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21 December 2016

Dear Jenny

**Subject: Consultation Document: Triennial review of UK and Ireland accounting standards – Approach to changes in IFRS (September 2016)**

The Accounting Committee of Chartered Accountants Ireland (AC) welcomes the opportunity to respond to this Consultation Document and is supportive of the FRC's proposals included therein. AC's specific responses to the questions asked and its additional comments on various matters are set out in the attached Appendix.

#### Other matter

AC notes that the UK GAAP Technical Advisory Group from time to time reviews issues that relate to the implementation of FRS 102. AC considers it would be very helpful if information was published on a regular basis on the FRC website on the nature of issues arising and any decisions made by this grouping to keep preparers, auditors and users of financial statements up to date.

If you would like to discuss this response further please contact me at [barbara.mccormack@charteredaccountants.ie](mailto:barbara.mccormack@charteredaccountants.ie) or at + 353 1 637 7236.

Yours sincerely

**Barbara McCormack**  
**Secretary to the Accounting Committee of Chartered Accountants Ireland**

## Appendix

### Question 1

**The FRC has reviewed its principles for developing succinct financial reporting standards for the UK and Republic of Ireland. As a result, limited changes have been made to the principles, to emphasise the need to balance improvement with stability and the need for proportionate solutions (see paragraph 1.11). Do you agree with the principles? If not, why not?**

AC agrees with the FRC's approach.

### Question 2

**Significant changes in IFRS have been considered against the FRC's principles for developing succinct financial reporting standards for the UK and Republic of Ireland; see Section 3 *Changes in IFRS – Detailed analysis*. Do you agree with the proposals for updating FRS 102 as result of changes in IFRS as part of this triennial review? If not, please provide alternative suggestions.**

AC supports FRC's approach which is to consider each of the more recent significant IFRS amendments with a view to amending FRS 102 in a proportionate and practical way, taking into account the entities that are using FRS 102. AC also supports the general proposed timing for the introduction of the new requirements, with the more significant items being brought in for 2022. AC is also supportive of FRC's proposal in section 1.21 of the Consultation Document to allow in all cases the early application of new requirements for entities wanting to implement the new requirements sooner.

AC's comments on the proposals where specific questions were asked by FRC are set out in the responses to Questions 3-8 below. AC's comments on other FRC proposals referred to in Section 3 are set out below.

#### 2.1 IFRS 3 Business Combinations (2008) - paragraphs 3.4 – 3.7 of the Consultation Document

With certain exceptions, AC supports FRC's proposal not to change FRS 102 to increase consistency with IFRS 3 (2008) for the reasons outlined in the Consultation Document. However, the areas where AC would favour greater alignment are as follows:

- (i) Contingent consideration measurement: AC is of the view that in light of the recent revision to company law that permits the fair value measurement of this type of liability coupled with the potential significance of such an item, it appears appropriate to revise FRS 102 to align it more

closely with IFRS. Therefore, as required by IFRS, the obligation is set up at fair value at the time of the business combination and then subsequently re-measure at fair value through profit or loss.

