September accounting reminders – IFRS and UK GAAP

Introduction

This publication relates to reporting requirements as at 30 September 2020. The first section on Topical issues includes items that you might want to consider for this year end but you should note that these items are updated real time on PwC’s Inform (see www.inform.pwc.com).

The second part of the document includes the standards and interpretations that are newly applicable for 30 September year ends.

The final part of the document includes the standards and interpretations that are effective in the future but as per paragraph 30 of IAS 8 need to be disclosed.

Topical issues

Climate change

There continues to be an unprecedented level of attention on the work of companies around climate-related reporting. UK Government, investors and regulators have all contributed with the UK Financial Reporting Council (‘FRC’) labelling climate change as “one of the defining issues of our time”.

Further, the FRC has announced that they will be performing a review on how companies and auditors report on the impact of climate change in the coming months.

Key areas of focus that companies need to ensure they consider:

• Quality of their compliance with reporting requirements in relation to climate change;
• Quality of disclosures under the new UK Corporate Governance Code regarding risk, emerging risk and long-term factors affecting their viability; and
• Adoption of the Financial Reporting Lab’s recommendation for companies to report in line with the Task Force on Climate-related Financial Disclosures (TCFD) framework.

Consideration of the accounting impact in financial statements

Companies should also consider the accounting implications of climate change, not limited to the following areas:

• expected credit losses under IFRS 9, ‘Financial instruments’;
• the impairment of tangible and intangible assets under IAS 36, ‘Impairment of non-financial assets’;
• the net realisable value of inventory under IAS 2, ‘Inventories’;
• deferred tax assets in accordance with IAS 12, ‘Income taxes’;
• any asset or liability measured at fair value;
• provisions and contingent liabilities under IAS 37; and
• banking covenants.

This information is extracted from Inform. More information, is available under the Accounting topic home pages which are updated in real-time.
**Front half reporting and considerations**

Areas of front half reporting which may require reporting on climate change, include:

- Principal and emerging risks;
- Non-financial reporting;
- Section 172 (1) statement; and
- Viability statement.

**Coronavirus – impact on the annual report**

The COVID-19 pandemic has developed rapidly throughout 2020. Measures taken to contain the virus have affected economic activity across many sectors, which in turn has implications for financial reporting. As the pandemic continues companies should remain aware of the accounting implications of these developments, not limited to the following areas:

- expected credit losses under IFRS 9, ‘Financial instruments’;
- the impairment of tangible and intangible assets under IAS 36, ‘Impairment of non-financial assets’;
- the net realisable value of inventory under IAS 2, ‘Inventories’;
- deferred tax assets in accordance with IAS 12, ‘Income taxes’;
- any asset or liability measured at fair value; and
- provisions and contingent liabilities under IAS 37, including onerous contracts.

Detailed disclosures on the impact of developments on the carrying amount of assets and liabilities (for example, the need to impair assets or remeasure fair values), or the impact on revenue or on borrowing covenants may be required. Furthermore, disclosures of significant estimates required by IAS1, Presentation of Financial Statements, might need expanding where there is a significant risk of a material adjustment in estimates within the next financial year.

Ensuring that the wider effects of the Coronavirus outbreak have been fully considered is critical – regulators will expect to see evidence of those considerations of the impact on the entity, its business, the numbers, disclosures in the financial statements and other information.

In reporting the impact of the virus and in presenting any exceptional items or Adjusted Performance Measures (‘APM’s’), companies should ensure that they have considered the latest guidance issued by regulators, including the FRC.

For considerations relating to front half reporting refer to our publication which sets out information, based around Q&As, about how the COVID-19 crisis affects areas including going concern and viability, governance, risk and internal control and balancing the interests of shareholders and other stakeholders.

The document takes into account external guidance as well as own comments and recommendations.

We are continuing to update the COVID-19 home page on Inform with links to all of the latest resources we have published to help entities navigate COVID-19 related financial reporting. This includes standards, drafts, PwC interpretations, tools and practice aids and spotlights on specific industry considerations.

**Brexit**

**Considerations for now: risk to financial performance**

For some entities, the implementation period (IP) completion date on 31 December might introduce additional risks that should be factored into reporting. The reporting areas to consider are much the same as for COVID-19 and Climate Change, refer to sections above with both accounting and front half reporting implications.

**Considerations for next year: financial reporting impacts**

Changes have been made to UK company law as it applies to corporate reporting in order to address issues arising from the UK’s exit from the European Union. The Accounts and Reports (Amendment) (EU Exit) Regulations 2019 (‘SI 2019/145’) and the International Accounting Standards and European Public Limited Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (‘SI 2019/685’) address two principal issues:

- When UK quoted companies are no longer bound by the EU Regulation that requires consolidated financial statements to be prepared on the basis of EU-adopted IFRS, what should they do?
- How should the various references to EU or EEA entities in the Companies Act 2006 be dealt with?
In most cases the new statutory instruments will have little impact in practice, but there are some important changes to exceptions and exemptions that will be relevant for some companies – these cover areas such as:

- Qualifying as a small company
- Intermediate parent consolidated financial statements exemption:
- Alteration of accounting reference date
- Dormant subsidiaries
- Changing accounting framework
- Non-financial information statement in the strategic report
- Political contributions
- Control and share structures
- Entities that are not companies
- Overseas companies
- FRC scrutiny of accounts and reports

The changes related to financial years apply to financial years beginning on or after IP completion day (that is, 31 December 2020). For financial years that begin before, but end on or after, this day, the relevant UK law applies as if the UK continued to be a member State.

A company whose financial year straddles IP completion day, such as a 30 September 2021 year end, prepares its financial statements for that year under EU-adopted IFRS or UK GAAP as appropriate (subject to the transitional provision referred to in the next paragraph). In the following year, the financial statements are prepared under UK-adopted IFRS or UK GAAP.

The International Accounting Standards, Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2020 (‘SI 2020/335’) also introduce a transitional option for certain companies to choose to apply UK-adopted IFRS, including standards that are adopted for use within the UK after IP completion day, instead of IFRS as adopted by the EU as at IP completion day. This would include companies with financial years that begin before 31 December 2020 but end on or after 31 December 2020, and those whose financial years end shortly before 31 December 2020 but file their accounts after 31 December 2020.

