

THE FRC'S TRIENNIAL REVIEW

(Lecture A613/ A614 – 32.08/ 19.01)

On 14 December 2017, the Financial Reporting Council (FRC) issued the final amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* Triennial Review 2017 Incremental improvements and clarifications.

With the exception of the amendments to FRS 105 in respect of disclosures, all the other amendments must be mandatorily applied for accounting periods starting on or after 1 January 2019. Early adoption is permissible, provided that all the amendments are also early adopted. The only two amendments that can be early adopted separately are the directors' loans concession (see 1.4 below) and the gift aid accounting clarification (see 1.10 below).

The disclosure requirements of FRS 105 (see 1.16 below) must be applied for accounting periods starting on or after 1 January 2017. They are legally required disclosures that should have been applied for periods starting on or after 1 January 2016, but as 2016 year-ends have now been and gone, the FRC have introduced the effective from date for periods starting on or after 1 January 2017.

The amendments are not to be viewed as 'wholesale' changes but, as the title suggests, are incremental improvements to the standard which should prove beneficial to reporting entities. The FRC have also included clarifications in certain areas, such as the inclusion of a description of a basic financial instrument (see 1.3 below) and the accounting for gift aid (see 1.10 below). As a result, UK GAAP should be easier to work with and reflects most of the implementation feedback from users since it was first introduced for periods starting on or after 1 January 2015.

When FRS 102 was first issued in March 2013, the FRC indicated that they would review the standard every three years. This is consistent with the International Accounting Standards Board's (IASB) *IFRS for SMEs*. However, paragraph 18 of the Basis for Conclusions confirms that periodic reviews of FRS 102 are likely to take place every four to five years to allow time for experience of the most recent edition of FRS 102 to develop before seeking stakeholder feedback.

That said, it is important to emphasise that should an emerging issue prove to be of an urgent nature, the FRC may deal with it as an ad-hoc amendment to FRS 102 (or other FRS as applicable). Clearly, the FRC want as few divergent practices as possible and hence it may be necessary to deal with isolated issues through separate consultations. However, the FRC have suggested that future comprehensive reviews of UK GAAP may be carried out on a four- or five-year cycle.

Many commentators suggest that FRS 102 is aligned to IFRS or *IFRS for SMEs*. This is not strictly correct. While FRS 102 is based on the *IFRS for SMEs* issued in March 2009, the FRC has modified the *IFRS for SMEs* substantially both in terms of scope and accounting treatments provided. For example, Section 29 *Income Tax* in FRS 102 is notably different than Section 29 in *IFRS for SMEs*. In addition, the FRC have to develop accounting standards in accordance with five principles which ensure the financial reporting standards:

*FRS 102 Summary
paragraph (iii)*

- a) have consistency with international accounting standards through 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.

The IASB may introduce new standards, make amendments to existing standards or withdraw a standard. It is not strictly the case that the FRC will follow suit. In some cases, existing accounting treatments may achieve a better outcome for the UK and Republic of Ireland, or UK GAAP may already be at the stage where the IASB is seeking to be hence the FRC may choose not to follow the same course of action which the IASB has when it comes to introducing, amending or withdrawing accounting standards.

This is evidenced by the removal of the undue cost or effort exemptions in the FRC's triennial review (see 1.1 below). The FRC removed the undue cost or effort exemptions when comprehensively reviewing FRS 102, whereas when the IASB undertook their comprehensive review of *IFRS for SMEs* in 2015, they included more undue cost or effort exemptions.

The majority of the amendments to FRS 102 are editorial in nature. However, there are some amendments which have a direct impact on the financial statements themselves, which are discussed below.

1.1 **Undue cost or effort exemptions**

The FRC have taken the decision to remove the undue cost or effort exemptions in FRS 102 on the grounds that these were not being applied correctly. It became apparent to the FRC that the undue cost or effort exemptions were being applied as accounting policy options, which was never the intention.

