other hedging instruments listed will also be financial assets or liabilities and the current drafting is unclear as to whether the additional hedging instruments in relation to net investment hedge accounting must be a specific type of financial asset or liability. (We understand that the intention was to include foreign currency borrowings within the list of permitted hedging instruments for this purpose.)
- We note that the Board expects to consult on the hedge accounting requirements of the draft standard following the finalisation of IFRS 9. We nevertheless note that the requirement in paragraph 12.18(d) for the hedging instrument to have a maturity date no later than that of the hedged item may be unduly onerous. For example, if an entity uses standardised contracts (e.g. exchange-traded futures) for hedging and only month end futures contracts can be obtained, it would be logical to hedge a $ sale that is forecast to occur shortly before the end of July with a futures contract expiring on 31 July (rather than 30 June).

Sections 14 and 15 – Investments in associates and joint ventures

- Please see our comments on paragraph 9.26 above.

- It is unclear whether paragraph 14.4B applies only to consolidated financial statements, or also to accounts of a non-parent and/or the separate financial statements of a parent. We assume the former but this should be clarified in the final standard and any amendments to paragraphs 14.4 and 14.4A made as necessary (e.g. "Except as required by paragraph 14.4B…"). The same comment applies in respect of paragraph 15.9B.

Section 17 – Property, plant and equipment

- It is unclear why the requirement in FRS 15.65 to recognise all revaluation losses caused by a clear consumption of economic benefits in profit or loss has not been included in paragraph 17.15F. We understand that FRS 15 includes this requirement in order to meet the Companies Act requirements in relation to permanent diminutions in value which would be equally applicable under FRS 102 (and FRS 101). There is also no equivalent to the FRS 15 requirement not to recognise a revaluation decrease in profit or loss when the recoverable amount of the asset exceeds the revalued amount (i.e. the asset is not impaired) – consideration should be given to including this requirement in order to enhance consistency with the impairment requirements of section 27 of FRS 102.

Section 18 – Intangible assets other than goodwill

- Paragraph 18.8 refers to non-recognition of an intangible asset acquired in a business combination when the fair value of an intangible asset arising from contractual or legal rights cannot be reliably measured, either because the asset is not separable from goodwill or because there is a lack of exchange transactions. It is unclear whether this should be interpreted as applying to all (or only some) such assets that are not separable. The definition of an intangible asset refers to separability from the entity and states that this is not a barrier to identifiability; is a distinction intended between "goodwill" and "the entity" here? Further, the discussion on separability previously included in IFRS 3(2004) and the corresponding version of IAS 38 is not included in draft FRS 102 or in IFRS 3(2008). Under current UK GAAP, intangible assets acquired in a business combination are typically not recognised separately from goodwill as they are not considered capable of being disposed of separately without disposing of a business of the entity (FRS 10.2). Consequently those moving from UK GAAP to FRS 102 may interpret paragraph 18.8 as being equivalent to the existing UK GAAP requirements. We do not believe that this is the intention of the Board and therefore suggest that the wording of paragraph 18.8 should be clarified. In this respect we note that the wording of paragraphs 38(a) and (b) of the previous version of IAS 38 (on which paragraph 18.8 appears to be based) does not include the words "from goodwill" but does refer to circumstances in which it "might" not be possible to measure reliably the fair value of the asset, i.e. lack of separability does not automatically mean that the fair value cannot be measured reliably.

- Paragraph 18.20 refers to a "reliable estimate" of the useful life of an intangible asset. It is unclear why this concept has been included in the standard, given that the legal restriction that applies to goodwill (which in any case does not use this term) does not apply to other intangible assets and the useful life of an intangible asset other than goodwill does not appear to be restricted in the same way under draft FRS 101. We note that this requirement could result in inconsistent treatment of, for example, brands, between draft FRS 102 (and the proposed revised FRSSE) and full EU-IFRS and current UK GAAP, under both of which an indefinite life may be attributed to intangible assets other than goodwill. Please also see our related comments on section 19 of FRED 48 and paragraph 22(j) of FRED 46.

Section 19 – Business combinations and goodwill

- Paragraph 19.23 refers to a "reliable estimate" of the useful life of goodwill - please see our comments on paragraph 22(j) of FRED 46 in this respect. It is unclear why this concept has been included in the standard, since this term is not referred to in the relevant EU Directive.
- Further, it is unclear whether a true and fair override of the legal requirements is possible if the useful life of goodwill is considered to be indefinite (as currently permitted under FRS 10). Given that a true and fair override is proposed under draft FRS 101 in all cases since goodwill is not amortised under IFRS 3, it would appear illogical not to permit the same treatment under FRS 102 (and the FRSSE) in specified circumstances.
- Paragraph 19.24(b) should be updated in a manner consistently with the amendments to IFRS 3 set out in paragraph AG1(c) of FRED 47 to detail how any negative goodwill in excess of the value of the non-monetary assets acquired should be recognised in profit or loss.