**IFRS 16 amendment in light of COVID-19**

As a result of the coronavirus (COVID-19) pandemic, rent concessions have been granted to lessees. Such concessions might take a variety of forms, including payment holidays and deferral of lease payments. On 28 May 2020, the IASB published an amendment to IFRS 16 that provides an optional practical expedient for lessees from assessing whether a rent concession related to COVID-19 is a lease modification. Lessees can elect to account for such rent concessions in the same way as they would if they were not lease modifications. In many cases, this will result in accounting for the concession as variable lease payments in the period(s) in which the event or condition that triggers the reduced payment occurs.

The practical expedient only applies to rent concessions for lessees (but not lessors) occurring as a direct consequence of the COVID-19 pandemic and only if all of the following conditions are met:

- the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;
- any reduction in lease payments affects only payments due on or before 30 June 2021; and
- there is no substantive change to other terms and conditions of the lease.

The amendments are mandatory for annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted, including in interim or year end financial statements not yet authorised for issue at 28 May 2020 to permit application of the relief as soon as possible subject to any endorsement process.

Please refer to PwC *In brief INT2020-09* for further guidance.
New requirements for front half reporting

Where do I start?

For periods beginning 1 January 2019 further regulation becomes effective including stakeholder engagement reporting, section 172 and the new corporate governance code. For an overview of which existing and new regulation applies to particular entities refer to our guide: Where do I start? – Governance reform and the impact on corporate reporting. For further information see below.

Stakeholder engagement

A quick reminder of the requirements on stakeholder engagement reporting in the Directors’ Report:

<table>
<thead>
<tr>
<th>Disclosure requirements</th>
<th>Applicable to</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employee engagement</td>
<td>A company with over 250 UK employees.</td>
</tr>
<tr>
<td>• How the directors have engaged with employees, and</td>
<td></td>
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<tr>
<td>• How the directors have had regard to employee interest and the effect of that regard,</td>
<td></td>
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<td>including on the principal decisions taken by the company during the financial year.</td>
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</table>

<table>
<thead>
<tr>
<th>Other stakeholder engagement</th>
<th>A company that exceeds two of the following three thresholds (subject to smoothing arrangements where circumstances change):</th>
</tr>
</thead>
</table>
| How the directors have had regard to the need to foster the company’s business relationships with suppliers, customers and others, and the effect of that regard, including on the principal decisions taken by the company during the financial year. | • £36 million turnover  
• £18 million total balance sheet assets  
• 250 employees.                                                                 |

This information is required to be included in the directors’ report (there is no requirement for this to be made available on a website) and BEIS has been clear that this reporting is not intended to include only information that is strategically material.

For more information refer to: Navigating the stakeholder agenda: A review of how reporting on stakeholder engagement in the FTSE 350 is developing.

Tackling s172 and stakeholder reporting – a diagnostic for subsidiaries.

Section 172 (1) Statement

As a reminder s172(1) is:

“A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to –

a. The likely consequences of any decision in the long term,
b. The interests of the company’s employees,
c. The need to foster the company’s business relationships with suppliers, customers and others,
d. The impact of the company’s operations on the community and the environment,
e. The desirability of the company maintaining a reputation for high standards of business conduct, and
f. The need to act fairly as between members of the company.”

Applicable to: large companies, as defined by the Companies Act. Unquoted companies must also make the statement available on a website.

New Corporate Governance Code

Effective for periods beginning 1 January 2019 is the 2018 UK Corporate Governance Code which contains major revisions since the 2016 UK Corporate Governance Code. In summary the new code:

• Is shorter but not easier,
• Introduces a new emphasis on transparency by requiring companies to explain how governance is applied rather than listing out the processes and procedures,
• Emphasises the boards role to promote long-term sustainable success and how its governance contributes to the delivery of strategy; and
• Explores the boards role in engaging with stakeholders, establishing purpose, values and strategy and ensuring culture is aligned.
High profile changes include:

- **Employee engagement mechanisms** – workforce director, formal workforce advisory panel, designated NED or own arrangement
- **Emerging risks** – robust assessment of principal risks now also considers ‘emerging risks’, which are not necessarily principal risks
- **Remuneration** – reporting to address: strategic rationale (5 year holding period for schemes); fairness (Exec pension levels in line with workforce); engagement with shareholders and other stakeholders; and use of discretion
- **Time limit of tenure of chair** – nine years from first appointment to board (including any time before being chair)
- **Removal of relaxations for non-FTSE 350 companies** – board composition needs to be 50% iNEDs (excl. chair), Chair not allowed on audit committee

For further information refer to the following link.

**Non financial regulations (covered by FRC thematic review)**

The FRC’s November 2019 annual review on corporate reporting emphasised that, based on their review, there are still improvements to be made. They have stressed that the non-financial information statement needs to be more clear and accessible, and to include required content. There is also a need to focus on the impact on the environment.

The non-financial reporting regulations (‘the regulations’) require large EU Public Interest Entities with more than 500 employees on average in a financial year (unless they are exempt) to include a non-financial information statement in their strategic report.

The following are the principal categories of EU PIE:

- a traded company (that is, a company any of whose transferable securities are admitted to trading on a regulated market);
- a banking company;
- an authorised insurance company; or
- a company carrying on insurance market activity.

The non-financial information statement must contain information, to the extent necessary for an understanding of the company’s development, performance, position, and the impact of its activity, relating to, as a minimum:

a) environmental matters (including the impact of the company’s business on the environment),

b) the company’s employees,

c) social matters,

d) respect for human rights, and

e) anti-corruption and anti-bribery matters.

For quoted companies these regulations are broadly consistent with the requirements in the strategic report regulations (with some specific additions that need to be considered) but for those non-quoted companies that fall within the scope of the regulations and are not exempt, there will be a notable increase in the disclosure requirements.

Further information can be found within: UK non-financial reporting (2019)

*Checklist of recent reporting requirements.*

New Companies Act non-financial reporting requirements – Q&As on how to incorporate them into the annual report: In brief UK2019-14.

