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Dear Accounting and Reporting Policy team,

Mazars LLP response to FRED 82

Mazars LLP is the UK firm of Mazars, an international, integrated and independent organisation specialising in audit, accountancy and advisory services. We welcome the publication of FRED 82 *Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and other FRSs – Periodic Review* and are pleased to submit our response.

Mazars operates as a truly internationally integrated partnership in 95 countries and territories, with 47,000 professionals. In the UK, Mazars is among the largest firms in its sector and a leading auditor to Public Interest Entities (PIEs). It employs over 2,500 people in 15 locations across the UK, providing a balanced perspective and empowered expertise to clients of all sizes, from individuals and SMEs to mid-caps and global players, as well as start-ups and public organisations at every stage of their development.

General remarks

As part of this periodic review the Financial Reporting Council (FRC) is proposing changes to revenue recognition and lease accounting requirements as well as some other substantive changes mainly to align with amendments made by the International Accounting Standards Board (IASB) to International Financial Reporting Standards (IFRS) or the *IFRS for SMEs* Accounting Standard (IFRS for SMEs).

We continue to support the FRC's basic principle of developing UK and Ireland GAAP consistently with global accounting standards. However, when developing the new lease accounting and revenue accounting requirements, we believe the FRC should focus more on proportionality and practical solutions, which in our view should go beyond providing simplifications or additional options compared to IFRS.

We also believe the FRC should redeliberate on the expected costs and benefits of the proposed amendments in particular relating to the proposed changes to the concepts and pervasive principles and their alignment with the IASB's *Conceptual Framework for Financial Reporting* (Conceptual Framework). The FRC may wish to defer its decision on these changes.

We acknowledge that the FRC has, post-Brexit, more flexibility in mandating disclosures for small UK entities as set out in Section 1A of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (FRS 102), but we believe the FRC should use its new powers to reconsider the disclosure regime for small UK entities more holistically. On balance, given there is no clear evidence that the existing disclosure regime is broken, we would prefer to retain existing disclosure requirements.

Mazars LLP
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We believe the proposals to align the requirements for premium recognition of insurance contracts in FRS 103 *Insurance Contracts* with those in FRS 102 require more thought and analysis by the FRC. As proposed, we do not support the amendments.

The proposed effective date of 1 January 2025 for these amendments is going to be challenging to meet given the nature of the proposed changes. Furthermore, it may be necessary to re-expose certain aspects of the proposals and if so, the FRC's implementation timetable would need to be revised. Given the pervasive effect of the proposed changes we believe it is important for the FRC to take the time necessary to finalise the proposals so they are suitable for application by UK and Republic of Ireland entities reporting under FRS 102.

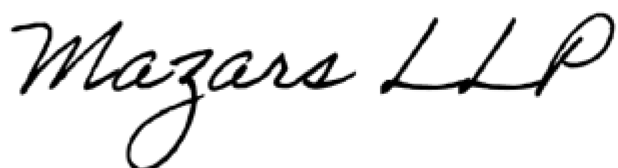
We note that the FRC has postponed its decision on whether to introduce an expected credit loss model for the impairment of financial assets. We do not favour the FRC's preferred approach to determine the scope by nature of activity or type of entity as this would result in sector specific recognition and measurement requirements. We believe the proposed approach by the IASB for the IFRS for SMEs to define scope by type of financial asset has some merits and therefore could be explored by the FRC. Ultimately a decision on the need of this model should be taken together with UK and Republic of Ireland prudential regulators which in our view are the key stakeholders on this topic.

The FRC is an organisation that champions digital reporting by UK entities. We had therefore expected that this periodic review would be an opportunity for the FRC to consider how it could make access and navigation in its own accounting standards easier for users. The existing pdf documents are time-consuming to search and navigate. We believe this is an area where the FRC can enhance its digital offering.

We also encourage the FRC to reconsider whether a committee similar to the IASB's IFRS Interpretation Committee could fit within its governance structure. At the moment, it is not transparent to external stakeholders how the FRC identifies urgent practical issues arising in the UK and Republic of Ireland and how they are dealt with unless they result in a proposed change. Greater transparency over the FRC's processes and decision making would be helpful for stakeholders and foster consistency of financial reporting.

We have set out our responses to the consultation questions in the Appendix below. If you would like to discuss any of our comments in more detail, please get in touch with us.

Sincerely,



Appendix:

Question 1: Disclosure

Do you have any comments on the proposed overall level of disclosure required by FRS 102?

Do you believe that users of financial statements prepared under FRS 102 will generally be able to obtain the information they seek? If not, why not?

Section 1A of FRS 102:

We note the FRC's new post-Brexit powers to require additional disclosures for small UK entities as set out in paragraph A.45. The additional disclosures proposed by the FRC would appear modest in scope and in our view the effort and cost to produce them should be limited. Nevertheless, it is not entirely clear why the FRC has identified these specific disclosures as important for small UK entities. For example, the existing disclosure requirements in relation to the income statement are relatively limited for small entities and there may be useful disclosure that could be added, especially in the context of the Companies House reform noted in paragraph B1A.5 and the new requirement for small companies to file their profit and loss account.

We believe some small UK entities may welcome the approach of more mandated disclosures, if it reduces their judgements on whether all relevant disclosures to show a true and fair view have been made. Others may view it as a new compliance burden and we note the FRC has not commented on how its new approach of additional disclosure requirements is aligned with the UK Government's general approach of seeking to reduce the regulatory burden for UK business and make them more competitive post-Brexit. It is also not clear how much flexibility the FRC has, i.e. has the FRC the ability to reconsider the disclosure regime for small UK entities more holistically, or is the FRC restricted to imposing some new disclosure requirements?