Section 20 - Leases

- As stated in our response to FRED 44 (repeated below for reference), the scope exclusion in paragraph 20.1(e) is unclear as to which leases it is intended to capture, and little or no guidance is provided elsewhere in the standard (beyond their inclusion in the scope of section 12).

  Certain leases are stated as being in the scope of section 12 (i.e. carried at fair value) rather than in the scope of section 20. It is unclear from paragraphs 12.3(f) and 20.1(e) as to what is meant by a "loss". It would appear that this requirement may capture, for example, turnover leases or finance leases with a variable rate of interest. Further, there is no guidance on how such leases should be accounted for – if the lease would otherwise be classified as an operating lease, it is unclear whether the gross or net liability is required to be recognised at fair value under section 12 and, if gross, how the corresponding debit entry should be accounted for. Consideration should be given to clarifying this requirement and potentially revising paragraph 12.3(f) to exclude from the scope of section 12 leases with an embedded derivative that is considered to be closely related to the host lease contract.

- As stated in our response to FRED 44, paragraph 20.3 is not wholly consistent with the requirements of IFRIC 4. We repeat those comments for reference:
- This paragraph as drafted states that all of the types of arrangements listed are in substance leases, whereas this is not always the case under IFRIC 4. It is unclear whether this is an intentional simplification of the requirements of full IFRSs to avoid the need to consider the substance of the arrangement (the matter is not discussed in the Basis for Conclusions on the IFRS for SMEs); if so this would be an onerous requirement for many entities. If this is not an intentional change in the requirements of full IFRSs, as a minimum we suggest that this paragraph should be reworded to state that "Such arrangements <u>may be</u> in substance leases of assets, <u>in which case</u> they should…". We suggest also either including fuller guidance

consistent with IFRIC 4 in FRS 102, to include clear principles, or the inclusion of a footnote cross-referring to IFRIC 4 as a source of guidance in developing accounting policies in relation to such arrangements.

Section 22 – Liabilities and equity

- It is unclear why paragraph 22.3 gives a general definition for liabilities. We would expect this to include instead the definition of a financial liability (as per the Glossary). Indeed, a present obligation to transfer a non-financial asset would not meet the definition of a financial liability and therefore would not be within the scope of section 22.

- Paragraph 22.4(a) lists the conditions for "equity" classification by exception for puttable instruments, including (v) the total expected cash flows attributable to the instrument over the life of the instrument are based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity over the life of the instrument. However, the example given in 22.5(b) appears to require that the holder receives a pro rata share of the net assets of the entity <u>measured in accordance with this [draft] FRS</u> and states that, if the holder is entitled to an amount measured on some other basis, the instrument is classified as a liability. Accordingly, a put for cash equivalent to a share of the entity's fair value would not qualify as equity under 22.5(b), even though specifically permitted under 22.4(a). Further, consideration should be given as to whether the definition should be expanded to also allow a share of net assets measured in accordance with full EU-IFRSs.

- Paragraph 22.4(b) presumably intends to replicate the exception to the normal "financial liability" classification presented in IAS 32.16C. However, we note that IAS 32.16C clarifies that it applies only to cases where liquidation is certain to occur and is outside the control of the entity (e.g. a limited life entity) or is uncertain to occur but is at the option of the instrument holder. Without this clarification, there is a conflict between the requirements of paragraphs 22.4(b) and 22.3A(b).

- The wording of paragraph 22.7(c) implies that "issued" and "called up" have the same meaning. However, these terms have distinct and different meanings in sections 546 and 547 of the Companies Act 2006. We suggest that paragraph 22.7(c) is reworded, perhaps to state "… issued (or called up) …".

- It is unclear whether paragraph 22.11 refers to derivatives that meet the definition of equity instruments or to equity instruments issued on the exercise of options and warrants. This should be clarified.

Section 26 – Share-based payment

- Paragraph 26.1(a) and (b) refer only to equity instruments "of the entity". This should be expanded to include instruments issued by other group entities. Although paragraph 26.16 deals with group plans, users of the standard may not look to this paragraph given that such arrangements are currently not included within the scope of the section.

- It is not clear from paragraph 26.16 how group plans should be accounted for if the "reasonable allocation" approach is not applied, or how the granting entity should account for the plan.
- Please see our comments on paragraph 1.12(e) in relation to the disclosure exemption available to qualifying entities.

