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Dear Jenny

BDO LLP response to 'FRED 72: Draft amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* - Interest Rate Benchmark Reform'

We are pleased to have the opportunity to comment on 'FRED 72: Draft amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* - Interest Rate Benchmark Reform' (FRED 72).

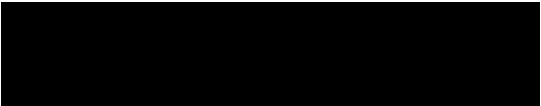
We broadly agree with the proposed amendments to FRS 102 that are set out in FRED 72. We consider that these changes are required in order to avoid unnecessary discontinuation of hedge accounting during the period of uncertainty prior to the interest rate benchmark being replaced. Our responses to the specific questions asked are set out in an appendix to this letter.

We note that the proposed amendments to FRS 102 are based on ED/2019/1 *Interest Rate Benchmark Reform - Proposed amendments to IFRS 9 and IAS 39* (the IASB Exposure Draft), which was published by the IASB in May 2019. We agree that this is the correct approach in order to ensure that the proposed relief is available to all entities applying FRS 102, regardless of their accounting policy choice in relation to financial instruments. Consequently, we also agree that finalisation of the proposed amendments to FRS 102 should take into account any changes made by the IASB on finalisation of its own Exposure Draft in addition to considering respondents' feedback on FRED 72. However, we have the following observations:

- The proposed amendments set out in the IASB Exposure Draft are far more detailed than those set out in FRED 72. As a result, there may inevitably be scope for divergence in practice between IFRSs and FRS 102 reporters and, indeed, between FRS 102 reporters that may interpret the amendments differently.
- While the effective date of FRED 72 aligns to the effective date proposed in the IASB Exposure Draft, we note that for EU IFRS reporters, the actual effective date will depend upon EU endorsement. As such, it is possible that, for a period of time, FRS 102 reporters would be in a position to avail themselves of reliefs that would be unavailable to EU-IFRS reporters.

If you wish to discuss any of the points further, please do not hesitate in contacting me directly.

Yours sincerely,



Nicole Kissun
Partner
For and on behalf of BDO LLP

Appendix: Responses to the questions asked in the Exposure Draft**Question 1****Do you agree with the proposed amendments to FRS 102? If not, why not?**

Yes, we broadly agree with the proposed amendments to FRS 102. We provide our specific comments below.

Section 1 - Scope

We agree with the proposed effective date of accounting periods beginning on or after January 2020 with early application permitted, which is consistent with the proposals contained within the IASB Exposure Draft.

We note, however, that there are no specific transition provisions proposed and, consequently, entities applying these new requirements would do so retrospectively in accordance with paragraphs 10.11(d) and 10.12 of FRS 102. While retrospective application is also consistent with the IASB Exposure Draft, we note that paragraph BC46 of the IASB Exposure Draft goes on to discuss what is meant by retrospective application in this context, noting for example that it would not allow designation in hindsight. We suggest that the FRC might consider whether a similar clarification is required in relation to the retrospective application of the proposed FRS 102 amendments.

Section 12 - Other Financial Instrument Issues

We broadly agree with the proposed amendments to specific hedge accounting requirements set out in paragraphs 7 - 9 of the Exposure Draft but we include below some specific observations for your consideration.

- Paragraph 12.25B proposes that the reliefs only apply to hedging relationships of interest rate risk that are affected by interest rate benchmark reform. We note that, in some cases, interest rate benchmark reform might affect hedge relationships where interest rate risk is not the only hedged risk, for example in cases where both interest rate and foreign currency risk are hedged using a cross-currency swap. In such cases, we consider that the proposed reliefs should apply to the interest rate cash flows affected by interest rate benchmark reform. In order to address this point, we suggest that paragraph 12.25B could be amended as follows:

'Paragraphs 12.25C to 12.25G only apply to hedging relationships of interest rate risk that are affected by interest rate benchmark reform [...].'

- We agree with the proposed reliefs from specific hedge accounting requirements set out in paragraphs 12.25C - 12.25F, which are consistent with those proposed by the IASB Exposure Draft and necessary to avoid discontinuation of hedge accounting during the period of uncertainty prior to the interest rate benchmark being replaced.

However, we consider that it would be helpful to clarify that the proposed reliefs are not intended to change the measurement of hedge effectiveness or to change how hedges are reflected in the financial statements. For example, the fair values of hedged items and hedging instruments might be affected by uncertainties relating to interest rate benchmark reform and this may give rise to ineffectiveness. Similarly, it is possible that the timing of the change in rate for the hedged item and the hedging instrument could be different, giving rise to additional ineffectiveness. While the application of the proposed reliefs may permit such hedge relationships to continue, in our view, any ineffectiveness arising should be recognised and measured in the financial statements in accordance with the normal requirements of FRS 102. We note that paragraph BC22 of the IASB Exposure Draft contains a similar clarification.

- Paragraph 12.25G stipulates the point at which an entity should cease to apply the proposed reliefs in paragraph 12.25C - 12.25E. We assume that an entity should cease applying the reliefs *at the earlier of* meeting one of the criteria listed in sub paragraphs (a) - (c) and as such we suggest that paragraph 12.25G should be amended as follows:

‘An entity shall cease applying paragraphs 12.25C to 12.25E ~~when~~ at the earlier of: [...]’

- Paragraph 12.30 refers to disclosure requirements and specifically the need to consider requirements of paragraphs 8.6 and 8.7 (Information about judgments and key sources of estimation uncertainty). In addition, the FRC may wish to consider whether the disclosure requirements set out in paragraphs 12.27-12.29 of FRS 102 should be disaggregated between those hedge relationships that are affected by interest rate benchmark reform and those that are not.

We also note that absent any specific relief, on initial application of the new requirements, an entity would be required to apply the disclosure requirements of paragraph 10.13 (Disclosure of a change in accounting policy). We consider that the numerical aspect of these disclosures would be an onerous requirement that would provide little benefit to users of financial statements given that the primary reason for the relief is to avoid the unnecessary discontinuation of hedge due to interest rate benchmark reform. We suggest that the FRC considers providing specific relief from this aspect of these requirements in order to reduce the risk of inconsistent and potentially inappropriate use of the ‘impracticable’ exemption included within that paragraph.

Replacement Issues

We note that the IASB is intending to assess the potential financial reporting implications arising from the actual replacement of interest rate benchmarks (Replacement Issues) during Q3 2019. We would similarly urge the FRC to consider such Replacement Issues and the need for potential amendments to FRS 102 as soon as possible.

Question 2

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

We have no comments on the costs and benefits identified in the consultation stage impact assessment.