The Glossary to FRS 102 does not define 'undue cost or effort' and hence there have been interpretational issues faced by entities leading to the confusion. Paragraph 2.14B of the *IFRS for SMEs* states that:

'Applying a requirement would involve undue cost or effort by an SME if the incremental costs (for example, valuers' fees) or additional effort (for example endeavours by employees) substantially exceed the benefits that those that are expected to use the SME's financial statements would receive from having the information.'

*IFRS for SMEs
paragraph 2.14B*

While the undue cost or effort exemptions have been removed because they were being applied as accounting policy choices, in some cases they have been replaced by accounting policy options. For example, where properties are rented out to group members (see 1.2 below).

The removal of the undue cost or effort exemptions will have an impact on some reporting entities; particularly those that have investment properties which they have not fair valued at each reporting date as they have previously exercised the undue cost or effort exemptions. Unless the property is rented out within a group, all investment property must be measured at fair value at each balance sheet date, with changes in fair value going through the profit and loss account. Also don't forget to bring deferred tax into account!

Areas of FRS 102 where undue cost or effort exemptions have been removed are:

- Section 14 *Investments in Associates* – paragraph 14.10
- Section 15 *Investments in Joint Ventures* – paragraph 15.15
- Section 16 *Investment Property* – paragraphs 16.1, 16.3, 16.4 and 16.10
- Section 17 *Property, Plant and Equipment* – paragraph 17.1(a)

It is important that practitioners carefully check that where they have previously exercised an undue cost or effort exemption, that they review the revised edition of FRS 102 when they are applying the amended version to ensure they do not continue applying an exemption that is no longer in the standard.

1.2 *Investment properties within a group*

As noted in 1.1 above, the removal of the undue cost or effort exemptions means that all investment properties, which are not occupied in a group context, will have to be measured at fair value at each balance sheet date with fair value fluctuations being taken through the profit and loss account. This is the treatment required by Section 16.

In order to address implementation issues, the FRC have introduced an accounting policy choice in situations where a group rents property out to other group members. This will prove to be extremely useful for groups because under the September 2015 edition of FRS 102, there was no scope exemption from groups measuring investment property at fair value as there was in previous SSAP 19 *Accounting for investment properties*.

Under the September 2015 edition of FRS 102, a group that owned a property which was let out to another group member, would have had to reclassify that property as investment property in its individual financial statements, replace the depreciation charge with a fair value gain or loss and bring deferred tax into account. This would all then be reversed out by way of consolidation adjustments in the group accounts as the property would be treated as property, plant and equipment (i.e. an owned property) as group accounts must reflect the economic substance of the group, which is that of a single reporting entity. Therefore, all intra-group transactions are eliminated.

Clearly, this caused quite a lot of additional work, with some groups even refusing to account for such properties in accordance with FRS 102, claiming undue cost or effort would be incurred by having to account for the property under Section 16 in the individual financial statements of the group member owning the property and then under Section 17 in the consolidated financial statements.

To address this issue, the FRC have included paragraphs 16.4A and 16.4B in FRS 102 which relate to group entities. Paragraph 16.4A states:

‘An entity that rents investment property to another group entity shall account for those properties either:

FRS 102 paragraph 16.4A

- (a) at fair value with changes in fair value recognised in **profit or loss** in accordance with this section (the Appendix to Section 2 provides guidance on determining fair value); or*
- (b) by transferring them to property, plant and equipment and applying the cost model in accordance with Section 17.*

An entity choosing to apply (b) above shall provide all the disclosures required by Section 17, other than those related to fair value measurement.’

Paragraph 16.4B states:

‘When only part of a property is rented out to another group entity and the remainder is used for other purposes (such as being rented to an external third party or owner-occupied), paragraph 16.4A only applies to the component of that property that is rented out to another group entity.’

FRS 102 paragraph 16.4B

It is likely that most investment property in a group context will be measured under paragraph 16.4A(b) as this effectively restores the position in previous SSAP 19 (i.e. measuring the property at cost, less depreciation and impairment).

It is to be emphasised that the above accounting policy option only relates to **investment property rented to another group entity**. This option does not apply to non-group investment property which must be measured at fair value through profit or loss at each balance sheet date (even for small companies). Micro-entities applying FRS 105 can only measure investment property at cost less depreciation (with the exception of the land on which the property stands) less impairment.