Section 28 – Employee benefits

- It is unclear whether the asset ceiling requirements of paragraph 28.22 are on a funding basis (which would be consistent with IAS 19(R)). This should be clarified in the final standard since this would be a change to the accounting basis under current FRS 17 and would likely give rise to more asset restrictions and/or the recognition of more additional liabilities.

Section 29 – Income tax

- In our view, the definition of substantive enactment of a tax rate in the UK and the Republic of Ireland as given in paragraphs 40 and 41 of FRS 19 should be included in section 29.
- The definition of a timing difference in the glossary incorrectly does not refer to items included in other comprehensive income and hence is inconsistent with the definition included in paragraph 29.6. Please also see the comment on that paragraph in Appendix 4B to this letter.
- It is unclear whether the disclosure requirements of paragraph 29.27(b) and (c) are intended to be broadly the same as the current requirements under FRS 19 (and IAS 12) to present a tax reconciliation and to disclose factors affecting future tax charges, or whether the proposal is to introduce new disclosures. If the latter, the reason for the change does not appear to be explained. In particular it is unclear whether "amounts reported to the tax authorities" is intended to be the current tax charge for the period, or a different amount which is not currently disclosed in financial statements. Also, the requirement to make disclosures in respect of the next three years in paragraph 29.27(c) may tend to become "boilerplate" over time, thus reducing the value of the disclosure. We suggest that this should be clarified and, if the requirements are intended to be the same as under FRS 19 (or IAS 12), that the wording should be based on the requirements of those standards.

Section 30 – Foreign currency translation

- Paragraph 30.13 refers to the recognition of exchange differences in relation to a net investment in a foreign operation as a component of equity. Paragraph 30.25(b) suggests that this should be a separate component of equity yet this is not made clear in paragraph 30.13. This inconsistency should be clarified in the final standard. We note that it is unclear why a separate component of equity would be necessary given that exchange gains and losses are not recycled through profit or loss upon disposal of the related foreign operation.

Section 34 – Specialised activities

Extractive activities

- We also note that the standard is silent in relation to exploration and evaluation (E&E) assets themselves; section 34 cross-refers to sections 17 and 18 only in relation to tangible or intangible assets for use in extractive activities. If the intention is for E&E assets to be accounted for under sections 17 and 18, this should be clarified in the final standard.

Financial institutions: disclosures

- It is unclear whether the disclosures required by this part of section 34 are required to be given on a consolidated basis (for example by a group headed by a financial institution) or whether they are required to be given only in the individual financial statements of a financial institution. If required on a consolidated basis, clarification should be provided as to when such disclosure is required. For example, a group containing a bank may not be headed by a financial institution (as defined). This should be clarified and, if the disclosures are to be given in consolidated financial statements, then a definition of a financial institution group should be provided (the definitions of a banking group and an insurance group in sections 1164 and 1165 of the Companies Act 2006 could be used as a starting point for such a definition). If the disclosures are to be given in consolidated financial statements, it should be clarified whether they then are to be given in respect of the financial instruments only of financial institution members of the group or of the group as a whole.

Retirement benefit plans: financial statements

- Please see our comments in Appendix 1 to this letter in response to question 6 raised by the ASB. Section 34 refers in various paragraphs (e.g. 34.34, 34.35) to the presentation of information either as part of the financial statements, <u>or alongside the financial statements</u>. In our view, it is surprising that an accounting standard would require disclosures outside the financial statements. If these disclosures are required in order for the financial statements to give a true and fair view, then they should be given in the financial statements (and referred to in the standard). Otherwise any requirement to make disclosures outside the financial statements should in our view be dealt with in the SORP. The content of the standard could therefore be streamlined as follows:

  – The following could be deleted from the standard: paragraphs 34.32, 34.34, 34.38, 34.45 and 34.46. The funding policy in particular (paragraph 34.34) should not be part of the financial statements – it is very subjective and should be disclosed elsewhere in the annual report.

  – Repetition in paragraphs 34.33 and 34.36 could be eliminated as the reporting requirements for defined benefit and defined contribution plans are the same. It is also unclear why paragraph 34.34 appears to apply only to defined contribution plans and paragraph 34.39 only to defined benefit plans. The standard could distinguish between defined benefit and defined contribution plans in the required disclosures as per the current SORP requirement.

  – References to profit and loss should be deleted and reference made only to the Fund Account (paragraph 34.39) as profit and loss is not relevant for retirement benefit plans.

- Please see our comments above in relation to paragraph 9.9A. We also note that our understanding of IAS 26 is that all subsidiaries (other than those that form part of the operations of the plan) are included at fair value rather than consolidated on a line-by-line basis. Clarification of the intended accounting for subsidiaries held by a retirement benefit plan in this section would be useful. A cross-reference to paragraphs 14.4B and 15.9B could also usefully be added to this section.