**Streamlined energy and carbon reporting (‘SECR’)**

*What is the issue?*

Under changes introduced by The Companies (Directors’ Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018 (‘SI 2018/1155’), large unquoted companies and large LLPs are now obliged to report their UK energy use and associated greenhouse gas (‘GHG’) emissions in their annual reports for the first time.

For quoted companies that are already reporting GHG emissions, there are new requirements to report on total global energy use, including detail around methodology and energy efficiency.

**When does it apply?**

SECR took effect from 1 April 2019, and the required disclosures should be included in the annual report for any financial year beginning on or after this date.
What is the impact and for whom?

Who is required to report?

In addition to quoted companies, large private companies and large LLPs are impacted.

The definition of ‘large’ is the same as applies in the existing framework for annual accounts in the Companies Act 2006.

A subsidiary is not obliged to report its energy and carbon information if it meets the following criteria:

• it is a subsidiary undertaking at the end of the financial year;
• it is included in the group report of a parent company;
• that group report is prepared for a financial year of the parent that ends at the same time as, or before, the end of the subsidiary’s financial year; and
• the group report complies with the relevant obligations of the parent to report energy and carbon information and their subsidiaries.

What needs to be reported?

The high-level requirements for reporting under SECR are as follows:

• UK energy use (including offshore), as a minimum:
  • gas;
  • electricity; and
  • fuel from transport purchased for business use (where the journey begins or ends in the UK).
• Underlying global energy use as above (quoted companies only).
• Associated GHG emissions, using published conversion factors.
• Previous year’s figures for energy use and GHG emissions (N/A for the first year of reporting).
• At least one intensity ratio.
• Energy efficiency action taken.
• Disclosure of methodology used (for example, GHG Reporting Protocol).

The report must disclose a measure, in kWh, of the annual quantity of energy consumed in the ways set out above.

Where do I get more details?

The following guidance has been issued by the government: Environmental Reporting Guidelines – Including streamlined energy and carbon reporting guidance March 2019.

Revised Shareholder Rights Directive – remuneration-related aspects

The implementation of the revised EU Shareholder Rights Directive (known as ‘SRD II’) in the UK has resulted in a limited number of changes for quoted companies to the rules around the approval of the remuneration policy. In particular, for policies taking effect on or after 10 June 2019, it is no longer possible to seek shareholder approval of a one-off payment; companies must seek approval for an amendment to the policy. There are also a number of changes to the requirements around the disclosure of the policy, though UK market practice means that many quoted companies have already adopted these.

Changes in relation to the annual report on remuneration include the following, all applicable for financial years commencing on or after 10 June 2019:

• The pay of a de facto CEO must now be disclosed, even if he or she is not officially a main board director.
• The single total figure table must include additional columns to show total fixed and total variable pay.

The report must now set out the annual percentage change in salary, benefits and bonus for all the directors (individually) compared with the annual percentage change for all employees of the parent company. BEIS has confirmed that an additional voluntary disclosure can be made, comparing the changes for directors with another (more representative) group of employees.

Phase 2 amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Amendments for IBOR reform

Following the financial crisis, the replacement of benchmark interest rates such as LIBOR and other interbank offered rates (‘IBORs’) has become a priority for global regulators. Many uncertainties remain but the roadmap to replacement is becoming clearer. The IASB has embarked on a two-phase project to consider what, if any, reliefs to give from the effects of IBOR reform. The Phase 1 amendments, issued in September 2019, provided temporary reliefs from applying specific hedge accounting requirements to relationships affected by uncertainties arising as a result of IBOR reform (‘the Phase 1 reliefs’). The Phase 2 amendments that were issued on 27 August 2020
address issues that arise from the implementation of the reforms, including the replacement of one benchmark with an alternative one.

The Phase 1 amendments provide temporary relief from applying specific hedge accounting requirements to hedging relationships directly affected by IBOR reform. The key reliefs provided by the amendments relate to:

1. Risk components.
2. ‘Highly probable’ requirement.
3. Prospective assessments (economic relationship or expected to be ‘highly effective’).
4. IAS 39 retrospective effectiveness test.
5. Recycling of the cash flow hedging reserve.

The amendments prescribe when each of the reliefs will prospectively cease. In general, the reliefs end at the earlier of (a) when there is no longer uncertainty arising from IBOR reform over the timing or amount of the IBOR-based cash flows of the relevant item, and (b) when the hedging relationship to which the relief is applied is discontinued. More specifically the reliefs cease as follows:

• There is no end date for the relief on risk components.
• The ‘highly probable’ requirement – at the earlier of (a) when there is no longer uncertainty arising from IBOR reform over the timing or amount of the IBOR-based cash flows of the hedged item, and (b) when the hedging relationship of which that the hedged item is part is discontinued. More specifically the reliefs cease as follows:
  • Prospective assessments (expected to be highly effective or economic relationship) – for each of the hedging instrument and the hedged item: when there is no longer uncertainty arising from IBOR reform over the timing or amount of the IBOR-based cash flows or hedged risk of the hedged item or hedging instrument. This means that the relief could end at different times for the hedging instrument and the hedged item. However, if the hedging relationship is discontinued earlier than this date, this relief ceases to apply at the date of hedge discontinuation.
  • Retrospective effectiveness test (IAS 39 only) – at the earlier of (a) when there is no longer uncertainty arising from IBOR reform over the hedged risk and the timing and amount of the IBOR-based cash flows, of both the hedged item and the hedging instrument, and (b) when the hedging relationship to which the relief is applied is discontinued.

• Recycling of the cash flow hedge reserve – at the earlier of (a) when there is no longer uncertainty arising from IBOR reform over the timing or amount of the IBOR-based cash flows of the hedged item, and (b) when the entire amount in the cash flow hedge reserve for a discontinued hedging relationship has been recycled to profit or loss.