1.3 **Financial instruments**

It is fair to say that the wording in Section 11 *Basic Financial Instruments* is far from basic. Financial instruments are possibly the most complex area of UK GAAP and Section 11 has seen some significant amendments to it through the triennial review. Prior to the triennial review, a financial instrument had to meet the detailed conditions outlined in paragraph 11.9 if the instrument were to be classed as basic. There are examples at the foot of paragraph 11.9 to aid application of the conditions and the FRC have included additional examples as part of the triennial review to further aid an understanding.

In addition, the FRC have included a description of a basic financial instrument. Even if the financial instrument does not meet the conditions for classification as basic in paragraph 11.9, but meets the description, then it can still be classed as basic and accounted for under Section 11. This will mean that for a relatively small number of financial instruments, they can be treated as basic rather than non-basic and use the amortised cost method which will provide relevant information for the users.

The description of a basic financial instrument according to paragraph 11.9A is as follows:

'A debt instrument not meeting the conditions in paragraph 11.9 shall, nevertheless, be considered a basic financial instrument if it gives rise to cash flows on specified dates that constitute repayment of the principal advanced, together with reasonable compensation for the time value of money, credit risk and other basic lending risks and costs (eg liquidity risk, administrative costs associated with holding the instrument and lender's profit margin). Contractual terms that introduce exposure to unrelated risks or volatility (eg changes in equity prices or commodity prices) are inconsistent with this.'

FRS 102
paragraph
11.9A

Accounting policy choice to apply IAS 39 Financial Instruments

FRS 102 has been amended to retain the option in Section 11 and Section 12 *Other Financial Instruments Issues* to apply the recognition and measurement requirements of IAS 39 *Financial Instruments*. The option is available until the impairment requirements in FRS 102 (Section 27 *Impairment of Assets*) are amended to reflect IFRS 9 *Financial Instruments*, or the FRC decide not to amend FRS 102 any further in respect of IFRS 9. The IAS 39 EU-carve out option also continues to be available.

In addition, paragraph 11.42 also requires an entity to disclose information which enables the users to evaluate the significance of financial instruments on the entity's financial position and performance. Therefore, an entity which has taken the accounting policy choice to apply the recognition and measurement requirements of IAS 39 or IFRS 9 may need to consider additional disclosures based on IFRS 7 *Financial Instruments: Disclosure*.

When the IASB finalised IFRS 9, amendments were also made to IFRS 7 to reflect the new requirements in IFRS 9. Financial assets must be tested for impairment using an expected credit loss model (rather than an incurred credit loss model) and therefore the disclosure requirements of IFRS 7 were changed to reflect the recognition of expected credit losses. This means that some of the disclosures in FRS 102 are inconsistent with the application of the recognition and measurement requirements of IFRS 9 and hence a number of changes have been made to the disclosure requirements so as to ensure that when an entity applies the recognition and measurement principles of IFRS 9, they are providing relevant information concerning the impairment of financial assets.

Investments in shares

There was an anomaly in FRS 102 prior to the amendments. The September 2015 edition of FRS 102 requires investments in non-convertible preference shares and non-puttable ordinary shares or preference shares to be measured at fair value, unless fair value cannot be measured reliably. Certain preference shares which are liabilities of the issuer (and measured at amortised cost) are treated differently by the holder.

Reference to such investments in shares in FRS 102 has been amended to non-derivative instruments which are equity of the issuer. This improves the accounting for those instruments which are liabilities of the issuer as they are measured at amortised cost if the instrument is accounted for under Section 11 (i.e. it is basic).

Loans with two-way compensation clauses

The FRC issued commentary in June 2016 concerning the accounting for social housing loans; notably the classification of loans with two-way compensation clauses. Respondents did not agree that the inclusion of a description of a basic financial instrument (which has been included in paragraph 11.9A) sufficiently addressed the issue. To alleviate concerns in this respect, paragraph 11.9(c) has been amended which confirms that compensation could be paid by either the holder (the lender) or the issuer (the borrower).

