Exposure Draft

Financial Reporting Council

December 2015

FRED 63
Draft amendments to FRS 101 *Reduced Disclosure Framework*

2015/16 cycle

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries, and oversee the regulatory activities of the accountancy and actuarial professional bodies.

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Contents

Summary

(i) With effect from 1 January 2015, the Financial Reporting Council (FRC) revised financial reporting standards in the United Kingdom and Republic of Ireland. The revisions fundamentally reformed financial reporting, replacing the extant standards with five Financial Reporting Standards:

(a) FRS 100 *Application of Financial Reporting Requirements*;

(b) FRS 101 *Reduced Disclosure Framework*;

(c) FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*;

(d) FRS 103 *Insurance Contracts*; and

(e) FRS 104 *Interim Financial Reporting*.

The FRC has also issued FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* to support the implementation of the new micro-entities regime.

This FRED proposes limited amendments to FRS 101.

(ii) 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.

(iii) In meeting this objective, the FRC aims to provide succinct financial reporting standards that:

(a) have consistency with international accounting standards through the application of an IFRS-based solution unless an alternative clearly better meets the overriding objective;

(b) reflect up-to-date thinking and developments in the way entities operate and the transactions they undertake;

(c) balance consistent principles for accounting by all UK and Republic of Ireland entities with practical solutions, based on size, complexity, public interest and users' information needs;

(d) promote efficiency within groups; and

(e) are cost-effective to apply.

Draft amendments to FRS 101

(iv) After considering the 2015/16 annual review of FRS 101 this FRED proposes amendments to FRS 101 to provide certain disclosure exemptions in relation to IFRS 15 *Revenue from Contracts with Customers* and clarify a legal requirement relating to the order in which the notes to the financial statements are presented.

Invitation to comment

1 The FRC is requesting comments on FRED 63 by 31 March 2016. The FRC is committed to developing standards based on evidence from consultation with users, preparers and others. Comments are invited in writing on all aspects of the draft standard. In particular, comments are sought in relation to the questions below.

Question 1

The principles for determining whether disclosure exemptions from EU-adopted IFRS should be available in FRS 101 are set out in paragraph 9 of the Accounting Council's Advice. These are relevance, cost considerations and avoiding gold plating.

Qualifying entities have limited external users of the financial statements. These external users are likely to be providers of credit with a greater focus on information that supports the statement of financial position of the qualifying entity, when compared with detailed analysis of performance as required by some of the disclosures in IFRS 15 *Revenue from Contracts with Customers*. Do you agree?

Question 2

Do you consider that additional refinements could be made to the principles set out in paragraph 9 of the Accounting Council's Advice that, when applied, would help to increase further the cost-effectiveness of FRS 101?

Question 3

Do you agree with the proposed amendments to FRS 101? If not, why not?

Question 4

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 of the quantifiable costs or benefits of these proposals.

2 Information on how to submit comments and the FRC's policy in relation to responses is set out on page 13.

[Draft] Amendments to FRS 101 *Reduced Disclosure Framework*

[Draft] Amendments to FRS 101

1 The following paragraphs set out the [draft] amendments to FRS 101 *Reduced Disclosure Framework* (inserted text is underlined).

2 Paragraph 8(eA) is inserted as follows:

<u>8(eA) The requirements of the second sentence of paragraph 110 and paragraphs 113 to 115, 118 to 127 and 129 of IFRS 15 *Revenue from Contracts with Customers*.</u>

[Draft] Amendments to Appendix II: Note on Legal Requirements

3 The following paragraphs set out the [draft] amendments to Appendix II: *Note on Legal Requirements* (inserted text is underlined).

4 Paragraph A2.11A and the sub-heading preceding it are inserted as follows:

<u>Notes to the financial statements</u>

<u>A2.11A Paragraph 42(2) of the Regulations requires the notes to the financial statements to be presented in the order in which, where relevant, the items to which they relate are presented in the statement of financial position and the income statement. A qualifying entity preparing financial statements in accordance with FRS 101 shall have regard to this requirement when determining a systematic manner for the presentation of its notes to the financial statements in accordance with paragraphs 113 and 114 of IAS 1.</u>

The Accounting Council's Advice to the FRC to issue FRED 63 *Draft amendments to FRS 101 – 2015/16 cycle*

Introduction

1 This report provides an overview of the main issues that have been considered by the Accounting Council in advising the Financial Reporting Council (FRC) to issue FRED 63 *Draft amendments to FRS 101 Reduced Disclosure Framework – 2015/16 cycle*.