The amendments require disclosure of:

• the significant interest rate benchmarks to which the entity’s hedging relationships are exposed;
• the extent of the risk exposure that the entity manages that is directly affected by the interest rate benchmark reform;
• how the entity is managing the process of transition to alternative benchmark rates;
• a description of significant assumptions or judgements that the entity made in applying the reliefs (for example, assumptions or judgements about when the uncertainty arising from interest rate benchmark reform is no longer present with respect to the timing and amount of the interest rate benchmark-based cash flows); and
• the nominal amount of the hedging instruments in those hedging relationships.

The amendments are mandatory and should be applied for annual periods beginning on or after 1 January 2020. Earlier application is permitted.

The Phase 2 amendments provide additional temporary reliefs from applying specific IAS 39 and IFRS 9 hedge accounting requirements to hedging relationships directly affected by IBOR reform:

1. Accounting for changes in the basis for determining contractual cash flows as a result of IBOR reform

For instruments to which the amortised cost measurement applies, the amendments require entities, as a practical expedient, to account for a change in the basis for determining the contractual cash flows as a result of IBOR reform by updating the effective interest rate using the guidance in paragraph B5.4.5 of IFRS 9. As a result, no immediate gain or loss is recognised.
This practical expedient applies only to such a change and only to the extent it is necessary as a direct consequence of IBOR reform, and the new basis is economically equivalent to the previous basis. Insurers applying the temporary exemption from IFRS 9 are also required to apply the same practical expedient. IFRS 16 was also amended to require lessors to use a similar practical expedient when accounting for lease modifications that change the basis for determining future lease payments as a result of IBOR reform (for example, where lease payments are indexed to an IBOR rate).

2. End date for Phase 1 relief for non contractually specified risk components in hedging relationships

The Phase 2 amendments require an entity to prospectively cease to apply the Phase 1 reliefs to a non contractually specified risk component at the earlier of when changes are made to the non contractually specified risk component, or when the hedging relationship is discontinued. No end date was provided in the Phase 1 amendments for risk components.

3. Additional temporary exceptions from applying specific hedge accounting requirements

| Changes to designations and hedge documentation | When the Phase 1 reliefs cease to apply, entities are required to amend the hedge documentation to reflect changes that are required by IBOR reform by the end of the reporting period during which the changes are made. Such amendments do not constitute a discontinuation. |
| Amounts accumulated in the cash flow hedge reserve | When amending the description of a hedged item in the hedge documentation, the amounts accumulated in the cash flow hedge reserve are deemed to be based on the alternative benchmark rate on which the hedged future cash flows are determined. |
| Retrospective effectiveness test (IAS 39 only) | For the purposes of assessing the retrospective effectiveness of a hedge relationship on a cumulative basis, an entity may, on an individual hedge basis, reset to zero the cumulative fair value changes of the hedged item and hedging instrument when ceasing to apply the retrospective effectiveness assessment relief provided by the Phase 1 amendments. |
| Groups of items | When amending the hedge relationships for groups of items, hedged items are allocated to sub-groups based on the benchmark rate being hedged, and the benchmark rate for each sub-group is designated as the hedged risk. |
| Risk components – separately identifiable requirement | An alternative benchmark rate designated as a non-contractually specified risk component, that is not separately identifiable at the date when it is designated, is deemed to have met the requirements at that date if the entity reasonably expects that it will meet the requirements within a period of 24-months from the date of first designation. The 24-month period will apply to each alternative benchmark rate separately. The risk component will, however, be required to be reliably measurable. |

4. Additional IFRS 7 disclosures related to IBOR reform

The amendments require disclosure of: (i) how the entity is managing the transition to alternative benchmark rates, its progress and the risks arising from the transition; (ii) quantitative information about derivatives and non-derivatives that have yet to transition, disaggregated by significant interest rate benchmark; and (iii) a description of any changes to the risk management strategy as a result of IBOR reform.

The amendments are mandatory and should be applied for annual periods beginning on or after 1 January 2021. Earlier application is permitted.

The amendments are subject to endorsement in the EU/EEA, and the EU is following an accelerated process with a view to endorsement in time for use via early adoption for December 2019 year ends. We understand the FRC has plans in place for UK endorsement if EU endorsement does not occur prior to the UK exiting the EU.

This IFRS Talks podcast explains the latest and what clients can do now in response to Phase 1 of IBOR reform. For further details refer to PwC In depth INT2019-04: Practical guide to Phase 1 amendments IFRS 9, IAS 39 and IFRS 7 for IBOR reform, and PwC In brief INT2020-12: Phase 2 amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 – interest rate benchmark (IBOR) reform.
**FRC thematic reviews**

In September 2020 the FRC released two new thematic reviews:

- IFRS 16 – a thematic review of disclosures in the first year of application
- IFRS 15 – a follow-up thematic review

The FRC’s findings and focus areas are primarily aimed at listed companies, however the disclosure recommendations are relevant to any company that applies IFRS in the UK.

For IFRS 16, ‘Leases’, the FRC noted that generally companies provided sufficient disclosures to enable users of the financial statements to understand the adoption of IFRS 16 however there is room for improvement around the quality of disclosures.

The key recommendations related to IFRS 16 are:

- Accounting policies - ensure that these are entity specific and not boilerplate
- Judgements - ensure that disclosures of significant judgements are made and that where they are that the description is adequate
- Disclosures - a reminder to provide the following required disclosures:
  - IFRS 16 para 59 requires information on exposure to lease extension options, variable payment features, and lease commitments; are:
  - IFRS 7 para 39 and B11 requires more granular information for certain time bands in the liquidity disclosures for lease liabilities; and
  - IAS 7 para 44A requires information about changes in lease liabilities arising from financing activities.

For IFRS 15, ‘Revenue from contracts with customers’, the FRC noted that disclosures were not of a sufficient quality – especially around:

- Performance obligations – details around when these are satisfied and therefore when the revenue is recognised
- Variable consideration disclosures
- Disaggregated revenue disclosures – entities could do better at illustrating the nature, amount, timing and uncertainty of revenues
- Timing of revenue recognition and significant judgements made
- Significant movements in contract balances
- Costs to obtain or fulfil a contract

Two FRC thematic reviews that were released in 2019 are still relevant for reporting:

- IFRS 9 – review of disclosures in the first year of application
- Impairment of non-financial assets

The FRC had noted that the implementation IFRS 9 represented significant challenge and change for many companies and that significant work was performed in preparing for and complying with the new requirements. However, the FRC has identified based on its review that there is considerable scope for companies to improve the quality of their disclosures in relation to these standards.