In our view the FRC should decide on whether to mandate for small UK entities all the disclosures they would typically need to provide, similar to the approach applicable to other entities reporting under FRS 102 as described in paragraph 3.2. Paragraph 1A.6 would then be redundant for small UK entities. Alternatively, the FRC should retain the existing disclosure approach for UK and Republic of Ireland small entities as in the extant Section 1A, possibly augmenting the list of suggested disclosures. The proposed approach by the FRC appears to be something in the middle, i.e. there are more mandated disclosures, but small entities still have the burden of making judgements on true and fair under paragraph 1A.6. We find this unsatisfactory. If the FRC believes the new disclosures are sufficient for small UK entities, then a statement to that effect would be helpful.

Other considerations

It is not clear whether the FRC is also seeking views on other aspects of the existing disclosure regime as part of this review of FRS 102. The FRC has not set out its rationale for seeking this feedback, for example by identifying any concerns that have been raised by stakeholders or issues that have been identified by the FRC's Corporate Reporting Review function.

We are of the view that the more limited disclosure requirements in FRS 102 compared to IFRS are justified and provide adequate information for users.

We have one further comment linked to Question 4 and the expected credit loss model. The FRC may explore, as an alternative model to the expected credit loss approach, enhanced disclosures by financial institutions. Although the level of information on credit losses by banks currently reporting under IFRS 9 *Financial Instruments* (IFRS 9) can be overwhelming, the disclosures required under FRS 102 are in comparison basic and provide much less insight.

Question 2: Concepts and pervasive principles

The proposed revised Section 2 *Concepts and Pervasive Principles* of FRS 102 and FRS 105 would broadly align with the IASB's 2018 Conceptual Framework for Financial Reporting.

The IASB's Exposure Draft Third edition of the IFRS for SMEs Accounting Standard (IASB/ED/2022/1) contains similar proposals. The FRC considers it appropriate that FRS 102 and FRS 105 should be based on the same concepts and pervasive principles as IFRS Accounting Standards including the IFRS for SMEs Accounting Standard, given the FRC's aim of developing financial reporting standards that have consistency with global accounting standards.

The FRC has made different decisions from the IASB in some respects in developing proposals to align FRS 102 and FRS 105 with the 2018 Conceptual Framework in a proportionate manner.

Do you agree with the proposal to align FRS 102 and FRS 105 with the 2018 Conceptual Framework? If not, why not?

This FRED, and IASB/ED/2022/1, propose to continue using the extant definition of an asset for the purposes of Section 18 *Intangible Assets other than Goodwill* and the extant definition of a liability for the purposes of Section 21 Provisions and Contingencies of FRS 102. This is consistent with the approach taken in IAS 38 *Intangible Assets* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* which use the definitions of an asset and a liability from the IASB's 1989 Framework for the Preparation and Presentation of Financial Statements. Do you agree with this approach? If not, why not?

Do you have any other comments on the proposed revised Section 2?

We understand the FRC's rationale presented in paragraph B2.2 for introducing the concepts of the IASB's Conceptual Framework. However, we miss an analysis by the FRC of the possible effects of these changes. In addition, it would have been helpful for the FRC to highlight and explain the simplifications it has made compared to the wording proposed for the IFRS for SMEs as per paragraph B2.3.

We note that the proposed amendments increase the length and complexity compared to the previous version of this section. Consequently, we are concerned how these changes fit with the FRC's objectives of proportionality, practicability and suitability for UK entities applying FRS 102. We therefore believe more work needs to be done to tailor the requirements and make them more accessible. An analysis of the practical impact of changes to the qualitative criteria and the definitions of assets and liabilities should be performed, so to avoid unintended consequences.

For example, in respect of the new qualitative criterion "faithful presentation", it is not clear whether and if so how this is linked to the concept of true and fair in Section 3 *Financial Statement Presentation* of FRS 102. Does the FRC intend to use references to the "objective of financial statements" and "objective of general purpose financial statements" in this section interchangeably or not? More clarity is needed.

Proposed paragraph 2.4 sets out that general purpose financial statements should provide information to a wide range of users. On the other hand proposed paragraph 2.6 refers to existing and potential investors, lenders and other creditors as users. Proposed paragraph 2.27 makes reference to the efficient functioning of capital markets and lower cost of capital, which seem to be objectives more relevant for publicly listed entities, rather than those reporting under FRS 102.

We also have some observations in relation to the definition of materiality. The FRC has promulgated IAS (UK) 320 *Materiality in planning and performing and audit* (ISA 320). As per ISA 320, materiality as defined in the financial reporting framework is the frame of reference for an auditor to determine materiality. However, there would seem to be some differences in the discussion of the concept of materiality in IAS 320 and the definition proposed in this FRED. For example, ISA 320 refers to "economic decisions" whilst FRS 102 refers to "decisions" by users, the latter would appear to be a wider concept and include ESG and other social responsibility matters. Information needs are assessed considering investors that provide risk capital under ISA 320, whilst the general purpose financial statements as defined in FRS 102 would appear wider as it includes a 'wide range of users'.

It would be helpful for the FRC to align its requirements or at least confirm what is intended and which framework auditors should apply.

In relation to going concern, we believe the drafting should be completely aligned in proposed paragraph 2.32 and paragraph 3.8, as this is an area where words matter.