Macro hedging

Fair value hedge accounting for a portfolio of financial instruments was not included in FRS 102 and therefore entities wishing to apply macro hedging applied the provisions in paragraph 11.2 (and 12.2) and used the recognition and measurement provisions in IAS 39/IFRS 9.

FRS 102 has been amended to cross-refer to the IAS 39 requirements for macro hedging.

1.4 *Directors' loans*

Prior to the finalisation of the amendments to FRS 102 from the triennial review, on 8 May 2017 the FRC took an unprecedented step and announced a change to UK GAAP which was to come in with immediate effect for small companies that had received a loan from a director-shareholder, or a close family member of the director-shareholder.

The way that an off-rate market loan is accounted for under FRS 102 has not been without controversy. Many practitioners have expressed their disapproval of having to discount off-rate loans using a market rate of interest. There are 'workarounds' where discounting is concerned; for example, if there are no terms in place, FRS 102 would regard the loan as being repayable on demand and hence will be measured as a current asset or current liability at the undiscounted amount of cash payable. In practice, most off-rate loans are unstructured (e.g. directors' loans and intra-group loans) and therefore discounting may be avoidable.

The FRC recognised that using the amortised cost method (and effective interest rate method) in Section 11 for loans which are provided by a director-shareholder, or close family member of that director-shareholder does prove arduous, with costs outweighing benefits. The FRC's Press Release on 8 May 2017 confirmed that loans to a small company from a director-shareholder or close family member of that director-shareholder can be measured at transaction price rather than at present value. The FRC took this unprecedented step on the grounds that they were not expecting any pushback from commentators disapproving of the need *not* to discount the loan!

The triennial review extends this concession slightly to small groups of the director's family. Paragraph 11.13A states:

'As an exception to paragraph 11.13, the following financing transactions may be measured initially at transaction price:

FRS 102 paragraph 11.13A

- (a) *a basic financial liability of a **small entity** that is a loan from a person who is within a director's group of close family members* ^[*footnote 1], *when that group contains at least one shareholder* ^[*footnote 2] *in the entity; and*
- (b) *a public benefit entity concessionary loan (see paragraph PBE11.1A).* ^[*footnote 1] In this context, a director's group of close family members shall be the director and the close members of the family of that director (see glossary definition of **close members of the family of a person**). This includes a person who is the sole director-shareholder of an entity. ^[*footnote 2] For small LLPs this shall be read as a member who is a person.'

The definition of 'close members of the family of a person' per the Glossary to FRS 102 is as follows:

'Those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity including:

FRS 102 Glossary **close members of the family of a person**

- (a) *that person's children and spouse or domestic partner;*
- (b) *children of that person's spouse or domestic partner; and*
- (c) *dependants of that person or that person's spouse or domestic partner.'*

Therefore, loans to small entities from a director who is not a shareholder, and has no close family members that are shareholders, will not qualify for the exemption. Loans to small entities from a directors' group of close family members (including the director) will qualify when that group also includes a shareholder in the small entity.

The relief is also available to small LLPs.

It is important to emphasise that the relief does not apply to loans to a director from a company, nor does it apply to intra-group loans. If there are no workarounds to discounting the loan (e.g. if the loan is unstructured or if it is not a 53-week loan), the loan must be discounted to present value using a market rate of interest.

The concession is available for small companies from December 2016 year-ends onwards. The FRC brought forward the relief for small companies to allow those small companies with a December 2016 year-end the opportunity of taking advantage of it. Had they not brought it forward, a small company with a December 2016 year-end would have had to discount such loans, only to then reverse the effects of discounting in the December 2017 year-end; but a small company with a March 2017 year-end would have been able to take the option if they used the full nine-months' filing grace from Companies House. This was due to the timing of the finalisation of the amendments to FRS 102 (December 2017).

It should be noted that where a director-shareholder, or close family member of that director-shareholder, provides a loan to the small entity at below market rates of interest or at zero rates of interest, the loan will be caught by the related party disclosure requirements in paragraph 1AC.35 of Section 1A *Small Entities*; hence the loan must be disclosed as a related party transaction as it has not been concluded under normal market conditions.