In addition, impairment of non-financial assets is of particular interest to investors given the macroeconomic uncertainty at present. The FRC’s thematic review of IAS 36 disclosures also identified opportunities for improvement in a number of areas.

The key recommendations relating to IFRS 9 disclosures are:

- Analysis of the credit risk profile of financial assets by credit risk ratings grade, days past due or in a provision matrix.
- Disclosure of qualitative and quantitative factors used to determine whether there has been a significant increase in credit risk.
- Explanation of how the simplified approach has been applied to trade receivables, contract assets and lease receivables.
- Discussion of the business model in assessing the classification of financial assets, which tended to be boilerplate or even not provided.

The main opportunities to clarify and enhance disclosures related to IAS 36 impairment are:

- Providing relevant information around significant judgments and key assumptions made in estimating the recoverable amount of assets and cash generating units.
- Explaining the sensitivity to changes in key assumptions, where reasonably possible changes could give rise to impairment or material further adjustments to already impaired assets.

Further details are set out in the key reminders for impairment reviews section below.
While there is no ‘effective date’, the FRC makes clear that the matters referred to above should be taken into account in entities’ next annual reports.

**FRC’s 2018/19 annual report of corporate and reporting**

In October 2019 the FRC has published its Annual Review of Corporate Reporting for 2018/2019. This incorporates a separate open letter to Audit Committee Chairs and Finance Directors to prompt better disclosures in annual reports. Particular areas of focus are on new accounting and reporting requirements, including the new accounting standards on revenue and financial instruments, section 172(1) statements and climate risk. We have gone into further detail on these key areas below.

The FRC’s findings and focus areas are primarily aimed at listed companies. However, there are many aspects of their annual review that could be relevant to any UK company reporting under both IFRS and UK GAAP.

**Corporate reporting generally**

The FRC explores a number of areas that frequently arise from reviews of annual reports performed by its Corporate Reporting Review team. Areas particularly emphasised include:

- **Judgements and estimates**, which continues to be the area in which most questions are raised. Improvements have been noted with more companies clearly distinguishing judgements from estimates, less boilerplate wording and fewer cases where matters were not disclosed as key judgements in the financial statements despite indications to the contrary elsewhere in the annual report. However, lack of, or inadequate sensitivity analysis or information about the range of possible outcomes continues to be the key area of challenge.

- **Consolidation judgements** are the area where most complex cases appear, specifically the question of control over another entity.

- **Statement of cash flows** – a substantial proportion of adjustments that arose from the FRC’s review related to the cash flow statement. Half of the cash flow related adjustments the FRC found related to companies in the FTSE 350 and in the majority of cases the errors were easily identifiable from a desktop review. Most of the errors identified related to misclassification between operating, investing and financing activities, which included:
  - Fees received from associates and joint ventures, restructuring and post-acquisition integration costs and purchase and sale of rental fleet assets were incorrectly presented as investing cash flows rather than operating as required by IAS 7;
  - Disposals of investments in joint ventures and non-trading advances to joint ventures were incorrectly classified as operating cash flows rather than investing cash flows as required by IAS 7; and
  - Repayments of loans from joint ventures were incorrectly presented as operating rather than financing cash flows as required by IAS 7.

**Narrative reporting**

Key themes in this area are consistent with those outlined in the prior year, namely:

- Disclosure of principal risks and uncertainties – more companies were written to in this period with enquiries prompted by information set out elsewhere in the annual report or externally, which may give rise to significant risk but which weren’t identified as such. Climate change is a key example of one such area and the FRC’s Financial Reporting Lab has recently issued a report that includes a range of examples of developing practice in climate-related reporting, as well as outlining what investors want to understand and suggesting some key questions companies should consider when reviewing the quality of their disclosures.

- The comprehensiveness of business reviews – there is sometimes limited reporting about significant balances or transactions that occur in a year and the impact these have on performance, working capital and cash flows.

- Adjusted performance measure (APMs) disclosures – improvements have been noted in the year with better labelling of APMs, less prominence given to such measures and more informative reasons given as to why they have been used. However, this will continue to be an area of focus, in particular clear use of definitions and/or reconciliations to the equivalent IFRS line item, identification of ‘non-recurring’ items that have
been used for a number of years, and identification of the audited IFRS numbers from which APMs are derived.

- Effects of the UK’s decision to leave the EU – whilst the review notes that the continuing lack of uncertainty in this area makes reporting difficult, there was an improvement in disclosures made particularly in regard to the key risks that would be impacted by a departure.

- Non-financial information statement – the reviews found that a number of disclosures in this area were generic and lacked the link to policies, the outcome of the policy of due diligence done. It was also felt that companies had overlooked the requirement to discuss the impact of the business on the environment and associated risks.

**Future developments**

The report also provides a focus on areas of upcoming changes to reporting that will be a focus in the forthcoming year. Notably:

- The introduction of IFRS 16 ‘Leases’
- Interest rate benchmark reform
- Section 172(1) reporting
- UK GAAP – Triennial review 2017 amendments.

**Supplier finance arrangements**

We continue to see a large number of questions around the accounting for supplier financing arrangements, and ever more complicated arrangements involving special purpose vehicles, charitable trusts with companies having both payables and investments tied up in the arrangements. Such arrangements raise the question of whether the trade payables that are the subject of the supplier financing should be derecognised and replaced by a bank borrowing and whether any investment vehicles should be consolidated by the entity.

Accounting correctly for supplier financing arrangements has attracted significant attention from the regulators since the failure of Carillion, with focus, amongst other areas, on a company’s source of finances. This includes whether a company has made material use of supplier finance, if this is transparent from the annual report, whether related balances are appropriately presented as bank debt or trade creditors and whether subsequent cash flows are appropriately presented in the statement of cash flows.