In conclusion we do not believe it is necessary for the FRC to make the proposed changes, but if the FRC proceeds there needs to be a more thorough effects analysis. This is particularly important given that contrary to the IASB's Conceptual Framework, this is part of the standard and it hence would be mandatorily applicable. In our experience the concepts and principles of Section 2 are more often used and relied upon in practice, than perhaps the Conceptual Framework, as FRS 102 is a less prescriptive accounting framework.

We note that the title of this section refers to Concepts and Pervasive Principles, which is also referred to in other parts of FRS 102, for example paragraph 10.5. Given that there is no heading in this Section itself that refers to 'concepts' or 'pervasive principles' it is not clear what requirements is exactly being referred to or indeed whether it is intended to refer to all requirements in this Section. We ask the FRC to review internal references and headings so references are unambiguous.

For reasons set out above we would also advise caution with making equivalent amendments to FRS 105. If the FRC was to proceed it should consider tailoring the requirements, so they are more suitable for micro-entities.

Question 3: Fair value

The proposed Section 2A *Fair Value Measurement* of FRS 102 would align the definition of fair value, and the guidance on fair value measurement, with that in IFRS 13 *Fair Value Measurement*. Do you agree with this proposal? If not, why not?

Do you agree with the proposed consequential amendment to Section 26 *Share-based Payment* of FRS 102 to retain the extant definition of fair value for the purposes of that section? If not, why not?

We concur with the FRC's proposal to include the fair value measurement requirements in a new stand-alone section of FRS 102. The fair value measurement basis is a concept that is accepted and has matured within the UK GAAP reporting framework since FRS 102 was introduced. Incorporating more comprehensive requirements based on IFRS 13 *Fair Value Measurement* (IFRS 13) into FRS 102 will in our view foster consistency of application.

We do not believe that pervasive changes will be needed for entities to develop fair value measurements under the new requirements. Nevertheless, the new requirement to base fair value on the 'highest and best use' may drive a difference for entities that have not taken this into consideration previously, because it was not explicitly required.

We support calls from other stakeholders to introduce these changes prospectively. We also would like the FRC to clarify whether proposed Section 2A would set mandatory requirements or as implied by the question above, non-mandatory "guidance". It is important that the scope of this section is clear.

The FRC is also proposing to align the definition of fair value with that in IFRS 13. Existing accounting literature suggests that there is an intended difference between measurement of a liability based on: (i) the amount for which it could be settled (old definition); and (ii) the price paid for it in a transfer (new definition), which affects, in particular financial liabilities. Given existing disclosure requirements in paragraph 11.48A on own credit risk, accounting literature suggested that there is an accounting policy option whether or not to incorporate own credit risk into the fair value measurement of a financial liability under FRS 102. The FRC is not proposing to incorporate the specific requirement of IFRS 13 paragraph 42 which specifies that the fair value of a liability reflects the effect of non-performance risk, which includes an entity's own credit risk. It is not clear whether the FRC intended this specific requirement of IFRS 13 to apply in FRS 102 or not and therefore whether the FRC intended to remove the existing accounting policy choice under current FRS 102 or not. We

believe the FRC should clarify the position whether financial liabilities are required to be measured including non-performance risk as required under IFRS 13 or whether this continues to be an option.

If entities were required to include non-performance risk in the fair value measurement of a liability, we would find it useful for the FRC to clarify where gains and losses relating to own-credit risk should be recorded. Paragraph 40 of Schedule 1 to *The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008* and FRS 102 (depending on accounting policy choice for financial instruments) requires all fair value gains and losses, including for own-credit risk to be included in profit and loss. This may result in counterintuitive accounting, which is why the IASB decided to include these gains and losses in other comprehensive income instead. The FRC should clarify whether it expects entities to apply a true and fair override and record such gains and losses in other comprehensive income (as suggested in paragraph A3.12C for entities applying the IFRS 9 option) or whether they should be presented in profit and loss by entities that do not apply the IFRS 9 option for financial instruments accounting.

On the basis that the IASB was unable to develop a fair value definition that could be applied to all IFRSs, we concur with the FRC's proposal to scope share-based compensation and lease accounting out of this section and apply the extant definition of fair value in respect of these requirements.

Question 4: Expected credit loss model

The FRC intends to defer its conclusion as to whether to align FRS 102 with the expected credit loss model of financial asset impairment from IFRS 9 *Financial Instruments* pending the issue of the IASB's third edition of the IFRS for SMEs Accounting Standard. Any proposals to align with the expected credit loss model will therefore be presented in a later FRED. Do you agree with this approach? If not, why not?

In IASB/ED/2022/1 the IASB proposes to retain the incurred loss model for trade receivables and contract assets and introduce an expected credit loss model for other financial assets measured at amortised cost. The FRC's preliminary view is that, in the context of FRS 102, it may be appropriate to require certain entities to apply an expected credit loss model to their financial assets measured at amortised cost but allow other entities to retain the incurred loss model. Do you agree with this view? If not, why not?

Based on stakeholder feedback received to date, the FRC does not intend to use the existing definition of a financial institution to define the scope of which entities should apply an expected credit loss model. The FRC's preliminary view is that it may be appropriate to define the scope based on an entity's activities (such as entering into regulated or unregulated credit agreements as lender, or finance leases as lessor), or on whether the entity meets the definition of a public interest entity. Do you have any comments on which entities should be required to apply an expected credit loss model?

The FRC had indicated previously that this aspect of accounting is a key potential amendment for this periodic review. Although we concur with the FRC's conclusion to postpone its decision, we believe the FRC has missed an opportunity to present a comprehensive analysis of the options available. It is, for example, not clear from the current proposals whether, and if so why, the FRC believes it is necessary to introduce an expected credit loss model in FRS 102. We are concerned that a future FRED will contain detailed drafting proposals, rather than seeking views on different options, including not to introduce an expected credit loss model in FRS 102 at all.

