Periodic Review of UK and Ireland financial reporting standards

Q&A – FRED 82 launch webinar 19 January 2023

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During the FRED 82 launch webinar on 19 January 2023, a number of questions were received from stakeholders, not all of which could be answered live. The following responses are intended to be informative; however, in case of any conflict between these responses and the requirements of the FRC's published codes and standards, the latter shall prevail.

Consultation

1. Is this consultation just for show or will you really take note of our feedback?

The purpose of the consultation is to publicise our proposals to a wide range of stakeholders and encourage feedback to inform our final amendments. Naturally, we cannot promise to accommodate all requests, but the views of interested parties are weighed carefully as part of the FRC's deliberations in finalising the amendments.

2. Why do you propose a relatively short consultation period, falling into a busy period for many stakeholders? Would you consider extending the consultation period?

The FRC's customary consultation period is 12 weeks; for FRED 82 we have allowed over 19 weeks, taking into account factors including respondents' other commitments at this time of the year. We trust that this will provide sufficient time for stakeholders to comment on the proposals.

3. Can you promise there'll be no further changes to FRS 102 for another five years?

We cannot promise that there will be no further changes to FRS 102 (or the other standards) until the next periodic review. Urgent issues often arise in the intervening period (for example, see Question 28) and we need to consider each individually in order to determine whether further amendments may be needed before the next periodic review. Amendments in between periodic reviews will tend to be narrower in scope than those made as a result of periodic reviews.

Effective date

4. Does the proposed effective date of 1 January 2025 give people long enough to prepare? 5. Does this give SORP-making bodies enough time to revise their SORPs?

Our intention is to give preparers sufficient time to implement the amendments once they have been issued. Because the headline proposals to update revenue and lease accounting are based on IFRS 15 and IFRS 16, we expect that preparers will be able to benefit from implementation experience, guidance, and products that already exist in the market. In addition, our proposals include appropriate simplifications in the requirements, and proportionate transitional provisions. The length of the implementation period naturally depends on both the date the final amendments are issued and their effective date; the FRC has stated that it intends to allow an implementation period of at least 12 months. Question 8 of the invitation to comment invites feedback on the effective date as well as the transitional provisions.

We recognise that SORP-making bodies will have a particular interest in our proposals and the timeline. We interact with the SORP-making bodies regularly in the course of our observation of their work, and will welcome their feedback alongside that of other stakeholder groups.

6. Why is the proposed effective date 1 January 2025 rather than (say) 15 December 2024? Many entities change their reporting date by a few days each year, and this would help them be treated consistently.

The customary effective date for amendments to UK GAAP is periods beginning on or after 1 January, which is aligned with the IASB's usual practice. We intend to apply this consistently; FRED 82 does however propose to permit entities to adopt the amendments early.

7. Are you permitting early adoption? If so, what will be the early-adoption window?

Early adoption will be permitted and would require a preparer to apply all the amendments at the same time, as set out in proposed paragraph 1.34. The ability to early-adopt will be available once the final amendments to the standard have been issued.

Overall level of disclosure

8. Does Question 1 of the Invitation to Comment relate to the proposed amendments to disclosure requirements, or to disclosure requirements more broadly?

The FRC welcomes stakeholders' views on the overall level of disclosure in a set of financial statements prepared in accordance with FRS 102 – taking into account, but not limited to, the amendments proposed in FRED 82.

FRS 102 Section 1A *Small Entities*

9. Is it the FRC's view that all the disclosures proposed to be added to Appendix C to Section 1A are already required for small company accounts to give a true and fair view?

At present, a small entity is required to present sufficient information to meet the requirement to give a true and fair view (FRS 102 paragraph 1A.16, referring to the requirement in FRS 102 paragraph 1A.5) and is encouraged to consider the disclosure requirements throughout Sections 8 to 35 in doing so (FRS 102 paragraph 1A.17). In addition to the disclosures required by Appendices C and D to Section 1A (FRS 102 paragraph 1A.18), a small entity is specifically encouraged to make the disclosures set out in Appendix E (FRS 102 paragraph 1A.20).

