



Financial Reporting Advisory Board Paper

In year amendments for Government Financial Reporting Manual (FReM) and Illustrative Statements for 2019-20

Issue:	HM Treasury requests that the FRAB agrees to the publication of an update to the 2019-20 FReM and Illustrative Statements.
Impact on guidance:	The FReM and Illustrative Statements are updated for application from 2019-20. Amendments are made for minor corrections; to improve clarity; and to reflect decisions made on IFRS 16 in April 2019.
IAS/IFRS adaptation or interpretations for the public-sector context?	Yes – the 2019-20 FReM introduces new interpretations and adaptations for the public-sector context for IFRS 16 (only applicable for those entities early adopting IFRS 16 from 1 April 2019).
Impact on WGA?	Yes – WGA will be expected to incorporate the changes made in accounting standards within the Whole of Government Accounts. The 2019-20 WGA will be prepared on an IAS 17 basis.
IPSAS compliant?	Yes, for 2019-20 (given the public sector will mainly be following IAS 17 in 2019-20)
Impact on Estimates/budgetary regime?	No Estimates or budgetary regime impacts are anticipated for 2019-20.
Alignment with National Accounts	Yes, for 2019-20 (given the public sector will mainly be following IAS 17 in 2019-20).
Recommendation:	That FRAB notes the proposed amendments to the FReM and illustrative statements for 2019-20 and agrees their publication.
Timing:	The updated Manuals will be published in December 2019.

DETAIL

Background

1. The Memorandum of Understanding between the Relevant Authorities for developing financial reporting guidance for the public sector requires that the version of the FReM for financial year 2020-21 is available to users by 1 January 2020. This is covered in FRAB (138) 03. This paper

requests that the Board notes the proposed amendments to the FReM for 2019-20 and agrees to their publication.

2. In-year changes are proposed for the 2019-20 FReM and illustrative statements for minor corrections and to improve clarity. This paper requests that the Board notes the proposed amendments to the FReM for 2019-20 and agrees to their publication.

3. This paper also summarises the major and minor amendments to IFRS applicable for reporting periods starting from 1 January 2019 or 1 January 2020.

Amendments to the 2019-20 FReM and illustrative statements

4. Minor changes and corrections are proposed to the 2019-20 FReM for clarity, and to incorporate some changes to the reporting of Statement of Parliamentary Supply (SoPS) note 4. The proposed amendments to the FReM and illustrative statements are summarised at Annex B.

5. In Autumn 2019 the Treasury had public consultation on the reporting requirements of SoPS note 4 (See paper (138) 03). There was consensus from respondents that there is a need to improve SoPS 4 disclosure. The Treasury believe that some of these changes can be brought into 2019-20 FReM. The data being presented is not changing, merely the way it is being presented. Alterations to disclosures relate to formatting and the requirement to include explanatory text, which is provided in the illustrative disclosures.

6. The final version of the 2019-20 FReM is included at Annex C.

Amendments to IFRS

Minor amendments

7. There are no minor amendments in the updated 2019-20 FReM.

8. Does the Board agree with the proposed approach to adopt all amendments in the 2019-20 FReM?

Major amendments

IFRS 16

9. IFRS 16 is effective in the private sector from 1 January 2019. The FRAB have agreed that it will be effective in central government from 1 April 2020 (with an option for early adoption when specific, limited criteria have been met).

10. As set out in paper FRAB 138 (06), the following text is proposed for the 2019-20 FReM to support the early adoption of IFRS 16 for those departments who meet the criteria for early adoption.

11. This text is shown in track changes from the draft 2019-20 FReM published in December 2018. The changes are mainly needed to reflect the decisions FRAB made on nil-consideration leases and subsequent measurement of the right-of-use asset in April 2019.

IFRS 16 Leases	
Adaptations	<p>1. IFRS 16, as adapted and interpreted by this Manual, will be effective from 1 April 2020, with one exception. Early adoption from 1 April 2019 is available for entities where the following criteria are met:</p> <ul style="list-style-type: none"> • the entity has at least one subsidiary that, under the Companies Act, is required to follow IFRS as adopted by the EU, and the total assets of the subsidiary comprise at least 10% of the total assets at the group level; • the subsidiary (or subsidiaries) described above have operating lease commitments that comprise at least 10% of the operating lease commitments at the group level; and • approval to early adopt has been received from HM Treasury. <p>2. The definition of a contract is expanded to include intra-UK government agreements where non-performance may not be enforceable by law.</p> <p>3. Peppercorn leases are defined as leases for which the consideration paid is nil or nominal (that is, significantly below market value). Peppercorn leases are in the scope of IFRS 16 if they meet the definition of a lease in all aspects apart from containing consideration. All lessees shall account for peppercorn leases using the following criteria:</p> <ul style="list-style-type: none"> • Recognise a right-of-use asset and initially measure it at current value in existing use or fair value, depending on whether the right-of-use asset will be held for its service potential and as set out in paragraphs 7.1.4-7.1.6. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with paragraphs 7.1.34-7.1.39. • Recognise a lease liability measured in accordance with IFRS 16. • Recognise any difference between the carrying amount of the right-of-use asset and the lease liability as income as required by IAS 20 as interpreted in this Manual. • Subsequently measure the right-of-use asset following the principles of IFRS 16 as adapted and interpreted in this Manual. • Upon transition, any peppercorn leases that were not previously classified as finance leases under IAS 17¹ shall be recognised as follows: <ul style="list-style-type: none"> • The right-of-use asset shall be measured at current value in existing use or fair value, depending on whether the right-of-use asset will be held for its service potential and as set out in paragraphs 7.1.4 7.1.6. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with paragraphs 7.1.34-7.1.39. • The lease liability shall be measured at the present value of lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application. • The difference between the carrying amount of the right-of-use asset and lease liability shall be included as part of the adjustment to the opening balances of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16 (C5(b)).

