HM Treasury

Post implementation review of IFRS 9 and IFRS 15

Contents

1. Executive summary and overview 1
2. Strand 1: Preparers' review 5
3. Strand 2: Users' review and desktop review 9
4. Strands 1 & 2: Summary of findings and conclusions 21
5. Strands 1 & 2: More detail and next steps 22

Executive summary

Why this thematic review:

- The Treasury has committed to undertake regular thematic reviews of government financial reporting
- IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* were implemented in the public sector from 01 April 2018, so were first reflected in the 2018-19 annual report and accounts
- IFRS 9 and IFRS 15 are the most significant change in financial standards in recent years and the implementation has been a major reporting challenge for the whole of the public sector
- The Treasury is the relevant authority for central government financial reporting and, as such, leads the implementation process for new financial standards
- The Treasury supports the continuous improvement of financial reporting and will learn from the implementation of these standards for the implementation of future standards

The review:

- This review was undertaken over the summer and autumn of 2019. It had two strands, consisting of:
    1. A request for feedback from preparers of annual reports and accounts focusing on the four year implementation process led by the Treasury and some questions on self-review
    2. A review into the quality of disclosures contained in the annual reports and accounts via:
        - a request for feedback from users
        - a desktop review of a sample of 30 annual reports and accounts
- This report provides a summary of the review, with more detail on each strand.
- It also sets out findings, conclusions, and next steps.

Summary findings:

- Preparers were content with the timing and content of guidance provided during the implementation process run by the Treasury but there are lessons learnt for the Treasury which will be relevant when implementing new accounting standards in future
- Some organisations developed very good examples of clear, succinct and easy to read disclosures which significantly add to users' understanding in respect to IFRS 9 and IFRS 15. Examples are shared in this report.
- Disclosure quality is variable. Some annual reports and accounts contain less information, or less well-structured detail of the standards and impact of implementation on the organisation. As well as sharing best practice examples, the Treasury is revising guidance to support departments as they improve the quality of their financial reporting.

Overview
Key terms and concepts

The Government Financial Reporting Manual (FReM):

- Central government entities follow EU adopted International Financial Reporting Standards (IFRS) as adapted and interpreted for the public sector context set out in the Government Financial Reporting Manual (FReM)
- The FReM is a technical accounting guide for the preparation of financial statements and is owned by the Treasury
- It is prepared following consultation with the Financial Reporting Advisory Board (FRAB).

The government financial reporting review:

- The Treasury published the [The government financial reporting review]() in April 2019
- In this report, the Treasury made a number of commitments aimed at supporting the continuous improvement in government financial reporting
- One of the commitments made in this report was to undertake regular thematic reviews of government financial reporting
- These thematic reviews are intended to support the Treasury's statutory role as a standard setter for central government financial reporting

The Financial Reporting Advisory Board (FRAB):

- The Government Resource and Accounts Act 2000 (GRAA) sets out that the Treasury shall consult a group of appropriate people to advise on financial reporting and standards.
- This statutory role is fulfilled by FRAB, and independent body which ensures that government financial reporting meets the best possible standards

IFRS 9

The International Accounting Standards Board (IASB) sets out the objective of IFRS 9 *Financial instruments* as:

"The objective of this Standard is to establish principles for the financial reporting of *financial assets* and *financial liabilities* that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows" (IFRS 9, page A304)

IFRS 15

The International Accounting Standards Board (IASB) sets out the objective of IFRS 15 *Revenue from contracts with customers* as:

"The objective of this Standard is to establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing and uncertainty of *revenue* and cash flows arising from a *contract* with a *customer*" (IFRS 15, page A665)

Overview
Process of the IFRS 9 & IFRS 15 thematic review

Scope and methodology:

- This early post-implementation review focused on the way IFRS 9 and IFRS 15 were implemented in central government
- The review referred to disclosures made in the audited 2018-19 annual reports and accounts
- Both preparers and users of annual reports and accounts were invited to respond via questionnaires
- A sample of 30 annual reports and accounts from across government were reviewed as part of the Treasury's desktop review
- All respondents were invited to a workshop in October 2019 to discuss the initial findings from this thematic review and to provide the opportunity for any further feedback

Strand 1:

Preparers of annual reports and accounts gave feedback on:

- the Treasury-led implementation plan, including guidance content
- self-reflection on their organisation's own implementation process
- Disclosures relating to IFRS 9 and IFRS 15 in their annual reports and accounts