By adding additional disclosure requirements to Appendix C, the FRC intends to reduce the amount of judgement required of UK small entities in order to present sufficient information to give a true and fair view. The proposals in Section 1A are not intended to be read as a comment on current practice.

10. The Section 1A changes, which are welcome, say that deferred tax disclosures are required to give a true and fair view. Did you consider mandating current tax disclosures as well, eg the tax reconciliation? Are there any other Section 1A disclosures you're looking for feedback on?

The FRC recognises the importance of balance. In developing the proposed additions to Appendix C to Section 1A, we have tried to identify the disclosures most likely to be required in order to give a true and fair view, based on our own views and feedback from stakeholders. However, the overall requirement for a small entity's financial statements to give a true and fair view is unchanged, and some small entities may need to provide disclosures not specifically mentioned in Appendix C in order to achieve this, when relevant to material transactions, other events or conditions of the small entity.

We welcome feedback on our proposed amendments to the Section 1A disclosure requirements.

11. Are you aware of any proposed changes to Irish company law that would allow similar amendments to Appendix D to Section 1A?

The FRC is not currently aware of any such changes to Irish company law. As a prescribed body for issuing accounting standards in the Republic of Ireland, the FRC maintains a regular dialogue with Irish stakeholders and we welcome feedback from respondents in the Republic of Ireland.

FRS 102 Section 3 *Financial Statement Presentation*

12. Is there going to be clarification on what basis to use when going concern isn't appropriate?

13. Guidance is available elsewhere, but something in FRS 102 would be helpful – why should you need to go to an external source? If you intend to wind up an entity then currently you can't see from the standard alone how that should be done.

The requirements of FRS 102 are based on the presumption that the going concern basis of accounting is appropriate. To issue guidance on accounting when the going concern basis is not appropriate would therefore be likely to require a separate financial reporting standard. Neither the FRC nor the IASB has issued such guidance in the past and, although this issue was raised by some stakeholders during the request for views to inform the periodic review, the FRC does not consider that there is sufficient evidence that standard-setting is required. As with all aspects of the proposals, we welcome additional feedback and evidence from stakeholders.

FRS 102 Section 11 *Basic Financial Instruments*

14. Is there any timeline for aligning FRS 102 with the IFRS 9 expected credit loss model and recognition and measurement?

15. FRED 82 mentions any move to adopt an expected credit loss model would come with further consultation. Are you saying that could still come within this periodic review and be effective from 1 January 2025? That seems tight.

It is likely that we will await the IASB's conclusion as to aligning the *IFRS for SMEs* Accounting Standard with the IFRS 9 expected credit loss model before considering this again for FRS 102. When we do consider it, any proposals will be subject to public consultation and, once issued, we would expect to provide an implementation period of at least 12 months before the effective date. We do not expect the third edition of the *IFRS for SMEs* Accounting Standard to be published before 2024. Therefore it is unlikely that any such changes to FRS 102 would be effective from 1 January 2025.

Other aspects of IFRS 9, besides the expected credit loss model, were considered prior to and during the Triennial Review 2017 resulting in some amendments to FRS 102, and the FRC does not anticipate reconsidering them.

FRS 102 Section 16 *Investment Property*

16. Is there going to be clarification of what to do if investment properties can't be measured at fair value?

Extant paragraphs 2A.5 and 2A.6 of FRS 102 refer to situations in which a reliable measure of fair value is not available, as noted in paragraph B16.4 of the Basis for Conclusions to FRS 102. FRED 82 proposes to retain these requirements, as new proposed paragraphs 2A.19 and 2A.20. We have not proposed any additional guidance regarding the valuation of investment properties.

17. Are the Section 19 changes on consideration v remuneration intended to align with the very rigid interpretation of IFRS 3 or will there be some scope for judgement on substance of the arrangement?

Proposed paragraph 19.11B of FRS 102 is based on paragraphs 52(b) and B54 of IFRS 3. It does not include the detailed discussion of specific indicators which is included in paragraph B55 of IFRS 3, instead stating that an entity shall carefully consider the substance of the arrangement.