2 The FRC, in accordance with the *Statutory Auditors (Amendment of Companies Act 2006 and Delegation of Functions etc) Order 2012* (SI 2012/1741), is a prescribed body for issuing accounting standards in the UK. The *Foreword to Accounting Standards* sets out the application of accounting standards in the Republic of Ireland.

3 In accordance with the *FRC Codes and Standards: procedures*, any proposal to issue, amend or withdraw a code or standard is put to the FRC Board with the full advice of the relevant Councils and/or the Codes & Standards Committee. Ordinarily, the FRC Board will only reject the advice put to it where:

(a) it is apparent that a significant group of stakeholders has not been adequately consulted;

(b) the necessary assessment of the impact of the proposal has not been completed, including an analysis of costs and benefits;

(c) insufficient consideration has been given to the timing or cost of implementation; or

(d) the cumulative impact of a number of proposals would make the adoption of an otherwise satisfactory proposal inappropriate.

4 The FRC has established the Accounting Council as the relevant Council to assist it in the setting of accounting standards.

Advice

5 The Accounting Council is advising the FRC to issue FRED 63 *Draft amendments to FRS 101 Reduced Disclosure Framework – 2015/16 cycle.*

6 The Accounting Council advises that these proposals will ensure that FRS 101 *Reduced Disclosure Framework* continues to be effective in providing disclosure reductions when compared with EU-adopted IFRS and maintains consistency with company law.

7 When these draft amendments are finalised the Accounting Council's Advice to the FRC in respect of these amendments will be added into FRS 101.

Background

8 The Accounting Council advised the FRC to update FRS 101 at regular intervals to ensure that the reduced disclosure framework continues to be effective in providing disclosure reductions when compared with EU-adopted IFRS. An annual review is carried out to consider changes in IFRS and their potential impact on FRS 101.

Draft amendments to FRS 101

9 The Accounting Council advised the FRC that the following principles should be applied when determining which of the disclosure requirements in EU-adopted IFRS should be applied by qualifying entities:

(1) Relevance:

Does the disclosure requirement provide information that is capable of making a difference to the decisions made by the users of the financial statements of a qualifying entity?

(2) Cost constraint on useful financial reporting:

Does the disclosure requirement impose costs on the preparers of the financial statements of a qualifying entity that are not justified by the benefits to the users of those financial statements?

(3) Avoid gold plating:

Does the disclosure requirement override an existing exemption provided by company law in the UK?

IASB projects completed since the 2014/15 cycle

10 The IASB has completed four projects since those considered in the review for the 2014/15 cycle, which was performed in August 2014. In addition, one project was brought forward for consideration as part of this review.

	IASB project	Date issued	Date effective	Date endorsed in the EU
1	Equity Method in Separate Financial Statements (Amendments to IAS 27)	Aug 2014	1 Jan 2016	Expected Q4 2015
2	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)	Sept 2014	1 Jan 2016	Postponed
3	Annual Improvements to IFRSs (2012 – 2014 Cycle)	Sept 2014	1 Jan 2016	Expected Q4 2015
4	Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10, IFRS 12 and IAS 28)	Dec 2014	1 Jan 2016	Expected Q1 2016
5	Disclosure Initiative (Amendments to IAS 1)	Dec 2014	1 Jan 2016	Expected Q4 2015

11 The amendments[1] resulting from these five projects were reviewed in the context of the reduced disclosure framework for any amendments that:

(a) alter disclosure requirements, as consideration will need to be given to whether changes should be made to the disclosure exemptions permitted in FRS 101; and/or

(b) are inconsistent with current UK legal requirements, as consideration will need to be given to whether changes should be made to the Application Guidance: *Amendments to International Financial Reporting Standards as Adopted in the European Union for Compliance with the Act and the Regulations* to FRS 101.

[1] The full IASB documents setting out the amendments for each project are available on the IASB website (www.ifrs.org).

12 The Accounting Council advises that only limited amendment to FRS 101 are necessary in relation to these amendments to IFRS. These are discussed below.

Equity method in separate financial statements

13 Following changes that implemented the EU Accounting Directive, company law now permits the use of the equity method in an entity's individual financial. As a result, the Accounting Council advises that no amendments to FRS 101 are necessary in relation to the recent amendment to IAS 27 *Separate Financial Statements*.

Disclosure initiative

14 The Accounting Council notes that this project was intended to clarify existing requirements and give greater guidance, particularly on the application of materiality to disclosures, the levels of aggregation (or disaggregation) permitted and the order in which notes might be presented. As a result it did not change disclosure requirements.