In our view the implementation experience under IFRS 9 has made stakeholders concerned about the potential cost and efforts involved. They therefore contest that any benefits outweigh the costs. Implementation experience would also indicate that the highest costs would fall on building societies and similar institutions. For other entities, the implementation costs would appear to be more modest, including for insurers as many measure their financial assets at fair value.

The expected credit loss model was introduced following the 2008 banking crisis and a key driver of reform were prudential regulators. We therefore believe a decision on whether entities reporting under FRS 102 should apply this model, ultimately falls on, or is at least unreservedly backed by, UK and Republic of Ireland prudential regulators. We believe prudential regulators are the key stakeholders

that could have an interest in the expected credit loss information. Other stakeholders may, given the significant compliance costs, prefer the status quo.

The IASB is in the process of the post-implementation review ('PIR') of the impairment requirements in IFRS 9. Whilst the outcome of the PIR is not known, we do not expect a significant shift from the existing reporting requirements, in particular we do not expect the IASB to revert back to an incurred loss model. There may be some lessons in terms of simplification, but since the model is now implemented, there may be limited appetite from stakeholders for change. It is currently not clear whether the IASB will implement an expected credit loss model in the IFRS for SMEs. The responses from stakeholders have been cautious on whether the benefits will outweigh the costs. Therefore, there is no clear picture on the whether the IASB will move to an expected credit loss approach for all entities or exclude SMEs. Despite these uncertainties, we think the FRC can move forward with its own assessment.

The FRC's preferred approach would seem to mandate an expected credit loss approach based on type of entity. We are concerned that this would lead into sector specific accounting rules and would mark the departure from generally applicable accounting requirements to all entities. We believe this is a significant step and the implications on other sectors and their specific accounting needs should be assessed before proceeding. We would also advise against adding new definitions or sub-definitions of financial institutions to FRS 102 to define the scope. If the FRC were to define the scope based on type of financial institution it needs to look at the scope of the disclosure requirements for 'financial institutions' in Section 34. We do not support various definitions of financial institutions as this increases complexity unnecessarily, an example of this is narrative reporting, where multiple versions of similar, but not identical scope definitions apply.

The FRC is also seeking views on whether an expected credit loss approach should apply to entities that are PIEs. The definition is under review and therefore it is not clear which entities would eventually be required to adopt the expected credit loss model. That said, as noted above, we would be cautious about defining the scope of recognition and measurement requirements by type of entity. We also note that, although entities that fall under the PIE definition would be expected to be more sophisticated and possibly be more capable of implementing an expected credit loss approach, the PIE definition was introduced to drive enhanced disclosures and transparency as there is a greater information need from stakeholders. It is not clear how the application of an expected credit loss fits within this objective.

If the FRC wishes to move ahead with proposals to introduce an expected credit loss approach, we believe the scope as defined by the IASB for the IFRS for SMEs could be explored by the FRC. It avoids introducing sector specific recognition and measurement requirements and would seem more aligned with existing standard setting, for example insurance contract accounting, which is applicable to all entities that hold such contracts. For those financial assets where an incurred loss model would remain applicable, this could be optional, and provided the incurred loss model is limited to trade receivables and contract assets as proposed by the IASB we would not expect there to be material differences between an incurred and expected credit loss model. Alternatively, if the FRC was to proceed with an expected credit loss model but not follow the IFRS for SMEs approach we would prefer that the expected credit loss model applies to all entities and all financial assets measured at amortised cost.

Question 5: Other financial instruments issues

When it has reached its conclusion as to whether to align FRS 102 with the expected credit loss model, the FRC intends to remove the option in paragraphs 11.2(b) and 12.2(b) of FRS 102 to follow the recognition and measurement requirements of IAS 39 *Financial Instruments: Recognition and Measurement*. This intention was communicated in paragraph B11.5 of the Basis of Conclusions to FRS 102 following the Triennial Review 2017. In preparation for the eventual removal of the IAS 39 option, the FRC proposes to prevent an entity from newly adopting this accounting policy. Do you agree with this proposal? If not, why not?

Temporary amendments were made to FRS 102 in December 2019 and December 2020 in relation to interest rate benchmark reform (IBOR reform). The FRC intends to consider, alongside the future consideration of the expected credit loss model, whether these temporary amendments have now served their purpose and could be removed. Do you support the deletion of these temporary amendments? If so, when do you think they should be deleted? If not, why not?

We concur with the FRC's decision to defer the removal of the IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39) option. We believe such a decision should be postponed until the FRC decides whether or not to introduce an expected credit loss approach for impairment of financial assets measured at amortised cost (see Question 4 above). We believe clarity around whether, and if so how, an expected credit loss approach is implemented in FRS 102 will be an important factor for entities when deciding to adopt FRS 102 or IFRS 9.

We note that IAS 39 and FRS 102 share commonalities between their recognition, measurement and classification requirements. Therefore, as they are relatively aligned, it would seem unnecessary to remove the IAS 39 option. However, once the IASB has finalised its project on Dynamic Risk Management, IAS 39 will be entirely superseded. The IASB has already said it will not maintain IAS 39 and we therefore concur with the FRC that at some point the IAS 39 option will need to be removed. Drawing stakeholders' attention to this inevitable course of action early is important, so they can make informed decision on which accounting option they wish to apply. Nevertheless, beyond the signalling effect that this option will be removed in the future, the benefit of not allowing entities to choose IAS 39 as their accounting option is less clear. Why should an entity that is applying IAS 39 prior to moving to FRS 102 be prohibited from using this option, when other entities still apply that standard? This scenario will become more uncommon in practice after insurers have made their choice on whether to move from IFRS to UK GAAP, however it may still be a possibility.