FRS 102 Section 19 *Business Combinations and Goodwill*

18. Why was the definition of a business not amended in line with the latest changes to IFRS 3?

Please refer to paragraphs B19.1 to B19.3 in the Basis for Conclusions to FRED 82. Stakeholder feedback suggested we consider aligning the definitions of 'business' and 'business combination' to the latest IFRS 3 definitions. However, the FRC noted that doing so would exclude from the scope of Section 19 some transactions that are currently within its scope, including group reconstructions and combinations of entities that are not combinations of businesses. We therefore considered that before aligning these definitions, a new solution might be needed for accounting for group reconstructions. As we seek international solutions when possible, we have deferred consideration of the accounting for group reconstructions pending the progress of the IASB's project *Business Combinations under Common Control*.

FRS 102 Section 20 *Leases*

19. If the IASB has decided not to bring leases on-balance sheet in the *IFRS for SMEs* Accounting Standard, why does the FRC propose to bring leases on-balance sheet in FRS 102?

At this stage, the IASB has deferred the consideration of alignment of the *IFRS for SMEs* Accounting Standard with IFRS 16. The FRC has taken the same approach in respect of FRS 105. In respect of FRS 102, the FRC's view is that moving to an on-balance sheet lease accounting model would provide improved information to users of financial statements and that sufficient time has passed since the implementation of IFRS 16 for such a transition to be practicable for FRS 102 preparers. This view was supported by feedback received in response to our request for views, which was generally in favour of the new model provided that appropriate simplifications could be offered.

20. It's great that preparers could be permitted to use their "obtainable borrowing rate". Could the language in the glossary be changed to make it easier for preparers to understand the difference from the “incremental borrowing rate”, and clearer about how to determine it?

We are happy to receive feedback and suggested improvements to the proposed wording.

21. The Basis for Conclusions to IFRS 16 cites a monetary value in respect of low-value assets. The examples in FRED 82 are generally much lower value than that – mobile phones, home printers, TVs etc. Do you anticipate that low-value assets could be as "expensive" as, say, £4,000?

A monetary amount is referred to in the Basis for Conclusions to IFRS 16 but not in the standard itself. The FRC has chosen not to specify a monetary amount in FRS 102 either. However, we have included, in proposed paragraphs 20.11 and 20.12 respectively, additional examples of underlying assets that would typically, and would not, be considered to be of low value.

The proposed simplifications also have an impact here: under proposed paragraph 20.9, the assessment of the value of an underlying asset is based on the value of the asset at the start of the lease, whereas under paragraph B3 of IFRS 16 the assessment is based on the value of the asset when new.

We would welcome feedback on other categories of assets which could be added to the lists of examples in proposed paragraphs 20.11 and 20.12.

22. Whilst some of the proposed amendments are based on changes to IFRS Accounting Standards, there is other interpretative guidance issued by the IASB that has not been included. Would you clarify as part of the amendments whether these should, or should not, be applied?

Some guidance from IFRS Accounting Standards has been incorporated into our proposals – for example, proposed Section 20 of FRS 102 includes elements of Appendix B *Application Guidance* to IFRS 16. The FRC also has the ability to issue additional guidance, e.g. Staff Factsheets, when appropriate. In addition, paragraphs 10.2 to 10.6 of FRS 102 set out requirements for the selection and application of accounting policies, allowing management to consider the requirements and guidance in adopted IFRS in certain circumstances.

23. Did I hear correctly that we will not be required to restate comparatives for leases?

The proposed transitional requirements in relation to the adoption of the proposed amendments are set out in Section 1; in particular, the requirements in relation to the approach for leasing are set out in proposed paragraph 1.40.

Proposed paragraph 1.40 mandates the application of the 'modified retrospective' approach and specifies that a lessee shall not restate comparative information for leases.

24. Does imposing one particular transition method for leases constrain a subsidiary's ability to have numbers consistent with those of the group under IFRS?

Such a subsidiary could consider the practical expedient in proposed paragraph 1.41 to use balances calculated under IFRS 16 at the date of initial application. Whether its lease balances measured under FRS 102 remained consistent over time with the balances measured under IFRS 16 would be expected to depend on the subsidiary's use or otherwise of the optional simplifications proposed for FRS 102.

FRS 102 Section 23 *Revenue [from Contracts with Customers]*

25. How might he FRC's plans to replace Section 23 of FRS 102 be affected by feedback received by the IASB in response to its Exposure Draft *Third edition of the IFRS for SMEs Accounting Standard*?