- (ii) **Clarification of contingent payments that are in scope of business combination accounting:** Please consider expanding the guidance in FRS 102 in relation to determining whether arrangements for contingent payments to selling shareholders constitute (a) consideration for the acquired business (for inclusion as part of the business combination consideration and therefore the determination of the amount of goodwill arising) or (b) consideration for the provision of future services (for expensing in future periods). This is a matter that arises in practice which can have a significant impact on reported results. (IFRS 3.52(b) and IFRS 3.B54, B55)
- (iii) **Settlement of pre-existing contractual relationships:** It would be helpful if the IFRS requirements in this area were reflected in FRS 102 due to the potential significance of these arrangements on the accounting. (IFRS 3.52(a)).
- (iv) AC also suggests that as company law has now been amended to refer to the IFRS concept of 'common control', it would appear timely to review the circumstances in FRS 102 where acquisitions are not required to use purchase accounting (e.g. in group reconstruction situations) with a view to aligning FRS 102 to IFRS in this area. In practice, where there is no change in control but there is some level of change in ownership between shareholders, the use of merger accounting (i.e. book value accounting) may be precluded under FRS 102, thereby being more restrictive than IFRS. If this revision was made, it would result in FRS 102's merger accounting treatment being available for use more broadly i.e. where a 'common control' transaction arises.
- (v) AC considers it would be helpful to include in FRS 102 guidance where a newly incorporated parent (Newco) is added to the top of the group as part of an equity-based group re-organisation. It would be helpful to indicate that in this circumstance it is unlikely that the Newco will be the accounting acquirer and hence the consolidated financial statements of the group will continue to reflect the carrying value of assets and liabilities of the predecessor parent, i.e. no uplift to fair value arises. This guidance is in IFRS 3 and was also in old GAAP in FRS 6. (IFRS 3.B18 and see also FRS 6.14).

## 2.2 IFRS 9 Financial Instruments – paragraphs 3.8 – 3.15 - Definition of a basic debt in FRS 102

AC favours closer alignment of FRS 102's 'basic debt' criteria to IFRS 9's 'solely payment of principal and interest' (SPPI) criteria as the latter appear to be more broadly defined and accommodate common commercial features found in loan contracts. AC favours the consideration of the implementation of these amendments in the FRED Triennial review 2017 Phase 1, for implementation into FRS 102 in 2019.

### 2.3 IFRS 13 Fair Value Measurement

AC agrees with the proposals to more closely align the fair value measurement definition and related guidance in FRS 102 to that in IFRS 13 for 2019. AC also supports the proposal not to expand the level of disclosures generally arising under FRS 102 in this area.

### 2.4 IFRS 15 Revenue from Contracts with Customers

AC supports the objective of allowing groups to have a single accounting policy for revenue where the group applies IFRS, with its subsidiaries using FRS 102. However, for other entities, it may be more practical to deal with the implementation of the new revenue requirements in 2022 all at once rather than on a piecemeal basis. Therefore, AC suggests only making any revisions to FRS 102 in this area mandatory in 2022, but allowing early adoption.

### Question 3

**In relation to the impairment of financial assets, the FRC proposes to amend FRS 102 in order to incorporate an expected loss model. Paragraph 3.13 sets out three options for how this may be achieved, with the FRC favouring option (b). Which option would you prefer, and why?**

**Do you have any suggestions for how the simplified approach to impairment losses for trade receivables, contract assets and lease receivables in IFRS 9 might be developed into a suitable model for entities applying FRS 102 (other than financial institutions, or a sub-set such as banks and building societies)?**

In relation to the implementation of IFRS 9's expected loss model for the impairment of financial assets held at amortised cost, AC favours the option set out in paragraph 3.13(b) that:

- (a) requires certain financial institutions (e.g. banks and building societies) to apply the impairment requirements of IFRS 9 and
- (b) requires all other entities to apply a method based on IFRS 9's simplified approach for trade receivables.

AC considers the simplified approach for application to all other entities, as set out in IFRS 9, to be appropriate and at this point has no specific implementation suggestions to put forward. However, as IFRS preparers start their implementation of IFRS 9, this is an area to monitor to see if practice issues arise that could then be taken into account in developing FRS 102's requirements for 2022.