We would prefer for the FRC to wait until a decision on the expected credit loss has been taken before removing options currently available in relation to financial instruments accounting. The FRC could set a strong signal by including a footnote in the standard. We also believe entities will need to be given good time to transition from IAS 39 once the FRC has decided to remove this option. In our experience there are many financial institutions which use the IAS 39 option and the impact should therefore not be underestimated.

Although the IBOR reform amendments are temporary in nature and their removal would cut some length in the standard, we do not believe the FRC should remove the requirements prior to the IASB making equivalent changes to IFRS.

We would also like to draw your attention to a drafting error in paragraph 11.25(b) which makes reference to paragraphs 11.14(c) and (d)(ii). The references should be to paragraphs 11.14(c) and 11.14 d(i) and d(v) instead.

Question 6: Leases

FRED 82 proposes to revise the lease accounting requirements in FRS 102 to reflect the on-balance sheet model from IFRS 16 *Leases*, with largely-optional simplifications aimed at ensuring the lease accounting requirements in FRS 102 remain cost-effective to apply. An entity electing not to take these proposed simplifications will follow requirements closely aligned to those of IFRS 16, which is expected to promote efficiency within groups.

Do you agree with the proposals to revise Section 20 of FRS 102 to reflect the on-balance sheet lease accounting model from IFRS 16, with simplifications? If not, why not?

Have you identified any further simplifications or additional guidance that you consider would be necessary or beneficial?

The introduction of lease accounting principles aligned with IFRS 16 *Leases* (IFRS 16) is one of the three key considerations for this comprehensive review of FRS 102. The FRC notes in paragraph

B20.4 that stakeholders generally supported incorporating the new model in FRS 102 although with simplifications. We believe there is a not insignificant body of opposition to the proposal of bringing all leases on balance sheet. In our view it would have been beneficial for the FRC to provide more detail on its rationale for this significant change, rather than just pointing to alignment with IFRS 16. The introduction of the new model is expected to have significant cost implications and therefore setting out the benefits succinctly is critical to convince stakeholders of the merits of this proposal. We note that the IASB has decided to defer its decision on the introduction of IFRS 16 requirements in the IFRS for SMEs. The FRC has justified its approach on the basis that the scope of entities applying FRS 102 is significantly different. We do not believe that this argument provides sufficient justification and note that depending on the scope defined by a jurisdiction, the IFRS for SMEs may apply to larger private entities.

That said, on balance we have conclude that we support the introduction of an on-balance sheet approach for leases, although we believe such a decision is much more nuanced and balanced than reflected by the FRC in the Basis for Conclusions. However, we have concerns around the FRC's approach. The FRC appears to have used IFRS 16 as the template and then added options or other practical expedients with the intention to simplify the more complicated requirements in IFRS 16. In our view this approach has led to overly lengthy and complex requirements. The drafting is technical and will be inaccessible for many stakeholders without prior exposure to IFRS 16. We would have preferred an approach as adopted to Section 12 *Other Financial Instruments Issues* for hedge accounting, where the FRC identified key principles and requirements based on the underlying IFRS standard, but rather than copying the IFRS requirements, drafts its own tailored requirements using terminology that is more familiar and easier to understand by users of FRS 102. In terms of level of detail and complexity, we believe something akin to the current finance lease requirements applicable to lessees would be more suitable.

We are content that such an approach would introduce differences with IFRS 16 and would not address all possible lease accounting issues. We do not believe that maximum alignment with IFRS 16 should override proportionality of the requirements. In that regard we also do not consider that the argument of efficiency within IFRS groups carries much weight. Most group entities that wish to align with recognition and measurement of IFRS have the option to use FRS 101 *Reduced Disclosure Framework* (FRS 101). This standard provides the flexibility to apply the same IFRS recognition and measurement requirements in a group. Introducing IFRS 16-like requirements for the sake of efficiency in a group carries the risk of 'cherry picking' between recognition and measurement requirements of FRS 102 and IFRS, to the detriment of understandability and comparability of financial statements. In the same vein we do not support an option in FRS 102 to apply IFRS 16 instead of separate leasing requirements in FRS 102. We believe that such a piece-meal approach would reduce the understandability of financial statements and impair the integrity of FRS 102 as a stand-alone standard. As an alternative, for stand-alone entities wishing to apply IFRS based recognition and measurement requirements, but not all disclosure requirements, the FRC could explore whether such an option could be accommodated within FRS 101 by expanding the scope to stand-alone entities.

We welcome the exemptions in relation to short-term leases and low value assets. In respect of the latter, we appreciate the additional clarifications included in FRS 102. In addition, it would be helpful to clarify the accounting for bulk leases of identical or very similar low value assets, e.g. laptops or personal computers, i.e. a clarification whether the exemption applies when an entity leases many similar low value assets. It is not clear from the requirements as drafted.

We support the simplifications made in relation to the interest rate implicit in the lease. As a further simplification the FRC could consider removing the requirement to discount lease liabilities in situations when doing so would be immaterial, which may be the case for certain shorter-term leases.

Identification of components and combination of lease contracts are areas where the FRC could reduce the length of the requirements. Lease modifications and the reassessment of the lease liability requirements could be simplified by focusing on common transactions such as rent reviews.