1.5 *Intangible assets*

The definition of an intangible asset in FRS 102 is different than under previous UK GAAP and gave rise to the need to recognise additional intangible assets that were acquired in a business combination (i.e. where a parent acquires a subsidiary). This has increased costs of compliance in some instances, which the FRC have recognised goes against the principles of standard-setting.

The FRC decided to amend Section 18 *Intangible Assets other than Goodwill* so as to provide entities with an accounting policy choice of either separately recognising intangible assets acquired in a business combination or including them within goodwill. If the entity chooses to separately recognise intangible assets, they must apply this policy to all intangible assets in the same class and on a consistent basis.

Paragraph 18.8 of FRS 102 has been heavily amended and the amended paragraph 18.8 states:

*'Intangible assets acquired in a **business combination** shall be recognised separately from goodwill when all the following three conditions are satisfied:*

FRS 102 paragraph 18.8

- (a) the recognition criteria set out in paragraph 18.4 are met;*
- (b) the intangible asset arises from contractual or other legal rights; and*
- (c) the intangible asset is separable (ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged either individually or together with a related contract, asset or liability).*

An entity may additionally choose to recognise intangible assets separately from goodwill for which condition (a) and only one of (b) or (c) above is met. When an entity chooses to recognise such additional intangible assets, this policy shall be applied to all intangible assets in the same class (ie having a similar nature, function or use in the business), and must be applied consistently to all business combinations. Licences are an example of a category of intangible asset that may be treated as a separate class, however, further subdivision may be appropriate, for example, where different types of licences have different functions within the business.'

1.6 *Financial institutions*

The definition of a financial institution in the Glossary to FRS 102 has been amended to remove references to '... generate wealth or manage risk through financial instruments.' The removal of this phrase means there should be less uncertainty about how the definition should be applied and hence fewer entities will fall under the definition of a financial institution.

The Glossary provides a list of institutions that fall under the definition of a financial institution. The FRC have also removed 'retirement benefit plans' from the list, which will be a welcome change as they are not similar to the rest of the entities within the Glossary's definition. In addition, retirement benefit plans are also subject to their own disclosure requirements in Section 34 *Specialised Activities*.

1.7 Key management personnel compensation

The requirement to disclose key management personnel compensation in total is in paragraph 33.7 of FRS 102. Paragraph 33.7A has been inserted by the FRC which states that when an entity is required to disclose directors' remuneration (or equivalent) under law or regulation, it is exempt from the requirement of paragraph 33.7 provided that key management personnel and the directors are the same.

Care needs to be taken where this is concerned, because the definition of 'key management personnel' is quite broad and includes all individuals who have authority and responsibility for planning, directing and controlling the entity, whether directly or indirectly. The definition includes directors (whether executive or otherwise) and so it may not necessarily be the case that key management personnel and the directors are the same body of individuals; although in a smaller entity, this could well be the case.

1.8 Net debt reconciliation

For those entities which are required to prepare a cash flow statement, the net debt reconciliation is brought back into FRS 102. This has been done on the grounds that the FRC consider the reconciliation provides useful information to users. As preparers will already be familiar with the net debt reconciliation, the costs of compliance will be negligible and software providers will usually include this reconciliation within their accounts production software systems in any event.

1.9 Small entities

Section 1A *Small Entities* in FRS 102 has been extensively amended as part of the triennial review due to small entities in the Republic of Ireland being brought within the scope of Section 1A due to the enactment of the Companies (Accounting) Act 2017. The small companies' regime for entities in the Republic of Ireland is available for periods starting on or after 1 January 2017. However, entities in the Republic of Ireland can early adopt the requirements as far back as periods beginning on or after 1 January 2015 provided that the financial statements have not yet been approved.

Section 1A sets out the presentation and disclosure requirements which a small company is required to follow in the preparation of their financial statements. Recognition and measurement is still based on full FRS 102.