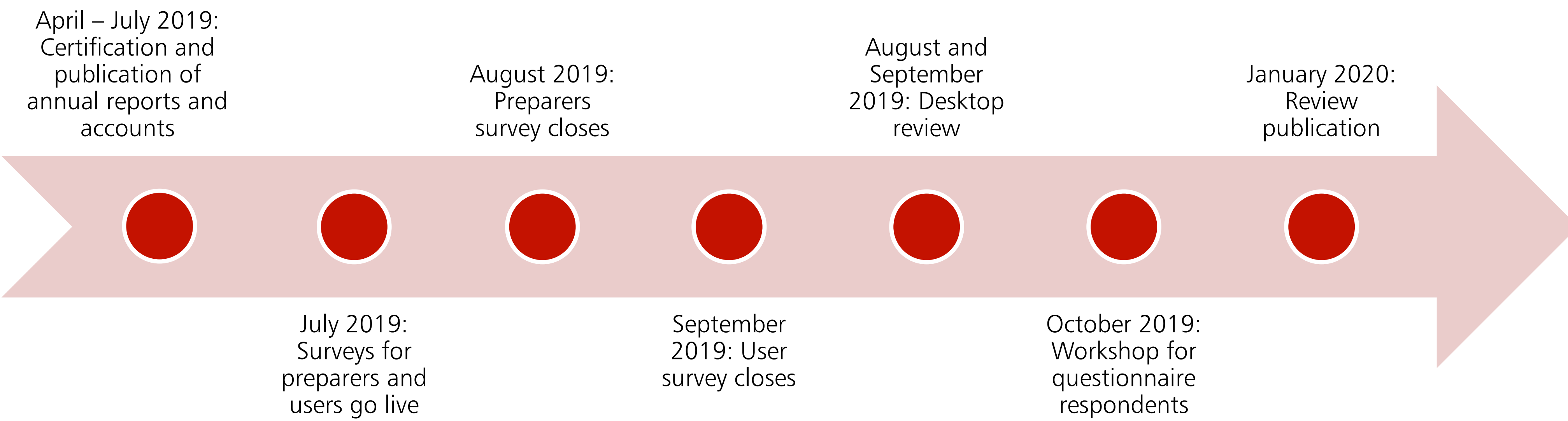
Strand 2:

Feedback from users and the desktop review undertaken by the Treasury looked at:

- the usefulness of disclosures on IFRS 9 and IFRS 15 in government annual reports and accounts

- The lessons learnt from this review will be applied to the implementation process for forthcoming new standards including IFRS 16 *Leases* and IFRS 17 *Insurance Contracts*

Overview
Timeline of the IFRS 9 & IFRS 15 thematic review



Strand 1
Preparers questionnaire and background

There was extensive stakeholder engagement throughout the four year IFRS 9 & IFRS 15 implementation process

- November 2014: initial analysis of the impact of the standards presented to FRAB
- 2015: Technical Working Groups for each standard are set up and meet multiple times
- October 2015: impact assessment is sent out to departments
- August 2016: exposure draft and public consultation are issued
- December 2017: application guidance for each standard is issued
- 2017 & 2018: various specific training on both standards is provided

Application guidance finalises any adaptations or interpretations of the reporting standard for the public sector

The preparers' questionnaire

- In 2019, the Treasury issued a questionnaire to annual reports and accounts preparers
- A total of 53 valid responses were received
- Annex A to this report gives a list of the questions asked

Areas covered by the questionnaire

- The timeliness of different parts of the implementation process
- Self-review for preparers and any further feedback for the Treasury
- Sufficiency of guidance and training
- Preparers' thought processes, and reference to users' perspective, in designing disclosures for the annual reports and accounts

Strand 1
Preparers' questionnaire feedback: timeliness

Financial guidance - feedback:

- Responses were similar for both IFRS 9 and IFRS 15 with the majority of respondents being in agreement with the timing of relevant materials produced by the Treasury
- 70% were satisfied with the timing of the impact assessment, and 80%, with the application guidance exposure drafts timing
- Around 60% of respondents were also very positive about the publication timetable (Dec 2017) for both application guidance and level of engagement on the timeline as a whole
- Around 30% of respondents reported the preference for earlier publication of both the IFRS 9 and the IFRS 15 application guidance, ideally before finance teams get busier preparing for year end
- Earlier publication of the application guidance, and the publication of an annually updated implementation timeline, would enable parent departments to support their arm's length bodies (ALBs) more effectively

What are knowledge networks?