The FRC could consider whether it is necessary to revise the drafting for lessor accounting so significantly if there are no intended changes to existing accounting practice. It includes for example

new and more complex requirements for variable lease payments and modifications, but there are no explanation as to why this is necessary.

We note the FRC has retained the existing accounting requirements for sale and leaseback transactions as an option. We suggest the FRC considers whether this option should be made mandatory. There is some opposition to the IFRS 16 requirements, which we assume is the reason for the FRC proposing to retain existing accounting requirements as an option. In the interest of reducing complexity, we believe the IFRS 16 requirements can be removed. In addition, the FRC should consider whether all the proposed requirements pertaining to the determination of the fair value of the consideration in a sale and lease back are needed.

We concur with the FRC's decision that IFRS 16 equivalent requirements are not incorporated into FRS 105. The complexity and current drafting are unsuitable for this standard. We also note that if the FRC were to require micro-entities to bring leases on balance sheet, this could have a knock-on effect for some entities if as a consequence they are no longer eligible for the micro-entities regime. Such secondary effects would need to be considered as part of an impact assessment.

Question 7: Revenue

FRED 82 proposes to revise the revenue recognition requirements in FRS 102 and FRS 105 to reflect the revenue recognition model from IFRS 15 *Revenue from Contracts with Customers*. The revised requirements are based on the five-step model for revenue recognition in IFRS 15, with simplifications aimed at ensuring the requirements for revenue in FRS 102 and FRS 105 remain cost-effective to apply. Consequential amendments are also proposed to FRS 103 and its accompanying Implementation Guidance for alignment with the principles of the proposed revised Section 23 of FRS 102.

Do you agree with the proposals to revise Section 23 of FRS 102 and Section 18 of FRS 105 to reflect the revenue recognition model from IFRS 15, with simplifications? If not, why not?

Have you identified any further simplifications or additional guidance that you consider would be necessary or beneficial?

We concur that the five-step model for revenue recognition based on IFRS 15 *Revenue from Contracts with Customers* (IFRS 15) is a suitable approach for revenue recognition under FRS 102. Although we do not believe that the existing revenue recognition requirements of FRS 102 are broken, we believe that the IFRS 15 approach could provide a sound and more robust basis for revenue recognition in different sectors. That said, we also understand concerns about costs and benefits. Entities will have to conduct their assessment on adoption of the new requirements; however, such an assessment may not change their revenue recognition policies, which is the most likely outcome in the majority of cases. Still, these costs could be significant and consequently the introduction of the new requirements would be considered an unnecessary and expensive burden by these entities. The FRC has not reflected upon these consequences in the Impact Assessment or Basis for Conclusions.

Although we agree with the IFRS 15 based five-step revenue recognition model, we have concerns about the volume and complexity of the requirements as drafted. Similarly, to the new leasing requirements, they appear to have been mostly lifted from IFRS 15. We understand that making simplifications can be difficult when the FRC is also trying to achieve consistency with IFRS requirements. Slightly different words or modified definitions, for example using 'promise' instead of 'performance obligation', can be deemed to introduce differences or may be interpreted differently by stakeholders who had prior exposure to IFRS 15 compared to those that have not dealt with IFRS 15 previously.

In our view it would be preferable to adapt IFRS 15 requirements even if this introduces differences with IFRS 15 and the IFRS for SMEs. Consistency with IFRS 15 to achieve efficiency in a group is not a priority for us when developing new requirements for FRS 102. The FRC has already developed solutions for entities that seek those efficiencies in FRS 101 (as we have already noted in Question 6). We also reemphasise that we do not support an option to apply IFRS 15 instead of the

requirements in FRS 102 for revenue recognition as this undermines the integrity of the standard and is to the detriment of users. In our view a mix and match of UK GAAP and IFRS requirements, although it offers preparers more flexibility, is confusing for users and will reduce understandability and comparability of financial statements. Entities wishing to take the IFRS 15 option would usually be able to do so by adopting IFRS.

We therefore recommend that the FRC shortens the length of requirements and eases the complexity by:

- Focusing on key issues relevant for FRS 102 users;
- Reducing the detailed requirements incorporated from IFRS 15;
- Removing multiple options designed to achieve consistency with IFRS 15; and
- Simplifying the drafting by avoiding IFRS technical jargon where possible.

In regard of proposed differences with IFRS 15 introduced by the FRC, we believe the proposal to reduce the period for which the time value of money does not need to be considered from 12 to 6 months would not appear to be a simplification and therefore such a change is difficult to support without explanations from the FRC as to why such a difference is justified.

The FRC is proposing to introduce the five-step model and a number of supporting requirements of IFRS 15 in FRS 105. We concur with the FRC that consistency between the principles applied in FRS 102 and FRS 105 is an important factor in the decision on whether to adopt the model in FRS 105. In our view applying consistent revenue recognition requirements makes the eligibility assessment for micro-entities (revenue criterion) more effective as otherwise different revenue might be reported by entities depending on whether they are above and below the threshold. It is also helpful for entities when they eventually become ineligible for using FRS 105, as they would already apply revenue recognition requirements largely consistent with those in FRS 102. On the other hand, for this subset of entities the requirements as currently drafted are too complex and the drafting too technical. This should be revised before proceeding with the proposals. It would also seem important that these entities are supported with illustrative examples of common revenue transactions.