- Paragraph 34.31 states that "in addition" to applying the draft FRS, retirement benefit plans shall apply the requirements of paragraphs 34.32 to 34.46 of the standard. We suggest that either this paragraph or paragraph 34.39 should clarify that the requirement to measure net assets available for benefits at fair value in paragraph 34.39 is "instead of" rather than "in addition to" the measurement requirements of section 11.

- "Net assets available for benefits" is in bold type in paragraph 34.39 yet is not defined in the body of the standard or its glossary. We note that this definition should incorporate the possibility of negative plan assets (e.g. derivatives which are liabilities).

- Paragraph 34.43 deals with disclosure of actuarial information. There appears to be an overlap between paragraphs 34.43(a) and 34.43(b) which appear to be asking for similar but not necessarily the same information. Paragraph 34.43(a) comes from IAS 26 whilst 34.43(b) appears to relate to the UK Summary Funding Statement (SFS). Draft FRS 102 would require disclosure of vested and non-vested benefits, which is not currently in the SFS information. In the UK, benefits vest immediately, and whilst it could be argued that the first three months of membership could be deemed to be non-vested, since the plan could insist on a refund if a member chose to leave in three months or less, such an amount would be likely to be very immaterial. The distinction could create more administration than necessary. Also IAS 26 requires disclosure of whether current or future salaries are used in the calculation of liabilities; it is unclear why this is not included in draft FRS 102. We suggest that this information should be included as part of the actuarial assumption disclosures.

Funding commitments

- The scope of this section now includes non-PBE entities. No definition of a "funding commitment" is given and it is therefore unclear what commitments are within the scope of the section. For example, it might appear that commitments to fund an investee company are within the scope. If so, this should be clarified as recognition of a liability to provide such funding would represent a change to current practice. We also note that inconsistent treatment between the investor and investee would result, since the investee would be unlikely to recognise any funding until it was received, yet the investor may be required to recognise a liability sooner than this.

- This section should provide examples of what is considered in practice to be an obligation "from which an entity cannot realistically withdraw". As we noted in our response to FRED 45, specific guidance should be provided in relation to gift aid payments made on an annual basis, for example by a trading subsidiary of a charity. In our view, under current UK GAAP, gift aid payments are recognised only when paid, consistent with the treatment of intra-group dividend payments, as no obligation can be considered to exist until this time. It is unclear whether this section of the draft standard is intended to change the accounting for gift aid payments, for dividends payable, or for intra-group funding commitments.

- We note that there is an apparent inconsistency between paragraph 34.57(a), which envisages constructive obligations, and the guidance in paragraph 34A.2 which refers to promises conditional on the receipt of future income. Some of these may be constructive obligations and some not, depending on the reliability and consistency of the entity's income stream.

- We note that paragraphs 34.A4 and 34A.5 use the term "performance-related conditions". It is unclear whether these are, or are intended to be, the same as "performance conditions" as defined in the glossary. If so, consistent terminology should be used. We also note that paragraph 34A.5 states that "A mere restriction on the specific purpose for which funds are to be used does not in itself constitute a performance condition". We suggest that (assuming that the definition of a performance condition remains as currently drafted) reference should be made in this paragraph also to the potential for return to the donor (as is done in paragraph 34.B13).

General comment on PBE sections of section 34

- We suggest that for ease of reference by PBEs, cross-references should be included in the relevant main sections of the standard (e.g. grants, business combinations, financial instruments) to the corresponding PBE sections in section 34.

Incoming resources from non-exchange transactions

- Paragraph PBE34.65 requires recognition of certain non-exchange transactions in income. As we noted in our response to FRED 45, it is unclear whether this is intended to apply regardless of the nature of the item received. Companies Act entities, for example, are permitted to recognise only realised profits in the income statement; for donations of goods that do not constitute qualifying consideration, the resultant gain therefore cannot be recognised in income.

- We note that the proposed definition of a performance condition in the glossary could lead to a change in current charity practice. In particular, we note that paragraph 105 of the current Charities SORP requires income to be recognised in relation to donations which are subject to conditions, where meeting such conditions is within the charity's control and there is sufficient evidence that the conditions will be met. If the Board intends to change current practice in this area, this should be explained.

- The interaction of paragraphs PBE34.65(b) and PBE34.69 is unclear. Paragraph PBE34.69 discusses when to recognise a liability for a resource that becomes repayable due to non-compliance with any associated performance conditions. This implies that income may have been recognised before the performance conditions are met. However, under paragraph PBE34.65(b) transactions with performance conditions are recognised in income only when the performance conditions are met and, under paragraph PBE34.65(c), held as a liability until that time.