Knowledge networks are platforms for sharing finance expertise across government and developing more standardised finance processes, built around best practice and the sharing of lessons learned. Examples include TACoE (Technical Accounting Centre of Excellence) and RASIG (Resource Accounts Special Interest Group)

Budgeting - feedback:

- The timing of the budgeting guidance for IFRS 9, which was published within the 2018-19 financial year, was found to be poor
- Explanations for the late change in the IFRS 9 budgeting guidance could have been communicated better with over half of the respondents indicating this communication was not satisfactory. Separate budgeting guidance for IFRS 15 was not needed
- Respondents also highlighted that this delay in publication of the budgeting guidance led to some duplication in work, for example when creating new codes in the finance system

What worked well for entities:

- ✓ Respondents suggested their own timeline for the implementation of both IFRS 9 and IFRS 15 had been sufficient
- ✓ Early engagement with the interpretations of the financial standards to understand the implications for the entity.
- ✓ Use of the knowledge networks that exist within government
- ✓ Comprehensive embedding of new financial standards into the underlying operations to make them business as usual
- ✓ Focus on project management and embedding the new practices into business as usual
- ✓ Early consultation with auditors to agree the treatment of relevant transactions and disclosures before the year end

Strand 1
Preparers' questionnaire feedback: guidance

Application guidance:

- The quality of the guidance was overwhelmingly well received and respondents agreed there was no need for any substantive changes on the guidance or the adaptations and interpretations for either IFRS 9 and IFRS 15
- Over 80% of respondents agreed there was effective alignment between the exposure draft, the application guidance and the FReM
- Positive responses were received on the usefulness and content of the application guidance – around 60% of respondents agreed that the information in the application guidance for both IFRS 9 and IFRS 15 was appropriate
- 70% agreed they could understand, and appropriately apply the central government specific interpretations and adaptations for both IFRS 9 and IFRS 15
- Respondents were on the whole satisfied with the amount of guidance relating to disclosure requirements. 70% of respondents were satisfied with the guidance for IFRS 9, which went up to 80% for IFRS 15
- However, written commentary suggested the application guidance could go further and include more public sector examples, some specific budgeting guidance or increased clarity in disclosure guidance

Training:

- The questions on training referred to both formal training, for example the sessions run by the Government Finance Academy, and the use of knowledge networks
- Training is important to ensure entities are supported and have the necessary capability for the successful implementation of new financial standards including their related disclosures
- Over 60% of respondents were satisfied with the training on offer for both IFRS 9 and IFRS 15
- However, some respondents were unaware of the training on offer or did not find it accessible which suggested the Treasury, in conjunction with relevant teams, could do more to increase the reach of its training

Why is alignment between the exposure draft, the application guidance, and the FReM important?

- The exposure draft sets out proposed adaptations and interpretations of a standard, as well as other aspects anticipated to be included in the application guidance for comment
- Unless communicated otherwise, central government entities would expect the application guidance to reflect the exposure draft
- The FReM also contains guidance for each adopted financial standard which must align with the information in the standard specific application guidance as central government entities must follow the mandatory guidance in both documents

Strand 1
Preparers' questionnaire feedback: disclosures

Disclosures and users of accounts:

- Entities are required to make certain disclosures in their financial statements to enable users to understand how the numbers have been calculated, including relevant decisions made by the organisation
- Central government entities have a wide range of users which can include both internal stakeholders, for example those in charge of governance, and external stakeholders, for example Parliament
- Different cohorts of users can have different needs and as such, may have a varying level of influence on the information disclosed in the annual report and accounts

Internal use of disclosures:

- Respondents were asked about the use of the IFRS 9 and IFRS 15 disclosures for internal decision making and by those in charge of governance
- Around half of respondents agreed the disclosures had been used, in some fashion, for internal decision making
- More entities around (65%) felt the disclosures had been used by those in charge of governance
- Where the information had not been used the following reasons were given:
  - More relevant information was available
  - More forward looking information was available
  - Due to how recently the information had been published, respondents were unable to know how the disclosures will be used internally

Influence of users on content of disclosures:

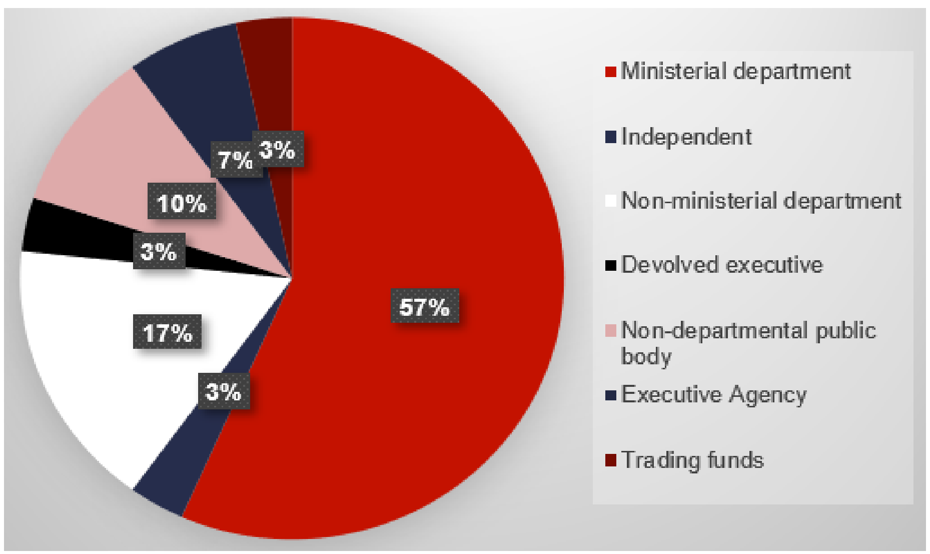
- Respondents were also asked how influential the needs of users had been when deciding on what and how to disclose
- Around 80% of respondents agreed the needs of the end user had influenced the disclosures included in annual reports and accounts for both IFRS 9 and IFRS 15
- However, only 30% of all respondents went further and agreed the needs of the end user had fundamentally shaped the information in their annual reports and accounts
- Written responses supported these statistics and highlighted that the focus had primarily been on compliance with disclosure requirements of each standard.
- However, once compliance was achieved, the needs of the end user did then have an influence on the content or type of language used

Strand 2
Users' questionnaire and the desktop review

Overview:

- The same aspects of the IFRS 9 and IFRS 15 disclosures within annual report and accounts were looked at for both the desktop review and user questionnaire
- These disclosures concern two distinct areas:
  - The clarity of explanation about the new standards in place
  - The specific application of the standards to an entity's accounts
- A final question looked at the overall ease for the user to understand the impact of the new standards

Desktop review sample:



Explanation of the new standards:

- This section reviewed how clear it was that two new standards had been implemented for the first time from 2018-19. This included:
  - Clarity that new standards had been implemented and from when
  - Clarity over what the new standards covered
  - Clarity on the impact of transition to the entity
  - Explanation of the interaction between IFRS 9 and IFRS 15

Specific application of the new standards:

- This section reviewed the clarity provided around how an entity had applied the principles contained in the standards to their specific situation. This included:
  - Explanation of the methodology chosen
  - Explanation given as to the concepts, judgements and conclusions made by the entity
  - Appropriateness of the disclosures

To find examples of good disclosures from the sample reviewed as part of the desktop review, look out for these blue boxes

Strand 2
Context: preparers explained the new standards

Why is this important?

- The 2018-19 annual reports and accounts were the first year IFRS 9 and IFRS 15 were implemented in central government
- In the first year of implementation, an entity should give detail on any new financial standards in their annual report and accounts
- Given the range of users of annual reports and accounts, many may not be aware of when new financial standards were implemented, or which elements of the balance sheet would be within scope.
- The 2018-19 annual reports and accounts provided entities the opportunity to explain to users:
  - IFRS 9 and IFRS 15 had been implemented
  - The effective date of implementation
  - What financial standards were being replaced
  - A summary of the new standards including newly introduced concepts and the impact of the new standards
  - The relationship between IFRS 9 and IFRS 15

Ministry of Housing, Communities and Local Government (2018-19 annual report and accounts, page 96):

IFRS 9 Financial Instruments was introduced by the International Accounting Standards Board (IASB) in July 2014, replacing IAS 39 Financial Instruments: recognition and management. In the current year, the department has applied IFRS 9 and the related consequential amendments to other IFRS Standards such as IFRS 7 Financial Instruments. The date of initial application is 1 April 2018.