In its 2019 open letter to Audit Committee chairs and finance directors, the FRC observed that it “continues to have particular concerns about the level of disclosure around supplier financing arrangements” despite warning companies in June 2018 that this was an area of specific focus for them that year. In September 2019, the FRC’s Financial Reporting Lab published a report on disclosures of sources and uses of cash. This includes an appendix on the subject of supplier finance which provides, among other things, an illustrative example of good disclosure. The FRC note that IFRS 7 ‘Financial Instruments: Disclosures’ requires companies’ accounts to disclose information that allows readers to understand the nature of and risks around financial instruments, including liquidity risk and that IAS 1 requires companies to consider whether balances are financing or working capital in nature and present them accordingly. It is clear that they expect these requirements to lead companies to disclose the nature of any material supplier financing arrangements, the implications for the company’s liquidity and the relevant amounts, along with any significant accounting judgements.

In February 2020, the IFRS IC has also been asked to consider both the accounting and disclosure of supply chain finance in corporate entities. Their initial discussions are expected to take place shortly.

The level of disclosure that the FRC has indicated it expects with regards to supplier finance arrangements may be greater than the disclosures currently provided by many companies. Companies and engagement teams may wish to revisit existing disclosures and consider if they wish to include any additional disclosures in light of the FRC’s communication and stakeholder attention to this area.

Further guidance on supplier finance arrangements and indicators of extinguishment are available in chapter 44 of the IFRS Manual of Accounting and PwC’s practice aid.

The accounting for supplier finance arrangements will depend on the exact facts and circumstances relating to them. In addition entities should consider how the accounting for supplier finance arrangements is impacted by COVID-19. Further guidance is available in PwC In depth UK2020-02, FAQ 3.5.1.
**Debt and derivative restructurings**

We continue to see a large number of questions on the restructuring of issued debt instruments, for example loan facilities or bond financing and modification of derivatives to take advantage of low interest rates. This is a complex area of accounting which can require significant judgement. To assist engagement teams in understanding the potential issues, some of the key accounting considerations (under IAS 39 and IFRS 9) are summarised below.

Relevant guidance (under IAS 39 and IFRS 9) is provided in IFRS MoA paras 44.106 – 44.110.

- Determining whether the new and old debt have substantially different terms – Under IFRS 9, where a financial liability is exchanged or its terms are modified but the liability remains between the same borrower and the same lender, it is necessary to assess if the terms are substantially different. If they are substantially different, the transaction should be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

- Treatment of gain or loss on modification/extinguishment of debt. In October 2017 the IASB confirmed that when a financial liability measured at amortised cost is modified without this resulting in derecognition, a gain or loss should be recognised immediately in profit or loss. The gain or loss is calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original effective interest rate. This means that the difference cannot be spread over the remaining life of the instrument which may be a change in practice from IAS 39. For further details refer to PwC In brief UK2018-01 and PwC In brief INT2017-13.

- Treatment of fees incurred as part of the renegotiation – whether the fees should be recognised immediately or whether they can be capitalised. (IFRS MoA paras 44.117 – 44.119)

- Use of an Intermediary – A corporate entity may use a bank as an intermediary when restructuring its debt. For example, when a corporate wants to change the terms or maturity date of an existing bond, it may use a bank as an intermediary to buy back the original bonds and then sell the modified bonds to investors.

The accounting for this is complex. A key accounting consideration in this situation is whether the bank is acting as an agent or as principal, which is highly judgmental. If the bank is not acting as principal the corporate would have to treat the modification of the bonds as an extinguishment with any gains/losses recognised in profit and loss.

- Modifications when a credit facility is undrawn. Treatment of a gain or loss arising on modification of derivatives, particularly where no cash payment or receipt is made at the time of the modification. There is often a difference in value due to changes in credit spreads or bank profit margins. This value change does not relate to any existing or future hedge relationships and, if unobservable, that is not directly related to changes in market conditions, should not be recognised in profit or loss immediately.

**Regulatory non financial asset interest and key reminders for impairment reviews**

Impairment is an ongoing area of concern for many of our clients. Regulators remain focused on this area and continue to push for increased transparency in disclosures. Groups holding significant amounts of goodwill and intangibles are at greater risk of a regulatory challenge to their impairment assessments and in particular the related disclosures.

For COVID-19 specific considerations on impairment refer to the first section of this document and to this In Depth which considers the impact of the new coronavirus (‘COVID-19’ or ‘the virus’) on non financial assets for periods ending after 31 December 2019 of entities whose business is affected by the virus.

The key points in impairment testing are:

- For the value-in-use (VIU) model key assumptions should stand up against external market data. Cash flow growth assumptions should be comparable with up-to-date economic forecasts.

- In times of greater uncertainty, it is likely to be easier to incorporate these uncertainties in impairment testing by
using multiple cash-flow scenarios and applying relative probability weightings to derive a weighted average set of cash flows rather than using a single central forecast and attempting to risk adjust the discount rate to reflect the higher degree of uncertainty in the environment.

- IAS 36 requires that the VIU model uses pre-tax cash flows discounted using a pre-tax discount rate. In practice, post-tax discount rates and cash flows are used which theoretically give the same answer but the need to consider deferred taxes makes this very complicated to achieve. Therefore if a post-tax VIU model results in a ‘near miss’ the next step should be to determine fair value less costs of disposal (FVLCD).

- The fair value model, which is a post-tax model, must use market participant assumptions, rather than those of management.

- In assessing for impairment, the carrying value should be determined on a consistent basis as the recoverable amount. For example:
  - Where the recoverable amount is determined using the fair value model, the carrying amount tested should include current and deferred tax assets/liabilities (but exclude assets for tax losses, because these are treated as separate transactions).
  - Where the VIU model (i.e. pre-tax) is applied, deferred tax assets should not be added to the carrying value and deferred tax liabilities should not be deducted (i.e. are not included in the carrying amount of the CGU). This could result in the carrying value for VIU being higher than the carrying value for FVLCD. However, in situations where there is significant deferred tax upfront, an IAS 36 VIU test may not be the most appropriate method to determine the recoverable amount of a CGU.