¹ This includes any peppercorn leases that previously were classified as operating leases under IAS 17, or were argued to be outside the scope of IAS 17 because they did not include a payment, or series of payments.

<p>Interpretations</p>	<p>1. The option to apply the election in IFRS 16 (5) has been withdrawn. All entities must apply the recognition and measurement exemption for short-term leases in accordance with IFRS 16 (6-8).</p> <p>2. Where lessees cannot readily determine the interest rate implicit in the lease, they are instead required to use the HM Treasury discount rates promulgated in PES papers as their incremental borrowing rate. However, if an entity can demonstrate that another discount rate would more accurately represent their incremental borrowing rate (for example, if they undertake external borrowing independently of the Exchequer), they shall use that discount rate as their incremental borrowing rate.</p> <p>3. The subsequent measurement basis for right-of-use assets shall be consistent with the principles for subsequent measurement of property, plant and equipment set out in the adaptations to IAS 16 in this Manual.</p> <p>4. The option to reassess whether a contract is, or contains, a lease at the date of initial application has been withdrawn. All entities shall use the practical expedient detailed in IFRS 16 (C3).^[1]</p> <p>5. Upon transition, the accounting policy choice to apply IFRS 16 retrospectively to each prior period presented in accordance with IAS 8 has been withdrawn. All entities applying this Manual shall recognise the cumulative effects of initially applying IFRS 16 recognised at the date of initial application as an adjustment to the opening balances of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16(C5(b)).</p> <p>6. Upon transition, entities shall measure the right-of-use asset for leases previously classified as operating leases per IFRS 16((C8 (b)(ii))): at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.</p> <p>7. Upon transition, all entities applying this Manual shall apply the following options for leases previously classified as operating leases:</p> <ul style="list-style-type: none"> • No adjustments for leases for which the underlying asset is of low value that will be accounted for applying IFRS 16 (6). (IFRS 16 C9 (a)) • No adjustment for leases for which the lease term ends within 12 months of the date of initial application (with a requirement to include the cost associated with those leases in the short-term lease expense disclosure). (C10 (c)) • Use hindsight in determining the lease term if the contract contains options to extend or terminate the lease. (C10 (e))
------------------------	--

^[1] This presumes that entities have been applying the guidance in IAS 17 and IFRIC 4 appropriately in the past. Any known misapplication of the definition of a lease guidance should be corrected as a prior period error in accordance with IAS 8 unless an entity has explicit approval from the relevant authority to do otherwise.

Recommendation

12. The Board is requested to consider the proposed amendments to the 2019-20 FReM and to agree the publication.

HM Treasury
21st November 2019



Annex A – Analysis of Amendments to IFRS

Amendment	IASB Effective date: periods beginning on or after	FRoM introduction effective date (subject to EU adoption)	Summary of changes	Public sector specific reporting issue
IFRS 16 – Leases (Replaces IAS 17 Leases and related interpretations)	January 2019 (EU Endorsed 31 October 2017)	2020-21 Early adoption permitted in limited circumstances for 19-20	<p>The IASB issued IFRS 16 in January 2016 with an effective date for annual periods beginning on or after 1 January 2019. Early application is permitted for those entities applying IFRS 15.</p> <p>IFRS 16 represents a significant change in lessee accounting by largely removing the distinction between operating and finance leases and introducing a single lessee accounting model. A lessee is required to recognise assets and liabilities for all leases, unless they qualify for low value or short-term exemptions. In addition, there are updated disclosure requirements.</p> <p>The lessor accounting model is generally unchanged from IAS 17 but entities should be aware of the introduction and impacts of IFRS 9 Financial Instruments, enhanced disclosure requirements and that a sub-lessor now determines whether a lease is finance or operating based on the right of use asset it subleases.</p>	IFRS 16 will likely affect all public sector bodies. Public sector adaptations and interpretations of the standard have finalised and departments should be preparing for implementation in 20-21.
Conceptual Framework	1 January 2020 (amendments to references to the conceptual framework in IFRS standards)	2019-20	<p>The revised Conceptual Framework, issued by the Board in March 2018, includes:</p> <ul style="list-style-type: none"> • a new chapter on measurement; • guidance on reporting financial performance; • improved definitions of an asset and a liability, and guidance supporting these definitions; and 	None noted