The disclosure requirements for small entities in the UK are set out in Appendix C of Section 1A *Disclosure requirements for small entities in the UK* (as was the case in the September 2015 edition of FRS 102). The disclosure requirements which a small entity in the Republic of Ireland is legally required to make are contained in Appendix D *Disclosure requirements for small entities in the Republic of Ireland*. The five encouraged disclosures that were contained in Appendix D in the September 2015 edition of FRS 102 have been moved into Appendix E *Additional disclosures encouraged for small entities*.

An additional paragraph has been inserted into Appendix E encouraging small entities in the Republic of Ireland to provide the disclosures in paragraphs 1AE.1(b), (c) and (e). These relate to the fact that an entity is a public benefit entity (if applicable), going concern disclosures and transitional disclosures on first-time adoption of FRS 102.

1.10 Gift aid

The FRC issued a separate FRED (FRED 68 *Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland* Payments by subsidiaries to their charitable parents that qualify for gift aid).

While FRED 68 was separately issued, it was part of the triennial review.

There have been divergent practices emerging where gift aid payments are concerned which were brought to the FRC's attention. For accounting purposes, gift aid payments are a distribution, but for tax purposes they are a donation. A legal opinion obtained by the ICAEW confirmed that gift aid payments are a distribution and hence should be treated in much the same way as a dividend. There is an ICAEW technical release (TECH 16/14BL REVISED *Guidance on donations by a company to its parent charity*).

The problem that gift aid payments presented was whether they should be accrued at the balance sheet date where no Deed of Covenant was in place. Where a Deed of Covenant was in place, the treatment was less complex because the Deed of Covenant satisfies the recognition of a gift aid payment as a liability where payment is made by the subsidiary to the charitable parent after the year-end.

Paragraph 85 of the Basis for Conclusions of FRS 102 confirms that gift aid payments are to be recognised as a distribution to owners as they are similar to dividends (i.e. they are recognised within equity). Paragraph 85 also cross-refers to paragraph 32.8 of FRS 102 which specifically deals with dividends and states that where an entity declares a dividend **after** the balance sheet date, that dividend is not to be recognised as a liability. The same principles must be applied to gift aid payments and an expected gift aid payment must not be accrued unless a legal obligation to make the payment exists at the balance sheet date. Paragraph 85 of the Basis for Conclusions confirms that a board decision to make a gift aid payment to a charitable parent, which has been taken prior to the reporting date, is not sufficient to create a legal obligation.

More than half of the respondents to FRED 68 stated that, in their opinion, a liability should be recognised for an expected gift aid payment if, for example, there is a past practice of making such payments. The FRC concluded that this is inconsistent with the requirements of FRS 102 (i.e. paragraph 32.8 and dividends) and they did not agree that this reflects the substance of the transaction which is that of a distribution to owners and hence no amendment was made to FRS 102 in this respect.

As noted above, gift aid payments are distributions for accounting purposes and donations for tax purposes. When a subsidiary does not have a legal obligation to make a distribution of its profits to its owners at the balance sheet date, it will have taxable profits and hence will need to recognise a tax expense. This is because paragraph 29.14 of FRS 102 prohibits the tax effects of dividends being recognised before the dividend itself has been recognised.

The amendments to FRS 102 state that when it is **probable** (i.e. more likely than not) that a gift aid payment will be made within nine months of the reporting date to the same charitable group, or charitable venturer, and the payment will qualify to be set against profits for corporation tax purposes, the gift aid payment can be accrued.

The gift aid payment is recognised as a distribution to owners and the tax effects are recognised in profit and loss.

1.11 Fair value guidance

The fair value guidance which was included in paragraphs 11.27 to 11.32 of FRS 102 has now been moved into the new Appendix in Section 2 *Concepts and Pervasive Principles*. This was done on the grounds that the FRC acknowledged that the fair value guidance is applied generally, rather than confined to financial instruments and illustrate a measurement basis described in Section 2. Hence, it was sensible to remove the guidance from Section 11 *Basic Financial Instruments* and include it within Section 2.

1.12 Analysis of expenses

Paragraph 5.11 of FRS 102 required an entity to present an analysis of expenses using a classification based on either the nature or function of the expenses within the entity. This paragraph has been removed as it effectively duplicated the requirements in paragraph 5.5 as the profit and loss account formats in the Regulations include requirements for the classification of expenditure.