The required disclosures in IAS 36 are extensive. IAS 36 requires disclosure of the key assumptions (those that the recoverable amount is most sensitive to) and related sensitivity analysis. Note also IAS 1 para 125 requires disclosure of critical accounting judgements and of key sources of estimation uncertainty. Where a reasonable possible change in key assumptions would reduce the headroom (excess of the recoverable amount over the carrying amount) of a CGU to nil, it is required to disclose this headroom.

Where the headroom is sensitive to changes in key assumptions, an entity would need to disclose the specific changes in assumptions that would erode headroom to nil (+/− x% in sales growth or discount rates). However, in cases where no reasonably possible change would either erode headroom for CGUs when testing goodwill or give rise to a material adjustment to any carrying value in the next year, companies should take care that additional sensitivity disclosures do not give the wrong impression or become confusing to users. Given the increased uncertainty and volatility in many markets at present, the range of reasonably possible changes has widened which means that more extensive impairment disclosures will be required.

Key assumptions and wider ranging assumptions covering multiple Cash Generating Units (‘CGUs’) should be clearly disclosed. Where material, assumptions specific to each CGU should be identified. Changes to assumptions used, such as the discount rate, which has changed significantly from the previous year should be explained. Furthermore, in an impairment case, the entities would need to clearly disclose what the cause of the impairment was and whether this is based on external data or changes in the company’s own estimates. An entity with a material impairment loss or reversal additionally need to disclose the recoverable amount of the asset(s) or CGU(s) affected (IAS 36 para 130 [e]).
Regulators have observed that, whilst the long-term growth rate used to extrapolate cash flow projections (to estimate a terminal value) and the pre-tax discount rate are important; they are not ‘key assumptions’ on which the cash flow projections for the period covered by the most recent budgets or forecasts are based. Therefore, attention should also be paid to the discrete growth rate assumptions applied to the cash flows projected to occur before the terminal period. Accounting policy disclosures should always be consistent with the basis used in the according impairment test. The regulators have pointed out, that they will continue to challenge companies where the recoverable amount is measured using VIU, but the cash flow forecasts appear to include the benefits of developing new business or to rely on future investment capacity.

Key points to consider for impairment related disclosures in 2019/2020 accounts:
• Brexit and other political/macroeconomic risks
• Climate change and environmental impact
• Impact of Coronavirus
• Interaction with IFRS 16.

For more tips on impairment reviews of non-financial assets, refer to In depth INT2015-08 or the FRC’s Thematic review (October 2019).

Additional considerations with the implementation of IFRS 16

With the implementation of IFRS 16, there had been some effects on IAS 36 accounting for impairments of non-financial assets, which includes right of use assets. The adoption of IFRS 16 might result in a reduction in headroom if the change in value in use discounted cash flows is lower than the increase in CGU assets being tested. This depends on the interaction of increased expected cash flows and lower discount rates.
• There will be more assets in the CGU as it now includes right of use assets
• There could be a change in gross cash flows because the lease payments that are part of the lease liability are excluded. Although these could be offset by an increase in cash outflows to replace leased assets where the lease term is shorter than the time period within the value in use model
• The discount rate could be lower due to the impact of lease liabilities when determining the debt:equity mix.
• If the increase in present value cash flows is lower than the increase in CGU assets being tested, headroom will reduce.
Standards, IFRICs and other guidance applicable to 30 September 2020 year ends

Standards and IFRICs newly applicable for companies with 30 September 2020 year ends are set out below.

IFRS 16 ‘Leases’

This standard replaces the current guidance in IAS 17 and is a far-reaching change in accounting by lessees in particular.

Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a ‘right-of-use asset’ for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees.

For lessors, the accounting stays almost the same. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees.

Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

For further details see In depth 2018-08.

Amendment to IFRS 9, Financial instruments’, on prepayment features with negative compensation and modification of financial liabilities

This amendment confirmed two points: (1) that reasonable compensation for prepayments can be both negative or positive cash flows when considering whether a financial asset solely has cash flows that are principal and interest and (2) that when a financial liability measured at amortised cost is modified without this resulting in de-recognition, a gain or loss should be recognised immediately in profit or loss. The gain or loss is calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original effective interest rate. This means that the difference cannot be spread over the remaining life of the instrument which may be a change in practice from IAS 39.

For further details see In depth 2018-08.

Annual improvements 2015–2017

These amendments include minor changes to the following standards:

• IFRS 3, ‘Business combinations’, – a company remeasures its previously held interest in a joint operation when it obtains control of the business.

• IFRS 11, ‘Joint arrangements’, – a company does not remeasure its previously held interest in a joint operation when it obtains joint control of the business.

• IAS 12, ‘Income taxes’ – a company accounts for all income tax consequences of dividend payments in the same way.

• IAS 23, ‘Borrowing costs’ – a company treats as part of general borrowings any borrowing originally made to develop an asset when the asset is ready for its intended use or sale.

For further details see In depth 2018-08.
Amendments to IAS 28 ‘Investments in associates’, on long term interests in associates and joint ventures
These amendments clarify that companies account for long-term interests in an associate or joint venture to which the equity method is not applied using IFRS 9.
For further details see In depth 2018-08.

Amendments to IAS 19, ‘Employee benefits’ on plan amendment, curtailment or settlement
These amendments require an entity to:
• use updated assumptions to determine current service cost and net interest for the reminder of the period after a plan amendment, curtailment or settlement; and
• recognise in profit or loss as part of past service cost, or a gain or loss on settlement, any reduction in a surplus, even if that surplus was not previously recognised because of the impact of the asset ceiling.
For further details see In depth 2018-08.

IFRIC 23, ‘Uncertainty over income tax treatments
This IFRIC clarifies how the recognition and measurement requirements of IAS 12 ‘Income taxes’, are applied where there is uncertainty over income tax treatments.
The IFRS IC had clarified previously that IAS 12, not IAS 37 ‘Provisions, contingent liabilities and contingent assets’, applies to accounting for uncertain income tax treatments. IFRIC 23 explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.
An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority. For example, a decision to claim a deduction for a specific expense or not to include a specific item of income in a tax return is an uncertain tax treatment if its acceptability is uncertain under tax law. IFRIC 23 applies to all aspects of income tax accounting where there is an uncertainty regarding the treatment of an item, including taxable profit or loss, the tax bases of assets and liabilities, tax losses and credits and tax rates.
For further details see In depth 2018-08.
**New IFRS standards effective after 1 October 2020**

Under paragraph 30 of IAS 8, entities need to disclose any new IFRSs that are issued but not yet effective and that are likely to impact the entity. This summary includes all new standards and amendments issued before 30 September 2020 with an effective date after 1 October 2020. These standards can generally be adopted early, subject to EU endorsement in some countries.