Amendment	IASB Effective date: periods beginning on or after	FReM introduction effective date (subject to EU adoption)	Summary of changes	Public sector specific reporting issue
	pending EU endorsement)		clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.	
IFRS 3 – Business Combinations: Definition of a Business (Amendments)	1 January 2020 (pending EU endorsement)	2020-21	<p>The amendments clarify the definition of a business and:</p> <ul style="list-style-type: none"> • confirm that a business must include inputs and a process, and clarify that: <ul style="list-style-type: none"> ○ the process must be substantive; and ○ the inputs and process must together significantly contribute to creating outputs. • narrow the definitions of a business by focusing the definition of outputs on goods and services provided to customers and other income from ordinary activities, rather than on providing dividends or other economic benefits directly to investors or lowering costs; and • add a test that makes it easier to conclude that a company has acquired a group of assets, rather than a business, if the value of the assets acquired is substantially all concentrated in a single asset or group of similar assets. 	<p>Minimal</p> <p>While there may be substantial investments held in businesses outside the public-sector boundary, it is unlikely the amendments will significantly affect public sector account preparers.</p>
IAS 1 and IAS 8 – Disclosure initiative: Definition of material (Amendments)	1 January 2020 (pending EU endorsement)	2020-21	<p>The amendments clarify the definition of material and its application by:</p> <ul style="list-style-type: none"> • aligning the wording of the definition of material across all IFRS Standards and other publications and making minor improvements to that wording; • including some of the supporting requirements in IAS 1 Presentation of Financial Statements in the definition to give them more prominence; and • clarifying the explanation accompanying the definition of material. 	None noted.



Annex B: In-year amendments to the 2019-20 Government Financial Reporting Manual (FReM)

Amendments have been made to the 2019-20 FReM and illustrative statements to correct minor errors and provide clarifications to improve disclosure requirements and the introduction of the Non-Financial Reporting Regulations.

Paragraph	Change	Reason for change
Throughout	Minor grammatical errors	
1.1.5	Paragraph added to make reference to government functional standard finance (GFS).	GFS is a summary document, signposting to other more relevant documents.
3.1 & 3.2	These Chapters have been updated to incorporate changes made to SOPS that is applicable in 2019-20.	To incorporate changes that are applicable to 2019-20.
4.1.5	New paragraph: Additional guidance on trading funds	To provide additional clarity on accounting boundaries
4.1.6, 7	New paragraph: Additional reference to Companies Act 2006	To provide additional clarity on accounting boundaries and disclosure requirements
4.2.12, 4.2.14	New paragraph, additional lines on Machinery of Government, and a link where guidance can be found.	To help users of the FReM access other relevant guidance.
5.2.8	Added reference to the Orange Book: Management of Risk - Principles and Concepts	To help users of the FReM access other relevant guidance.
5.2.11	New paragraph: additional wording to cover Northern Ireland reporting requirements.	To provide clarity to users of the FReM in Northern Ireland.
5.2.12	Previously para 5.2.11, rewording to improve clarity	Improve clarity
5.2.3	Performance report: Added reference to new table 5.2 Five top tips to improve government financial reports.	Included following additional advice sent out to Finance Directors.
5.3.15	New paragraph: added to make reference to Corporate Governance Code and the Orange Book.	To help users of the FReM access other relevant guidance.

5.3.18	Amended to reflect the importance of staff remuneration and staff report.	To emphasise the importance of staff report.
5.3.28 J	Amended wording in line with guidance provided by Civil Service Pensions (Annex C, exit packages table).	To ensure there is clarity on the data requirements for exit packages.
5.3.29 f)	Staff report - amended to clarify disclosure requirements for Trade Union Facility Time, and to provide a link to where the data can be published online.	To help users of the FReM access other relevant guidance.
5.3.29 f)	Updated reference to relevant legislation	Amended to reflect relevant legislation
5.5.2	Slight amendment to wording.	Amendment for clarification.
8.1.12	Updated reference to relevant legislation	Amended to reflect relevant legislation
8.2.15	Rewording to improve clarity on standard	Amended following feedback from stakeholders on IFRS implementation.
10.4.2	Updated reference to relevant legislation	Amended to reflect relevant legislation
Annex 4: links to supporting documents	Added additional links.	Links for documents referred to throughout the manual.
Table 5.2	Added: New table summarising HMT top 5 tips to improve government financial reports	This is in line with additional advice sent out to Finance Directors.
Table 6	Removed tick under "Applies as adapted for public sector",	Amendment for clarification.
Table 6.2	Updated wording on IFRS 16 adaptations and interpretations	To reflect FRAB decisions on nil consideration leases and ROU subsequent measurement in April 2019.
Table 6.2	Removed repeated row on IFRS 16.	Removed repeated row on IFRS 16.
Department Yellow	Changes to SOPS disclosure	To help provide more clarity in disclosure of accounts
Department Yellow, Agency Pink, NDPB Green	Added additional disclosure line in section 2.3 Exit packages	To identify exit packages accounted for in full

Department Yellow, Agency Pink, NDPB Green	Reference to Trade Union Facility Time disclosure	To help users of the FReM access other relevant guidance.
--	--	--