1.13 Debt for equity swaps

Paragraph 22.8A has been inserted to address concerns by stakeholders that FRS 102 was silent on the accounting for debt for equity swaps because, in some cases, such transactions can be significant. Paragraph 22.8A states that no gain or loss is recognised in profit or loss as a result of a debt for equity swap if:

- the creditor is also a direct or indirect shareholder and is acting in its capacity as a direct or indirect existing shareholder;
- the creditor and the entity are controlled by the same party/parties both before and after the transaction and the substance of the transaction includes an equity distribution by, or contribution to, the entity; or
- the extinguishment is in accordance with the original terms of the financial liability.

1.14 Business combinations

When a parent entity acquires a subsidiary, it is required to use the purchase method to account for the acquisition. The purchase method uses fair values to account for the assets acquired, liabilities and contingent liabilities assumed.

The purchase method outlined in paragraph 19.7 of FRS 102 has been amended to include more steps as a means of clarifying exactly what must happen for the purchase method to be applied correctly. In practice, the amendments are not expected to have any significant effects, but the amendments also mean that paragraph 19.7 is now consistent with the steps in IFRS 3 *Business Combinations*.

The definition of a group reconstruction has also been amended to incorporate, in certain circumstances, the transfer of a business in addition to the transfer of equity holdings.

1.15 *Comparatives for disclosures only required by a SORP*

The FRC have confirmed that when a disclosure is not required by FRS 102, but is required by a SORP, comparatives should be provided.

1.16 *Effects on other standards in the suite of UK GAAP*

All other FRSs in UK GAAP have seen some amendments arising as a result of the triennial review. Some of the more notable amendments are discussed below:

FRS 100 Application of Financial Reporting Requirements

The abbreviations and definitions that were contained in paragraph 3 have been deleted.

In addition, paragraph 10A has been inserted into FRS 100 which confirms that the amendments arising from the triennial review are to be applied for accounting periods starting on or after 1 January 2019. Early adoption is permissible provided that all the amendments are early adopted at the same time.

FRS 101 Reduced Disclosure Framework

FRS 101 reflects the changes made to the definition of a financial institution. In addition, Appendix II: *Note on legal requirements* has been amended at paragraph A2.10A to make it clear that a qualifying entity which has a disposal group may need to make additional disclosures either on the face of the balance sheet or within the notes to the financial statements.

Where the items are material, paragraph A2.10A requires this to be done on the face of the balance sheet.

FRS 103 Insurance Contracts and FRS 104 Interim Financial Reporting

There are few changes made to FRS 103 and FRS 104. The changes made mainly relate to the wording of those standards and confirmation of the effective date of the amendments.

FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime

It was expected that FRS 105 would see significant amendments as it is based on the provisions in FRS 102. The most notable change in FRS 105 is the inclusion of micro-entities in the Republic of Ireland which have been brought within the scope of the micro-entities' regime by virtue of the Companies (Accounting) Act 2017.

Micro-entities in the Republic of Ireland (RoI) are now able to apply FRS 105 for periods starting on or after 1 January 2017. Early adoption of FRS 105 is permissible provided the Companies (Accounting) Act 2017 is applied from the same date.

For UK micro-entities, there are two additional disclosure requirements which must be made at the foot of the balance sheet as follows:

- a) information about off-balance sheet arrangements as required by section 410A of the Act; and
- b) information about employee numbers as required by section 411 of the Act.

These disclosures apply for periods starting on or after 1 January 2017. They are a legal requirement and hence should have been included in financial statements for periods starting on or after 1 January 2016, but were omitted in the July 2015 edition of FRS 105.

Disclosures in respect of off-balance sheet arrangements and employee numbers were included as a result of amendments by *The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015* SI 2015/980. SI 2015/980 made amendments to sections 410A and 411 by removing the phrase '*In the case of a company that is not subject to the small companies regime*'. This meant that all companies must disclose off-balance sheet arrangements and employee numbers.