- We note that paragraph PBE34.71 requires measurement at the fair value <u>of the resources</u> received or receivable. However, the second sentence of paragraph PBE34.B15 and paragraph PBE34.B16 discuss measurement based on the fair value <u>of the asset received</u>. This inconsistency should be removed in the final standard since the fair value of the resource may differ from the fair value of the asset. For example, if a new Mercedes minibus were donated to a charity, the fair value of the resource received (access to the use of *a* minibus) could be lower than the fair value of the asset (the cost of a new *Mercedes* minibus).

- We made the following comment in our response to FRED 45 in relation to this topic which remains valid in respect of FRED 48:
  - Clarification should be given as to whether the requirements of section 34 are required to be applied to intra-group non-exchange transactions between PBEs, or between PBEs and non-PBEs within the same group. In our view, fair value accounting should not be mandated for all transactions conducted at undervalue, particularly those between group entities.

Public Benefit Entity combinations

- As we noted in our response to FRED 45, it is unclear whether any gain arising on a combination that is in substance a gift under PBE34.77 should be recognised in the income and expenditure account or within other comprehensive income. We note that PBEs which are, for example, companies within the scope of the Companies Act, and those subject to the Accounting Requirements for Registered Social Landlords General Determination 2006, are permitted to recognise only realised profits in the income and expenditure account. We would therefore expect either that the gain should be recognised in other comprehensive income or for similar requirements to those included in FRED 47 AG1(c) to be included in this paragraph.

Concessionary loans

- As we noted in our response to FRED 45:
  - Paragraph PBE34.91 does not address how any issue costs of the instrument should be accounted for. Paragraph PBE34.92 could also usefully state the basis on which the accrued interest payable or receivable should be accounted for, i.e. whether or not this should be on an effective interest basis (as Section 11 of draft FRS 102), and, if not, on what basis.
  - There is no discussion of how to account for any concessionary loans that fall within the scope of Section 12 of the standard; it is therefore unclear whether the option set out in paragraph PBE34.90(b) is available in respect of such loans.

Section 35 – Transition

- As noted in our comments on FRED 44:
  - Paragraph 35.10(a) states that a first-time adopter may elect not to apply section 19 *Business Combinations and Goodwill* to business combinations effected before the date of transition to FRS 102. It is unclear what this means in terms of any existing goodwill balance – for example, if goodwill was not previously amortised (if, for example, it had been ascribed an indefinite life under UK GAAP), it is unclear whether the goodwill is required to be amortised subsequent to the adoption of FRS 102 (and if so, from what date the useful life under FRS 102 is considered to commence), or whether, if section 19

is not being applied, the previous UK GAAP accounting policy may or must continue post transition.

- Paragraph 35.10(h) refers to a possible exemption from the recognition of deferred tax at the date of transition. The subsequent accounting for such amounts is unclear and we suggest that this paragraph should be redrafted to clarify whether the balance concerned, or movements therein, are required to be recognised subsequently.

Glossary

- The definition of a discontinued operation in the glossary no longer refers to "or is held for sale". We note that the definition of a discontinued operation under FRS 102 is therefore inconsistent with that under IFRS 5. We are unclear as to whether this was the Board's intention. If the definition of a discontinued operation is revised back to that in IFRS 5 and the IFRS for SMEs, we suggest that a definition of "held for sale" based on that in IFRS 5 could also usefully be included. If no reference to held for sale is added, we suggest that the definition should clarify whether the operation must have been disposed of at the balance sheet date in order to be classified as discontinued, particularly since this would represent a change from FRS 3's definition of a discontinued operation.

Appendix 4B

Other comments in relation to FRED 48

Section 1 – Scope

- To aid the simplicity of use of the standard, consideration should be given to identifying within each section of the standard those disclosures to which the disclosure exemptions in paragraphs 1.8 to 1.13 might apply, perhaps by the use of shading, a different font or annotation with a symbol or footnote.
- The glossary to FRED 48 refers to "which give a true and fair view" in the definition of a qualifying entity. Please see our comments on paragraph 4 of FRED 46 in this respect.
- Paragraphs 1.11(a) and (b) – please see our comments on paragraphs 7(a) and 7(b) of FRED 47.
- Paragraph 1.12(e) – please see our comments on paragraph 8(a) of FRED 47. A "group arrangement" is not defined in FRS 102.

Section 2 – Concepts and pervasive principles

- Paragraphs 2.53 to 2.56 discuss intermediate payment arrangements. It would be helpful to clarify that the accounting for an entity's own shares held via an EBT or similar arrangement should be accounted for in accordance with paragraph 22.16.