As to the costs for micro-entities, we would expect that the contracts of micro-entities are simpler and fewer and therefore adoption would be less onerous for these entities. Adopting the requirements prospectively should also ease the implementation efforts. On the other hand, if these entities enter into simpler contracts it is much less likely that there will be changes required to existing revenue recognition policies in which case the benefit of introducing new requirements is hard to justify. It is not possible for us to decisively answer the question of whether on balance the benefits would outweigh the costs for micro-entities, but the quantified costs per entity based on one hour for each micro-entity as estimated by the FRC would appear too low, even if applied as an average (paragraph 102 of the Impact Assessment). We also note the FRC justifies the introduction of new revenue recognition requirements on the basis that micro-entities will need to file a profit and loss account with Companies House under the planned Companies House reforms. In our view this is not a convincing reason for introducing new revenue recognition requirements.

Question 8: Effective date and transitional provisions

The proposed effective date for the amendments set out in FRED 82 is accounting periods beginning on or after 1 January 2025, with early application permitted provided all amendments are applied at the same time. Do you agree with this proposal? If not, why not?

FRED 82 proposes transitional provisions (see paragraphs 1.35 to 1.60 of FRS 102 and paragraph 1.11 of FRS 105).

In respect of leases, FRED 82 proposes to permit an entity to use, as its opening balances, carrying amounts previously determined in accordance with IFRS 16. This is expected to provide a simplification for entities that have previously reported amounts in accordance with IFRS 16 for

consolidation purposes, promoting efficiency within groups. Do you agree with this proposal? If not, why not?

Otherwise, FRED 82 proposes to require the calculation of lease liabilities and right-of-use assets on a modified retrospective basis at the date of initial application. Do you agree with this proposal? If not, why not?

In respect of revenue, FRED 82 proposes to permit an entity to apply the revised Section 23 of FRS 102 on a modified retrospective basis with the cumulative effect of initially applying the revised section recognised in the year of initial application. This is expected to ease the burden of applying the new revenue recognition requirements retrospectively by removing the need to restate comparative period information. Unlike IASB/ED/2022/1, to ensure comparability between current and future reporting periods, FRED 82 does not propose to permit the revised Section 23 of FRS 102 to be applied on a prospective basis. However, FRED 82 proposes to require micro-entities to apply the revised Section 18 of FRS 105 on a prospective basis. Do you agree with these proposals? If not, why not?

Do you have any other comments on the transitional provisions proposed in FRED 82?

Have you identified any additional transitional provisions that you consider would be necessary or beneficial? Please provide details and the reasons why.

The FRC intends to finalise the proposals without undue delay and we understand that the proposed effective date is based on the premise that the FRC would finalise the proposed amendments no later than by the end of 2023 to give entities sufficient time to implement the changes.

In our view it is important for the FRC to reflect upon the proportionality of the proposed requirements and adapt the drafting so it is more suitable for users of FRS 102 and FRS 105. This could involve re-exposure of the proposals and if so, the proposed effective date would need to be moved. In our view it is important for the FRC to take the necessary time for the drafting process to avoid implementation issues and unintended consequences once the standard is finalised.

If the FRC was to decide to finalise the proposed amendments largely unchanged by the end of 2023, entities would have effectively two years to prepare for implementation. Given that there are two significant accounting areas of changes that will be effective at the same time, it will require a not insignificant effort from entities to implement them. It is difficult to predict whether two years would be sufficient, but we are certain that it will be challenging for certain entities, their advisors and auditors. In our view extending the effective date would be acceptable, as we do not believe implementation of these changes is a matter of urgency. A longer implementation period could ease the pressure on resources and allow organisations, including the FRC, to produce better implementation guidance.

The FRC should also consider the effective date of changes relating to expected credit losses carefully, should the FRC proceed with making such changes. Entities' resources will have been stretched by implementing the changes to leasing and revenue accounting and they may need some time before they can embark on another significant implementation project.

We concur with the proposals that restatement of comparative periods is not required for the leasing and revenue recognition requirements. This should ease pressure on implementation.

In proposed paragraph 1.54 the FRC asks entities to recognise the cumulative effect of applying Section 23 in the opening balance of each affected component of equity. It is not clear here what the FRC has in mind. This requirement is different from proposed paragraph 1.40 where it is specified that the adjustment for leases should be recorded in retained earnings. It would be helpful for the FRC to clarity the difference between the two requirements or align them, if no difference is intended.

Question 9: Other comments
Do you have any other comments on the proposed amendments set out in FRED 82?

1) Going concern

The FRC is proposing to mandate an explicit disclosure that the financial statements are prepared on a going concern basis under proposed paragraph 3.8A. We note that this is a disclosure requirement beyond those in IFRS. As a rationale for the departure from the principle to follow a global solution, the FRC has only cited that a small number of stakeholders asked the FRC to emphasise when going concern disclosures would be necessary (paragraph B3.1).

Although it is a departure from IFRS, in our view most entities will include a statement that the financial statements are prepared on a going concern basis already and we do not consider that this part of the new disclosure requirement will be onerous for entities.

The FRC is also asking entities to confirm that management has considered all available information about the future, which is at least, but not limited to, 12 months from the date when the financial statements are authorised for issue. We agree that entities should specify the period over which management provides its going concern assessment, as there is flexibility under paragraph 3.8. Beyond that, the usefulness of this confirmation is not clear. If the FRC is seeking to enhance the diligence or processes applied by entities in relation to their going concern assessment, then the FRC should make that clear. Guidance should be provided on the FRC's expectations which would go beyond the scope of FRS 102 and should be published outside the standard.