<table>
<thead>
<tr>
<th>Amendments to IFRS 3 – definition of a business</th>
<th>This amendment revises the definition of a business. According to feedback received by the IASB, application of the current guidance is commonly thought to be too complex, and it results in too many transactions qualifying as business combinations. For further details see In brief 2018-13.</th>
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<tbody>
<tr>
<td>Published</td>
<td>October 2018</td>
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<tr>
<td>Effective date</td>
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<tr>
<td>Amendments to IAS 1 and IAS 8 on the definition of material</td>
<td>These amendments to IAS 1, ‘Presentation of financial statements’, and IAS 8, ‘Accounting policies, changes in accounting estimates and errors’, and consequential amendments to other IFRSs: i) use a consistent definition of materiality throughout IFRSs and the Conceptual Framework for Financial Reporting; ii) clarify the explanation of the definition of material; and iii) incorporate some of the guidance in IAS 1 about immaterial information. For further details see In brief 2018-14.</td>
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<tr>
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<tr>
<td>Amendments to IFRS 9, IAS 39 and IFRS 7 – Interest rate benchmark reform</td>
<td>These amendments provide certain reliefs in connection with interest rate benchmark reform. The reliefs relate to hedge accounting and have the effect that IBOR reform should not generally cause hedge accounting to terminate. However, any hedge ineffectiveness should continue to be recorded in the income statement. Given the pervasive nature of hedges involving IBOR-based contracts, the reliefs will affect companies in all industries. For further details see In brief INT2019-11</td>
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<tr>
<td>Published</td>
<td>September 2019</td>
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<tr>
<td>Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform – Phase 2</td>
<td>The Phase 2 amendments address issues that arise from the implementation of the reforms, including the replacement of one benchmark with an alternative one. For further details see In brief INT2020-12</td>
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<tr>
<th>Amendment to IFRS 16, ‘Leases’ – Covid-19 related rent concessions</th>
<th>As a result of the coronavirus (COVID-19) pandemic, rent concessions have been granted to lessees. Such concessions might take a variety of forms, including payment holidays and deferral of lease payments. On 28 May 2020, the IASB published an amendment to IFRS 16 that provides an optional practical expedient for lessees from assessing whether a rent concession related to COVID-19 is a lease modification. Lessees can elect to account for such rent concessions in the same way as they would if they were not lease modifications. In many cases, this will result in accounting for the concession as variable lease payments in the period(s) in which the event or condition that triggers the reduced payment occurs. See our In brief INT2020-09 for the details.</th>
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<tr>
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<tr>
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<tr>
<th>IFRS 17, ‘Insurance contracts’</th>
<th>This standard replaces IFRS 4, which currently permits a wide variety of practices in accounting for insurance contracts. IFRS 17 will fundamentally change the accounting by all entities that issue insurance contracts and investment contracts with discretionary participation features. See In depth 2018-08.</th>
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<tr>
<th>Amendments to IAS 1, ‘Presentation of financial statements’ on classification of liabilities</th>
<th>These narrow-scope amendments to IAS 1, ‘Presentation of financial statements’, clarify that liabilities are classified as either current or non-current, depending on the rights that exist at the end of the reporting period. Classification is unaffected by the expectations of the entity or events after the reporting date (for example, the receipt of a waiver or a breach of covenant). The amendment also clarifies what IAS 1 means when it refers to the ‘settlement’ of a liability. For further details see In brief INT2020-03.</th>
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A number of narrow-scope amendments to IFRS 3, IAS 16, IAS 17 and some annual improvements on IFRS 1, IFRS 9, IAS 41 and IFRS 16


**Amendments** to IAS 16, ‘Property, plant and equipment’ prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss.

**Amendments** to IAS 37, ‘Provisions, contingent liabilities and contingent assets’ specify which costs a company includes when assessing whether a contract will be loss-making.


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### New UK GAAP standards effective after 1 October 2020

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<tr>
<th>Standard</th>
<th>Description</th>
<th>Amendments</th>
<th>Published</th>
<th>Effective date</th>
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<tr>
<td>FRS 102 amendments to interest rate benchmark reform</td>
<td>These amendments to specific hedge accounting requirements in FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland provide relief that will avoid unnecessary discontinuation of hedge accounting during the period of uncertainty. Entities will apply specific hedge accounting requirements assuming that the interest rate benchmark relevant to the hedge accounting is not altered as a result of interest rate benchmark reform.</td>
<td>December 2019</td>
<td>Accounting periods beginning on or after 1 January 2020 with early application permitted.</td>
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<tr>
<td>Amendments to FRS 102 and FRS 105 – COVID-19-related rent concessions</td>
<td>These amendments set our clear requirements for recognising changes in operating lease payments arising from COVID-19-related rent concessions on a systematic basis over the periods the change in lease payments is intended to compensate.</td>
<td>October 2020</td>
<td>Accounting periods beginning on or after 1 January 2020 with early application permitted.</td>
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<td>Amendments to FRS 104 – Going concern</td>
<td>These amendments clarify and enhance the requirements relating to the going concern basis of accounting in respect of interim financial reports.</td>
<td>October 2020</td>
<td>Interim periods beginning on or after 1 January 2021, with early application permitted.</td>
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<td>Amendment to FRS 101 Reduced disclosure framework on the effective date of IFRS 17</td>
<td>These amendments change the effective date of an amendment to the definition of a qualifying entity, effectively allowing relevant insurers to continue to apply FRS 101 for a further two years.</td>
<td>October 2020</td>
<td>Accounting periods beginning on or after 1 January 2023.</td>
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