Section 3 – Financial statement presentation

- Consideration should be given to revising the first sentence of paragraph 3.10. The frequency of reporting is governed (for companies) by the Companies Act 2006, which permits (subject to conditions) accounting periods of longer than twelve months, hence the reference to "at least annually" is inconsistent with the requirements of the Act; we suggest that "generally" should be inserted before "at least annually".
- Paragraph 3.14 refers to "previous comparable period". In our view this should be changed to "comparative period" since the current drafting might be read as implying that the comparative period must be the same length as the current period.
- As noted in our comments on section 1 of the draft standard, disclosures which may be covered by the disclosure exemptions for qualifying entities should preferably be identified as such in the respective sections of the standard. This is particularly relevant to the requirement to present a cash flow statement in paragraph 3.17(d).

Section 6 – Statement of changes in equity and statement of income and retained earnings

- Paragraph 6.3(a) is not entirely consistent with paragraph 6.2. The latter refers to the presentation of an entity's profit or loss and other comprehensive income for the period (i.e. two separate amounts) in the statement of changes in equity, as does paragraph 6.3(c). Paragraph 6.3(a) requires these two items to be combined as total comprehensive income.

- Paragraph 6.3(b) refers to a component of equity. It might be helpful to define what are considered to be components of equity for this purpose, and in particular to clarify that non-controlling interests are considered to be a component of equity.

Section 7 – Statement of cash flows

- It would be helpful to include the illustrative examples from IAS 7 in this section as UK GAAP adopters may not be familiar with the required presentation.

Section 8 – Notes to the financial statements

- For consistency with the approach taken in relation to the format of the primary statements, a reference to the note disclosures required (for companies) under the Companies Act 2006 should be included in this section.

Section 9 – Consolidated and separate financial statements

- We suggest that an equivalent to paragraph 24 of FRS 2 should be included in section 9 to clarify that neither disproportionate expense nor undue delay can justify the exclusion of a material subsidiary from consolidation.
- The drafting of paragraph 9.28 could be clearer since “two or more entities controlled by a single investor” might apply to some groups required or choosing to prepare consolidated (rather than combined) financial statements.
- It would be helpful to include in paragraph 9.31(c) the guidance in UITF 31 paragraph 11(c) regarding where any gain should be recognised if it is unrealised.

Section 11 – Basic financial instruments

- It is unclear whether paragraph 11.5(e) refers to bonds and similar debt instruments which are both held and payable; perhaps this could be clarified.
- Section 11 refers to both “ordinary” and “preference” shares. For example, paragraphs 11.8(d) and 11.14(c) refer to “an investment in non-convertible preference shares and non-puttable ordinary shares or preference shares”. It is unclear why reference is made to the legal form of the instruments, i.e. ordinary shares or preference shares. If the legal form is not relevant we suggest that these references should be deleted. If it is relevant, a suitable explanation should be added.
- Paragraph 11.14(b) refers to measuring commitments to receive loans at cost (which sometimes is nil) less impairment. Consideration should be given to including guidance on when the cost is expected to be nil and whether the cost of such an instrument might include commitment fees paid by a borrower to secure a line of credit.
- Paragraph 11.39 does not appear to require any disclosure in relation to the impairment of financial assets. Consideration should be given to the inclusion of such disclosure requirements, if not for all entities, then at least for financial institutions (we note that only minimal impairment disclosure requirements are included in section 34 *Financial institutions: disclosures*).
- Please also see our comments in respect of section 34 *Financial institutions: disclosures*.

Section 12 – Other financial instruments issues

- It is unclear whether financial guarantee contracts are within the scope of section 12 of the standard or whether (or in what circumstances) they are covered by the reference to IFRS 4 *Insurance Contracts* in paragraph 1.6. This should be clarified in the final standard in order to avoid diversity in practice.
- Please see our comments on paragraph 20.1(e) in relation to the inclusion of certain leases within the scope of section 12.
- Paragraph 12.3(b) excludes "*interests* in subsidiaries, associates and joint ventures" from the scope of section 12. The equivalent scoping paragraph of section 11 refers to "*investments* in subsidiaries, associates and joint ventures". It is unclear whether there is intended to be a difference between the two terms. If so, then this should be clarified. If not, then consistent terminology should be used.
- We assume that paragraph 12.18(d) does not apply to net investment hedges, since the net investment which is being hedged will not have a maturity date; this might be clarified.
- Paragraph 12.23 states that "the hedging gain or loss recognised in other comprehensive income shall be reclassified to profit or loss when the hedged item is recognised in profit or loss or *when the hedging relationship ends*". We suggest that "except as otherwise required by paragraph 12.25" or similar wording should be added in order to clarify that "when the hedging relationship ends" does not include, for example, revocation of the hedge designation.
- Paragraph 12.25 should be expanded to clarify the required accounting for the gain or loss that was recognised in other comprehensive income in situations not covered in the final paragraph of that paragraph, for example when the forecast transaction is still expected to occur.