There is no requirement for Section 23 of FRS 102 to be aligned with Section 23 of the *IFRS for SMEs* Accounting Standard. However, we do seek an IFRS-based solution unless an alternative clearly better meets our overriding objective[1]. Accordingly, the proposals in FRED 82 are based on those in IASB/ED/2022/1, which are in turn based on the IFRS 15 model, and we will take an interest in the feedback that the IASB receives, alongside considering the feedback that we receive.

26. Will we be able to recognise all associated costs of sales, such as sales commissions/direct marketing campaigns, over the same basis as the revenue it generates is recognised?

The FRC proposes to permit an entity to recognise as an asset costs incurred in its effort to obtain a contract with a customer, in certain circumstances – please refer to proposed paragraphs 23.102 to 23.104. When an asset is recognised, it will be amortised as set out in proposed paragraph 23.110.

27. Can you discuss what consequential amendments there will be to FRS 103?

FRS 103 and its Implementation Guidance refer to Section 23 of FRS 102, and therefore require consequential amendment. These consequential amendments are included in FRED 82, as are consequential amendments to our other FRSs. Our upcoming roundtables will provide an opportunity to discuss specific proposals in more detail

[1] The FRC's overriding objective in setting accounting standards is 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.

and we encourage stakeholders to complete the survey at www.frc.org.uk/fred82 to let us know if there are particular topics they would like to see covered at those events.

FRS 102 Section 29 *Income Tax*

> 28. Is the FRC going to make a short-term change to FRS 102 similar to the IASB's proposals to amend IAS 12 relating to 'Pillar Two Model Rules'?

The IASB's exposure draft has been published since the publication of FRED 82, with a significantly earlier proposed effective date. This is a good example of the kind of urgent matter than can arise in between periodic reviews. The FRC will consider this matter as a separate project.

Consultation stage impact assessment

> 29. What is the assessed economic cost to businesses to prepare and implement these changes?

The expected costs to business of the proposed changes are set out in the consultation stage impact assessment within FRED 82.

> 30. The cost for each business noted is not realistic.

We expect the costs to fall differently on different-sized entities, and to depend on the extent to which an entity has transactions that fall within the scope of particular sections of the FRC's financial reporting standards. Question 10 of the invitation to comment invites feedback on the consultation stage impact assessment.

> 31. Compared with IFRS preparers, there are many more entities applying the FRC's financial reporting standards, many of which are smaller and with fewer resources and less support.

We appreciate that there is a broad range of entities applying our financial reporting standards and we encourage responses to our consultation from across this range.

Distributable profits

> 32. Do you expect to make changes to UK GAAP for any distributable profit requirements?

No such changes are included in FRED 82. Certain proposals relating to capital maintenance and dividends were included in the Government's response to the consultation *Restoring Trust in Audit and Corporate Governance*. This is outside the scope of the Periodic Review project.

The future of FRS 102

33. Is FRS 102 still required if there are going to be limited remaining GAAP differences to IFRS?

34. If the suggested changes were to be adopted what will be the purpose of having FRS 101, IFRS and FRS 102. Wouldn't this be a duplication of framework?

35. Agree, no need for FRS 102 after expected credit loss changes are dealt with – just UK-adopted IFRS, allowing reduced disclosures for SMEs.

The purpose of FRED 82 is to seek feedback on the proposed amendments to FRS 102 and other FRSs.

Whilst FRS 102 is based, where possible, on international solutions, the FRC's view is that FRS 101, FRS 102 and IFRS Accounting Standards address different needs of users (and preparers). In areas such as revenue and lease accounting where we propose to align towards IFRS solutions, the proposals in FRED 82 include simplifications that would not be available to an entity applying IFRS Accounting Standards. In various other areas, pre-existing GAAP differences also remain between FRS 102 and IFRS Accounting Standards; there are also significant differences in the level of disclosure required.

UK company law provides entities with an option to apply UK-adopted international accounting standards voluntarily. We have not heard support in the past for extending the mandatory application of UK-adopted international accounting standards beyond the scope of the existing legal and regulatory requirements.

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