#### Question 4

**Presently, in paragraph 11.2 (and paragraph 12.2), FRS 102 permits an accounting policy choice in relation to financial instruments, allowing an entity to choose the recognition and measurement requirements of FRS 102, IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 9 *Financial Instruments* (and elements of IAS 39 as amended by IFRS 9). The FRC proposes to retain the option to choose IAS 39 until the requirements for the impairment of financial assets have been amended in FRS 102 (ie for all accounting periods beginning before 1 January 2022). From 1 January 2022 the FRC proposes that the available options will be the requirements of FRS 102 or IFRS 9. Do you agree? If not, why not?**

AC agrees with the proposal to retain the IAS 39 policy option within FRS 102 until the standard reflects the new impairment requirements in 2022. In Ireland, there are a relatively large number of investment fund and securitisation entities that took this policy option on transition to FRS 102 in 2015. This arose because many of them had been in scope of FRS 26 under the prior UK/Irish accounting standards which was aligned with IAS 39. The retention of this IAS 39 policy option will be very helpful for such entities as they will not then be obliged to make policy changes in 2019 and then again in 2022, with their only alternative to doing this being to, in 2019, take an IFRS 9 policy election.

FRC may wish to consider the means by which it will make available to preparers, users and auditors the relevant version of IAS 39 given that it will no longer be available within IASB's book of standards. Arranging for the standard to be available on the FRC's website might be the most practical solution.

#### Question 5

**Do you have any suggestions for how the requirements of IFRS 16 *Leases* might be developed into a suitable model for entities applying FRS 102? In particular, do you have any suggestions relating to the application of the short-term lease exemption or the exemption for leases when the value of the underlying asset is low?**

AC supports addressing the above standard within FRS 102 in 2022 to allow preparers sufficient lead time as regards its effects. However, AC supports allowing entities to early adopt the new requirements should they choose to do so.

AC does not have any specific suggestions to put forward at this point. IFRS preparers are only starting to analyse the impact this new standard will have and therefore monitoring of this would appear helpful in the event that implementation issues arise.

## Question 6

**The FRC proposes to make changes to FRS 102 to incorporate the control model of IFRS 10 *Consolidated Financial Statements*. Company law specifies when consolidated financial statements are prepared, and any changes would supplement these existing requirements by providing further guidance on what is meant by 'control'. Are you aware of any legal barriers to incorporating the control model of IFRS 10 alongside the existing legal requirements?**

**In most situations, any changes to the definition of control in FRS 102 will have no impact in practice. However, in other cases entities may be consolidated for the first time or cease to be consolidated. Do you have any information about how significant the practical impact may be and the circumstances in which it might occur?**

AC favours the proposal to amend FRS 102 to reflect the requirements of IFRS 10 and IFRS 11 in 2019. AC would welcome FRC's consideration of whether there might be any inconsistency within the proposed new control model and company law to ensure that any issues arising are appropriately addressed. AC is not itself aware of any legal barriers to incorporating the control model of IFRS 10 alongside the existing legal requirements. AC agrees that for many entities, the amendments may have little or no effect. AC expects the areas where changes occur will be similar to those arising when IFRS preparers first applied IFRS 10. Different control conclusions may arise, for example, due to:

- the manner in which potential voting rights are taken into account when assessing control;
- the introduction of specific guidance for structured entities coupled with the removal of the 'risks and rewards' model for special purpose entities; and
- the guidance in determining if a party exercising power is doing so as a principal or an agent.

There are two other matters in particular that AC would like to raise here, in relation to FRS 102's consolidation requirements, as follows:

**(i) Exemption from the requirement to prepare consolidated financial statements (FS) in FRS 102.9.3(g)**

FRS 102.9.3(g) says that where a parent is not reporting under the Act (Companies Act, 2006 or the equivalent legislation in Ireland), it is exempt from the preparation of consolidated financial statements (FS) if its statutory framework does not require such consolidated FS to be prepared. This approach is in contrast to the position that prevailed in FRS 2 (in old UK GAAP). In that earlier standard, an entity that was not in scope of company law was required to apply the provisions of FRS 2 on an equivalent basis, i.e. as if it was a company and hence consolidated FS were more frequently required.