In addition, the disclosure information required by s396(A1) is required which requires the micro-entity's accounts to state:

- the part of the UK in which the company is registered;
- the company's registered number;
- whether the company is a public or a private entity and whether it is limited by shares or by guarantee;
- the address of the company's registered office; and
- where appropriate, the fact that the company is being wound up.

1.17 Areas not actioned from FRED 67

There were some proposals for change announced in FRED 67 which have not, in fact, been actioned as part of the triennial review. These are as follows:

Consolidated financial statements

FRED 67 proposed amendments to FRS 102 to update it for the control model in IFRS 10 *Consolidated Financial Statements*. The FRC felt that updating FRS 102 to reflect the control model in IFRS 10 would result in better financial reporting as it addresses concerns about the boundary of the reporting entity.

In practice, for many entities, there would be no effect on the financial statements as they would be required by law to prepare group accounts. In addition, feedback suggested that the cost of implementation of the control model in IFRS 10 would outweigh the benefits due to there being no actual effect for groups; the revised control model would merely have to go through an exercise to confirm there had been no change in the group structure.

FRS 102 has not been amended to reflect the control model in IFRS 10, but an additional disclosure regarding unconsolidated structured entities (e.g. special purpose entities) has been introduced which has been derived from IFRS 12 *Disclosure of Interests in Other Entities*.

Leases

The Consultation Document proposed to enhance the disclosure requirements in respect of leases in advance of any revised requirements based on the new IFRS 16 *Leases*. This was met with disapproval from respondents who suggested that it would be difficult for entities to provide more information concerning obligations arising from operating leases without first determining a detailed approach as to how FRS 102 will be updated for the effects of IFRS 16.

The FRC decided not to update FRS 102 in respect of lease disclosures.

Option to purchase own shares

The FRC proposed to insert a new example in Section 22 *Liabilities and Equity* which related to a written option to purchase own equity instruments. Respondents raised concerns to the FRC that there may be unintended consequences and hence the example has not been included in Section 22. However, the FRC may review this issue again in the future.

Revenue

FRED 67 proposed to amend Section 23 *Revenue* so as to provide greater clarity to the requirements for recognition of revenue from separately identifiable goods and services provided under a single transaction. This amendment was primarily proposed due so that Section 23 was slightly more aligned to that of IFRS 15 *Revenue from Contracts with Customers* which contains a five-step model for revenue recognition.

Concerns were raised that Section 23 was not causing any notable difficulties for preparers and that including principles from IFRS 15, when there was no implementation feedback, was too soon. Therefore, FRS 102 was not amended in this respect.

Share-based payment

The Consultation Document requested feedback as to the cost-effectiveness of applying Section 26 *Share-based Payment* by private companies.

The FRC confirmed that responses were mixed. Some respondents suggested that as the requirements had been in place for 10 years, they were well-established. Others noted that small private entities have difficulty in obtaining reliable and meaningful fair values for share-based payment arrangements. Other suggested that a disclosure-only approach could be considered if the legislation were to be changed in the future (currently it is not possible to include additional legislation in company law under the EU Accounting Directive).

No wholesale changes have been made to Section 26 of FRS 102, although minor improvements to the wording have been made to align it more to IFRS 2 *Share-based Payment*. The FRC may revisit this area in the future if the legislation is changed such that additional disclosures could be mandated for small entities.

Major changes to IFRS

In 2017, the FRC stated that they may issue a further exposure draft announcing changes to UK GAAP to reflect major changes in IFRS, notably:

- IFRS 9 *Financial Instruments*;
- IFRS 15 *Revenue from Contracts with Customers*; and
- IFRS 16 *Leases*.

Further changes reflecting these IFRSs were potentially going to be effective for accounting periods starting on or after 1 January 2022.

Following feedback from commentators suggesting implementation feedback from IFRS reporters is necessary prior to considering any changes to FRS 102 as a result of these IFRSs, the FRC took the decision not to propose any changes to UK GAAP for the effects of IFRSs 9, 15 and 16. However, it should be noted that eventually there will be consultations on changing UK GAAP for the effects of these IFRSs (but not for the foreseeable future).