Section 13 – Inventories

- It is unclear what, from a non-PBE perspective, might be considered to be "inventories held for distribution" or "any loss of service potential" (paragraph 13.4A). Should this be a "PBE" paragraph? Alternatively, if this paragraph is intended to include within its scope for example samples, this should be clarified in the definition of inventories held for distribution included in the glossary.
- Paragraph 13.7 should refer to the capitalisation of borrowing costs in relation to qualifying assets (and cross-refer to section 25).

Section 17 – Property, plant and equipment

- It is not immediately clear from the definition of depreciable amount (paragraph 17.18 and glossary) that, when applying the revaluation model, depreciation is charged based on the revalued amount. We suggest that this should be clarified.
- Consideration should be given to the inclusion of brief guidance on the expected frequency of valuations by professionally qualified valuers. Further, IAS 16.35 permits two different

accounting treatments for accumulated depreciation when an asset is revalued and it is unclear whether both of these would be available to users of FRS 102.

Section 18 – Intangible assets other than goodwill

- Please see our comments on revaluation of property, plant and equipment under section 17 of the standard.

Section 19 – Business combinations and goodwill

- Paragraph 19.30 states "The comparative information corresponding figures should be restated…". "Corresponding figures" should be deleted from this sentence. Also, it is unclear how the comparative information should be presented in individual financial statements in which merger accounting is applied. We would expect the previous stated comparatives to be unaffected as these are the statutory results for the comparative period, but that "proforma" comparative information on a merger-accounted basis might also be presented.

Section 22 – Liabilities and equity

- This section might more appropriately be headed "*financial* liabilities and equity"' since it does not apply to non-financial liabilities (please see our comment on paragraph 22.3 above).

- Paragraph 22.2(d) refers to "treasury shares" in relation solely to various types of share-based payment arrangement. The term is expanded in paragraph 22.16, which is not cross-referred to from paragraph 22.2(d). It is unclear whether both paragraphs are intended to refer only to treasury shares as defined by the Companies Act 2006, only to own shares held, for example, via an EBT or similar intermediate payment vehicle, or to both types. Please also see our comments on paragraphs 2.53 to 2.56 in this respect.

- The appendix to section 22 (end of first page) illustrates "gross" accounting entries. We suggest that clarification should be added to explain that the amounts should not be shown gross in the balance sheet.

Section 23 – Revenue

- Paragraph 23A.11 refers to "acting, in substance, as an agent". Consideration should be given to including guidance based on IAS 18.IE21 on determining whether an entity is acting as a principal or an agent.

Section 27 – Impairment of assets

- Paragraph 27.6 – please see our comments in relation to accounting for revaluation decreases under section 17 of draft FRS 102.

Section 28 – Employee benefits

- Paragraph 28.1 includes the definition of a short-term benefit that is in line with IAS 19 (Revised), i.e. "expected to be settled", whereas the examples for short-term benefits given in paragraphs 28.4 and 28.29 still include the wording of current IAS 19, referring to "profit sharing and bonus payments payable within twelve months…". We suggest that consistent terminology should be used.

- Paragraph 28.15 cross-refers to paragraphs 11.27-32 in relation to the determination of the fair value of plan assets that are financial assets. Consideration should be given to providing guidance on the determination of the fair value of other types of plan asset, for example investment property, perhaps by cross-reference to other relevant sections of the standard.
- The reference to "expected return on plan assets" should be deleted from paragraph 28.18 as this is not relevant except in the case of contribution-based promises.
- Paragraphs 28.21 and 28.23 refer to changes to the plan being recognised in profit or loss. Consideration should be given to clarifying that changes in this context are intended to refer to "benefit changes", given the debate over accounting for the RPI/CPI change.