Under FRS 102, for a parent that is not in scope of the Act, it appears it only needs to prepare individual FS and it will select a policy choice (FRS 102.9.26) as to how to account for its subsidiaries, with the one most commonly chosen being cost less impairment. This could occur where the parent is simply a holding entity with all substantive operating activities being undertaken by its subsidiaries such that the underlying net assets controlled are worth substantially more than cost. AC considers that it would be desirable to clarify that the exemption in FRS 102.9.3(g) is freely available and that consolidation is not required in order to give a true and fair view.

AC notes there is an investment fund-related Statement of Recommend Practice (SORP) in issue entitled *Financial Statements of UK Authorised Funds* published by the Investment Management Association – May 2014 which includes guidance on the topic of consolidation. This SORP's scope is 'authorised funds' which are defined in section 1.17 to include various unit trusts, open-ended investment companies established under the OEIC Regulations and certain other contractual schemes, all being entities that fall outside of the scope of regular company law. It also includes in section 1.31 a definition of a master-feeder arrangement being one where a feeder fund invests 85% of its assets in a single master scheme. As regards the guidance on consolidation, the SORP includes the following two pieces of guidance:

- (a) *'Authorised funds do not report under the Companies Act and therefore are exempted from the requirement to prepare consolidated financial statements by paragraph 9.3(g) of FRS 102. However, authorised funds that hold investment property through intermediate holding vehicles (IHVs) should prepare consolidated financial statements that include the authorised fund and the IHVs it controls. The consolidation should be prepared in accordance with the procedures set out in section 9 of FRS 102.'* (SORP, section 2.79)
- (b) *'A feeder in a master-feeder arrangement should not consolidate the master but should instead carry the master at fair value.'* (SORP, section 2.20)

In relation to (a) above, it appears the SORP requires the parent authorised fund to consolidate the IHV in order to ensure the parent's financial statements reflect the underlying assets within the IHV. As noted above, AC considers that clarification would be useful that the exemption in FRS 102.9.3(g) is available and is not subject to separate consideration of whether consolidation is necessary in order to give a true and fair view. In addition, the SORP may need to be brought into line with FRS 102.9.3(g).

In relation to (b) above, it appears that in this case it is the feeder parent that has limited operations, with the investing largely being conducted via its subsidiary (master). Here, the SORP indicates that there is no option to consolidate and thus reflect the master's assets on the statement of financial position of the feeder. This is despite, arguably, that the master is not necessarily that dissimilar to an IHV in (i) above.

While the equivalent Irish funds do not fall in scope of the SORP, AC considers that the SORP guidance raises some concerns as to the appropriate approach for entities applying FRS 102 that do not fall in scope of UK/Irish company law. AC therefore would welcome clarification of these points by FRC in its FRED Triennial review 2017 Phase 1.

**(ii) FRS 102's variant of IFRS 10's 'investment entity' (IE) exception**

Paragraph 3.20 of the Consultation Document notes that FRS 102 already includes a variant of the IFRS 10's IE exception. FRS 102's exclusion focusses on the investee and was developed within the constraints/requirements of company law, while IFRS focuses more on the nature of the investor and its business model. In practice, these are of most relevance to the investment fund sector. AC agrees that due to the legal requirements, it may not be possible to align FRS 102 to IFRS in this regard. When developing the amendments to FRS 102, it would be helpful to consider providing explanatory guidance on how the exclusions from consolidation in both standards differ, particularly in relation to the intermediate holding companies and master-feeders referred to in (i) above.

**Question 7**

**Do you have any comments on the cost-effectiveness of the requirements for share-based payments, currently set out in Section 26 *Share-based Payment* of FRS 102? If you consider that alternative requirements would be more cost-effective, please provide details of how you would adapt the current requirements whilst still providing useful information to users.**

AC does not have any proposed revisions to suggest here. Old UK GAAP's FRS 20 has been in place for some time with its requirements largely being carried forward into FRS 102.