15 However, one area where additional guidance was included relates to the systematic manner in which the notes to the financial statements are presented. Company law contains a requirement about the order in which the notes to the financial statements shall be presented. The amendments to IAS 1 *Presentation of Financial Statements* paragraphs 113 and 114 do not require entities to present notes to the financial statements in an order that would conflict with this legal requirement. However, some of the examples of how to present notes in a systematic manner are unlikely to comply with company law. Therefore the Accounting Council advises including an additional paragraph (paragraph A2.11A) in Appendix II: *Note on legal requirements* to discuss this issue.

IFRS 15 Revenue from Contracts with Customers

16 The disclosure requirements of IFRS 15 have been compared to the principles set out in paragraph 9. In doing so, the Accounting Council considered further how the principle of 'relevance' should be applied in the context of disclosure by qualifying entities. It noted that qualifying entities usually have few users of their financial statements, and particularly few users that would be external to the group the qualifying entity is part of. Any external users are likely to be providers of credit to the qualifying entity.

17 The Accounting Council considered that the interest a provider of credit has in the financial statements of a qualifying entity is generally likely to be focused on information about the liquidity and solvency of the qualifying entity, that might be relevant to the ability of the qualifying entity to pay (or repay) any credit advanced. This would mean that in relation to detailed disclosures, there would be greater interest in information supporting the statement of financial position, rather than information supporting the income statement. The Accounting Council therefore advises refining the application of the principle of 'relevance' in relation to disclosure by a qualifying entity to note that information supporting items in the income statement is less likely to make a difference to users' decisions than information supporting items in the statement of financial position.

18 As a result, the Accounting Council advises that significant disclosure exemptions from IFRS 15 should be available to qualifying entities. The Accounting Council also noted that, in addition, there are company law requirements relating to disaggregation of turnover and that IAS 1 contains requirements relating to judgements having a significant effect on the amounts recognised in an entity's financial statements.

19 The Accounting Council advises that disclosure exemptions from paragraphs 113 to 115, 118 to 127 and 129 should be available. In addition, an exemption from the second sentence of paragraph 110 should be provided to remove the cross-references to these later paragraphs.

Effective date

20 Paragraph 8 of FRS 101 notes that the exemptions are available from when the relevant standard is applied. Therefore there is no need to amend the effective date for these proposed amendments. However, it should be noted that the change in company law to permit the equity method in individual financial statements is effective from 1 January 2016 (or 1 January 2015 if it is applied early), which is the same date as the amendment to IAS 27 *Separate Financial Statements*.

Consultation stage impact assessment

Introduction

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

Draft amendments to FRS 101

2 FRS 101 *Reduced Disclosure Framework* is an optional standard that is intended to enable cost-efficient financial reporting within groups, particularly those applying EU-adopted IFRS in their consolidated financial statements. Therefore it is only applied by those qualifying entities that consider it a cost-effective option for the preparation of their individual financial statements.

3 FRS 101 requires an entity to apply EU-adopted IFRS subject to specified disclosure exemptions. Therefore without intervention to amend FRS 101, an entity applying FRS 101 would need to provide all the disclosures required by IFRS 15 *Revenue from Contracts with Customers* from the date that it applies that standard.

4 The draft amendments to FRS 101 provide disclosure exemptions from certain of the disclosures that would otherwise be required by IFRS 15, and are therefore expected to reduce the cost of compliance with FRS 101.

Conclusion

5 The FRC believes that the draft amendments to FRS 101 will have a positive impact on financial reporting and reduce the costs of compliance.

This draft is issued by the Financial Reporting Council for comment. It should be noted that the draft may be modified in the light of comments received before being issued in final form.

For ease of handling, we prefer comments to be sent by e-mail to:

ukfrs@frc.org.uk

Comments may also be sent in hard copy to:

Jenny Carter
Financial Reporting Council
8th Floor
125 London Wall
London
EC2Y 5AS

Comments should be despatched so as to be received no later than 31 March 2016.

The FRC's policy is to publish on its website all responses to formal consultations issued by the FRC unless the respondent explicitly requests otherwise. A standard confidentiality statement in an e-mail message will not be regarded as a request for non-disclosure. The FRC does not edit personal information (such as telephone numbers or postal or e-mail addresses) from submissions; therefore, only information that you wish to be published should be submitted.

The FRC aims to publish responses within 10 working days of receipt.

The FRC will publish a summary of the consultation responses, either as part of, or alongside, its final decision.

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