Section 29 – Income tax

- The scope of section 29 does not include VAT, yet the accounting for VAT is discussed in paragraph 29.20. We suggest that either: the scope (and potentially the title) of the section should be revised to include VAT; or the requirements of paragraph 29.20 should be incorporated into the scope of the section (e.g. "This section does not cover accounting for VAT, which is accounted for as follows…").
- Paragraph 29.6 refers to timing differences arising only in relation to items of income and expense recognised in profit or loss or other comprehensive income. It is unclear whether timing differences would be considered to arise in relation to items recognised directly in equity (for example, in respect of share issue expenses): we would expect this to be the case If so, "or equity" should be inserted after "other comprehensive income".
- In paragraph 29.10, "on acquisition" should be inserted after "differs from their fair value" to avoid the implication that deferred tax will always be updated for post-acquisition changes in fair value, even if unrecognised.
- It is unclear in section 29, for example in the case of a revalued depreciable asset, whether deferred tax should be calculated based on the sale or usage rate, or on a blended rate, depending on the intended use of the asset.
- In paragraph 29.26(f), "material" should be inserted before "errors".
- Paragraph 29.27(d) refers to the "applicable tax rate(s)". We assume that this is intended to be the statutory tax rate for the period, rather than the effective rate; we suggest that this should be clarified since the term is not currently used elsewhere in section 29.

Section 30 – Foreign currency translation

- The end of the last sentence of paragraph 30.22 should read "the entity shall recognise it in other comprehensive income" [rather than "classify it as equity"].

Section 33 – Related party transactions

- Please see our comments in Appendix 1 to this letter in response to question 7 raised by the ASB.

Section 34 – Specialised activities

Agriculture

- Please see our comments in Appendix 1 to this letter in response to question 5(a) raised by the ASB.

Extractive activities

- We understand that the SORP *Accounting for Oil & Gas* is to be updated to reflect the proposed changes to UK GAAP. Consideration should be given to including a reference to the accounting requirements of the SORP in paragraph 34.11.

Service concession arrangements

- Please see our comments in Appendix 1 to this letter in response to question 5(b) raised by the ASB.

Financial institutions: disclosures

- It would be helpful to include a cross-reference from sections 11 and 12 to the financial institution disclosure requirements of section 34.

Retirement benefit plans: financial statements

- It would be helpful if paragraph 34.31 could clarify that the financial institution disclosure requirements of paragraphs 34.17 to 34.30 also apply to retirement benefit plans. We also understand that the SORP *Financial reports of pension funds* is to be updated to reflect the proposed changes to UK GAAP. Consideration should be given to including a reference to the accounting requirements of the SORP in paragraph 34.31.

- The additional disclosures under paragraphs 34.17 to 34.30 for financial institutions will apply to retirement benefit plans. For defined contribution plans, to the extent that assets are held in individually designated portfolios rather than on a pooled basis, we question whether the risk disclosures required under those paragraphs are relevant since plan level risks are not relevant to members who have tailored portfolios.

- Paragraph 34.39 cross-refers to paragraphs 11.27-32 in relation to the determination of the fair value of net assets available for benefits. These paragraphs relate only to financial assets. Consideration should be given to providing guidance on the determination of the fair value of other types of asset, for example investment property, perhaps by cross-reference to other relevant sections of the standard.

Funding commitments

- As the proposed requirements in relation to funding commitments are no longer restricted to PBEs, consideration should be given to including the requirements of this section in section 21 *Provisions and contingencies* or, as a minimum, including a cross-reference from section 21 to this section of section 34.

- Paragraph 34.55 could helpfully refer explicitly to Appendix I to this section.

Incoming resources from non-exchange transactions

- Paragraph PBE34.63 could helpfully refer explicitly to Appendix II to this section.

Public Benefit Entity combinations

- PBE34.85 refers to both "corresponding" and "comparative" figures. The terminology used should be consistent within this paragraph and with that in paragraph 19.30. Please also see our comments above on that paragraph, including our comment on how we would expect the comparative information to be presented in individual financial statements in which merger accounting is applied.

Section 35 – Transition

- Paragraph 35.6 refers to the "comparable [prior] period". We suggest that this should refer instead to "comparative period" in order to avoid implying that the length of the comparative period should be the same as the current period.
- Paragraph 35.10(e) suggests that certain foreign exchange differences should be classified as a separate component of equity. Please see our comments on section 30 above in this respect. If section 30 is revised to clarify that a separate component of equity is not required, paragraph 35.10(e) should be deleted as it will not be required.

Glossary

- Please see our other comments on the glossary in the relevant section numbers above.

Appendix II

- We suggest that an additional line and third column comment should be added for current assets, referring to debtors due after more than one year being current assets under the Act but non-current assets under EU-adopted IFRSs.

Appendix III

- In relation to paragraphs A3.4 and A3.7 of FRED 48, please see our comments on paragraphs A2.5 and A2.7 of FRED 46 and paragraph 4 of FRED 47.
- Paragraph A3.11 refers to "company financial statements". As "individual accounts" has not been redefined by Appendix II, and "company financial statements" is not referred to in the glossary, this paragraph should instead refer to "individual accounts".
- The UITF 4 consensus could more helpfully be included within Section 4 of FRS 102 rather than in paragraph A3.26.