**Question 8**

**Do you agree with the proposed effective dates for the amendments arising from the triennial review, with incremental improvements and clarifications effective from 1 January 2019 and more fundamental changes effective from 1 January 2022?**

AC agrees with the proposed timelines in the Consultation Document. In particular, it supports the permission to early adopt the final revisions arising out of both the Phase 1 and Phase 2 FREDs to assist the alignment of FRS 102 subsidiaries of their policies where these entities form part of wider IFRS groups.



## Question 9

**Do you have any other comments on the approach to keeping FRS 102 up-to-date as part of the triennial review?**

**Please note that there is no need to repeat comments about potential areas for improvements to FRS 102 that have already been submitted to [ukfisreview@frc.org.uk](mailto:ukfisreview@frc.org.uk) as these comments have already been noted and will be considered. Detailed comments about potential improvements should continue to be submitted to [ukfisreview@frc.org.uk](mailto:ukfisreview@frc.org.uk). Those comments received by 31 October 2016 will be taken into account in developing formal proposals for changes. Comments received after this date will be taken into account in the later stages of the review, if they cannot be considered sooner.**

### 9.1 Definition of a financial institution

AC notes FRC's intention to review the definition of a 'financial institution' to ensure that it includes appropriate entities. (Footnote 2, on page 15 of the Consultation Document). AC welcomes this initiative and notes that there has been some uncertainty in determining what entities meet the definition of a 'financial institution' and the extent to which some entities appear to fall in scope it is not always entirely clear. One example relates to an investment manager company where its main business activity is providing investment management services to other parties and earning fees that are typically calculated based on a percentage of assets under its management coupled with a performance based fee.

Part (i) of FRS 102's definition of a financial institution includes:

*'any other entity whose principal activity is to generate wealth or manage risk through financial instruments. This is intended to cover entities that have business activities similar to those listed above but are not specifically included in the list above.'*

An investment manager's principal activity is the earning of fees but it achieves that by the generation of wealth/management of risk through financial instruments which are, in the main, not recognised on its own statement of financial position. In considering the second sentence of part (i) of the financial institution definition as set out above, it is unclear that an investment manager's activities are necessarily similar to the entities listed in the earlier parts (a) – (h) of the definition. AC considers that there would appear to be limited merit in including such an entity in scope of the financial institution definition as typically little additional useful information arises from providing the disclosures in section 34 of FRS 102. Some clarification on whether such an entity needs to be within the financial institution definition would be helpful.

## 9.2 Formats of the statement of financial position – Section 4 of FRS 102

The recent EU Accounting Directive introduced greater flexibility in terms of the permitted format of the statement of financial position to allow closer alignment to the ‘current’ versus ‘non-current’ analysis that arises in IAS 1 under IFRS. It would be helpful if FRS 102 were to provide guidance to confirm that this flexibility extends to permitting, where appropriate, IAS 1’s liquidity style format for the statement of financial position in IAS 1.60, with the ‘current’ versus ‘non-current’ analysis instead forming part of the notes to the financial statements.

## 9.3 Financial Instruments disclosures arising in Section 11 of FRS 102

Section 11.48(a) requires disclosure of income, expense, net gains or net losses, including changes in fair value recognised in relation to each of the following: (i) financial assets at fair value, (ii) financial liabilities at fair value, with separate disclosure for those that are neither held for trading nor derivatives, (iii) financial assets at amortised cost and (iv) financial liabilities at amortised cost. It would be helpful to clarify that in the case of items in scope of (iii) and (iv) above, that the requirement is to present the net gains or net losses, i.e. there is no requirement to separately split out income (interest income or dividends in the case of financial assets measured at fair value) or expense (interest expense in the case of financial liabilities).

### Question 10

**The FRC will be preparing consultation stage impact assessments to accompany the FREDs arising from the triennial review. At this stage do you have any comments on the costs and benefits likely to arise from the outline proposals in this Consultation Document that will help inform those impact assessments? Please provide evidence to support your views of any quantifiable costs or benefits.**

AC does not at this point have any comments to make on this matter.