The FRC is also mandating that entities disclose significant judgements in relation to going concern. It would be helpful, if the FRC could provide examples of instances when such disclosures should be made. For example, the 2014 IFRIC agenda decision on this topic refers to significant judgements when the entity determines that there is no material uncertainty regarding going concern, but it is not clear whether the FRC seeks disclosure in the same and/or other situations.

2) Footnote 49 in Section 11 *Basic Financial Instruments* and footnote 54 in Section 12

The FRC is proposing some limited amendments to these footnotes, but in our view there is room for further clarification. We note that IAS 39 has not been fully superseded by IFRS 9 as suggested in the footnote. IAS 39 as issued by the IASB is still in existence and contains hedge accounting requirements. The drafting of the footnote should be revised to avoid confusion The footnote also makes reference to a copy of the applicable version of IAS 39 being available on the FRC website. It would be helpful for this version of IAS 39 which includes the EU-carve-out to be posted on the FRC's website as stated.

3) Paragraph 11.9

The FRC is proposing to update references from LIBOR to SONIA. Given LIBOR has largely been replaced as a benchmark we agree with this drafting change. It is not clear why the references in example 6 on page 131 and in the examples in the Appendix to Section 12 have not been updated for the discontinuation of LIBOR as a benchmark rate. We also note that the definition of variable rate in footnote 50 should make reference to a single observable benchmark rate for clarification that such benchmarks are variable rates.

4) Section 24 *Government Grants*

We welcome the FRC's clarification in the Basis for Conclusion regarding the UK's RDEC schemes. This is a practical issue and in our view the FRC's guidance supports the existing interpretation of the scope of this section in relation to the schemes.

We have concerns about the amendments proposed to paragraph 24.5A. We believe, perhaps inadvertently, these amendments would change existing accounting practice and be inconsistent with the matching concept in situations when the grant has not yet been recognised as income. We would request the FRC to review the proposed requirements and reconsider whether they are appropriate or need expanding.

5) Section 26 *Share-based payments*

We note the additional requirements proposed in this Section. We do not object as these are consistent with IFRS 2 *Share-based Payments* (IFRS 2), however, the FRC should be cognisant of the length of this section and whether it needs to address all these additional issues or whether entities could develop their own accounting policies. Another very common practice issue for example arises in group situations. FRS 102 is silent on the accounting by a subsidiary when it uses shares of the parent as compensation. We believe there is sufficient guidance in IFRS 2 to allow entities to develop their accounting policies in this area, without the need for FRS 102 to repeat those.

6) Section 28 *Employee Benefits*

We note the amendments made in this section regarding defined benefit plans. However, the FRC has not included its rationale for making these changes. If the FRC retains these amendments the basis for making them and their effect should be explained.

7) Section 34 *Specialised Activities*

The FRC is proposing a number of changes to the requirements for agricultural activities. We believe the rationale for these changes should be explained in the Basis for Conclusion, including why these changes are necessary and whether they are intended to provide clarifications or present a change to existing accounting practice.

The proposed amendment to paragraph 34.28 would require financial institutions to include lease liabilities on an undiscounted basis in the maturity analysis of financial liabilities. We note lease liabilities would not normally fall into the scope of financial liabilities and the requirement goes beyond the equivalent requirements in IFRS 7 *Financial Instruments: Disclosures*. In our view the benefits of this disclosure for financial institutions are not clear and if the FRC believes that it is needed it should be included in Section 20 as a disclosure requirement applicable to all entities.

8) FRS 103

We welcome the FRC looking to align revenue recognition for insurance contracts better with the principles in FRS 102. In our view there is, however, more assessment required before any amendments to FRS 103 and the Implementation Guidance can be finalised by the FRC.

Based on the proposed changes to the Implementation Guidance it would appear that the FRC has taken a targeted approach to align FRS 103 with FRS 102 where there appear to be overlapping requirements. We are concerned that the current approach could have unintended consequences and would ask the FRC to consider a more comprehensive project on premium recognition for insurance contracts, so to avoid unintended consequences.

We have the following observations in relation to some of the proposed amendments:

- It is not clear to us why the FRC is seeking to restrict the recognition of pipeline premiums to those that have been reported to the undertaking by the date the financial statements are authorised for issue (paragraph IG2.4). Similar requirements are not proposed for FRS 102, it is not clear what the basis for this new requirement is and we have questions over whether it is consistent with the recognition principles in FRS 102. We would recommend that the FRC does not proceed with this amendment without further consideration.
- The intended effect of the amendment to paragraph IG2.5 should be clarified. Is the FRC seeking to restrict the recognition of written premiums to those where the policyholder has confirmed the renewal? We note the recognition of written premiums is not addressed in FRS 102, and it is not clear why such an amendment would be needed for consistency with FRS 102.
- The guidance in paragraph IG2.6 addresses when additional premiums or premium reductions should be deferred or recognised in income. The proposed amendments, however, would change when written premiums can be recognised. We do not concur with the amendments as drafted as they would change the requirements beyond what is covered by FRS 102.

Question 10: Consultation stage impact assessment

Do you have any comments on the consultation stage impact assessment, including those relating to assumptions, sources of relevant data, and the costs and benefits that have been identified and assessed? Please provide evidence to support your views.

In particular, feedback is invited on the assumptions used for quantifying costs under each of the proposed options (Section 3 of the consultation stage impact assessment); any evidence which might help the FRC quantify the benefits identified or any benefit which might arise from the options proposed which the FRC has not identified (Section 4 of the consultation stage impact assessment); and appropriate data sources to use to refine the assumption of the prevalence of leases by entity size (Table 23 of the consultation stage impact assessment).

We have shared some of our observations on specific matters in the responses above.