Welsh Government (2018-19 annual report and accounts, page 89):

The group has applied the following accounting standards for the first time for the reporting period commencing 1 April 2018

IFRS 15 Revenue from contracts with customers
IFRS 15 introduces a new five stage model for the recognition of revenue from contracts with customers replacing the previous Standards IAS 11 Construction Contracts, IAS 18 Revenue and related IFRIC and SIC Interpretations.

The relationship between IFRS 9 and IFRS 15:

- As well as influencing other financial standards, IFRS 9 and IFRS 15 impact each other
- The accounting treatment for IFRS 15 could lead to assets that then have to be accounted for in accordance for IFRS 9
- For example, the recognition of a receivable from income recognised as per IFRS 15, would be in scope of IFRS 9

Strand 2
Findings: preparers' explanation of the new standards

Good practice:

- ✓ *Good examples* – There were a number of high quality examples of disclosures in the annual reports and accounts that gave a good overview of the content of the financial standards and the majority of entities referenced the new standards
- ✓ *The effective date* – This was explicitly mentioned in the majority of the sample but this was done more often for IFRS 9 than for IFRS 15
- ✓ *Strong IFRS 15 disclosures* – For IFRS 15, the majority of annual reports and accounts mentioned all the key elements and new concepts whereas for IFRS 9, it was common for entities to provide explanation solely on the concepts impacting their annual report and accounts.
- ✓ *Further commentary* – A few of the sampled annual reports and accounts had commentary on other financial standards that would be impacted by the introduction of IFRS 9, namely IFRS 7 and IAS 32
- ✓ *A clear relationship* – Where the relationship between IFRS 9 and IFRS 15 was mentioned, it was succinct and clear to understand.
- ✓ *Sensitivity to materiality* – Where entities disclosed that a standard did not have a material impact on the organisation, it was common for less information to be provided

Ministry of Justice (2018-19 annual report and accounts, page 162):

IFRS 9 replaces the IAS 39 'incurred loss' approach to impairment provisioning with a forward-looking 'expected loss' approach. Expected losses on the Department's financial assets are not considered to be material.

In accordance with IFRS 9 each financial asset is classified at initial recognition, or at the point of first adoption of IFRS 9, into one of three categories:

i. Financial assets at fair value through profit and loss ('FVP&L');
ii. Financial assets at fair value through other comprehensive income ('FVOCI'); or
iii. Financial assets at amortised cost;

For assets at amortised cost, the amortised cost balance was reduced where appropriate by an allowance for amounts which were considered to be impaired or uncollectible. Financial liabilities are classified into one of two categories:

iv. Financial liabilities at FVP&L; or
v. Financial liabilities at amortised cost

Foreign Commonwealth Office (2018-19 annual report and accounts, page 128):

Contract asset: the difference between the amount invoiced to the customer and the latest milestone achieved. Any accompanying receivable will be recognised if the customer has yet to pay the invoice. This balance will also include recognition of a receivable for costs which have been incurred to support milestones that have not yet been fully achieved. Any impairment relating to this balance will be measured, presented and disclosed in relation to IFRS 9.

Strand 2
Findings: preparers' explanations of the new standards

Areas for improvement:

- *Referencing the standards* – In the sample reviewed two annual reports and accounts did not mention IFRS 9 and another two did not mention IFRS 15
- *Existence of old standards* – It was not always clear that IFRS 9 and IFRS 15 were both replacing existing standards. It was common for an annual report and accounts to refer to the old standards for either IFRS 9 or IFRS 15 but not both.
- *Missing concepts* – In particular for IFRS 9, there were instances were some concepts were missed altogether, for example there was no mention of the new expected credit loss model
- *Ease of identifying information* – In some annual reports and accounts it was difficult to find the information provided on the new standards, effective date and old standards. In some instances, the references were missing, and in others the information was spread throughout the document with no summary given
- *Level of detail* – In some instance the level of detail provided in was either too much (with the content covering multiple pages) or too little. The amount of information should be sufficient to give users the understanding they need, without too much information overwhelming them
- *Relationships between standards* – The relationship between IFRS 9 and IFRS 15, as well as the linkages to other standards (for example IAS 8) was often not mentioned.

HM Treasury (2018-19 annual report and accounts, page 134):

IFRS 15 provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for performance obligations as they are satisfied. The standard requires revenue to be recognised at the point of control passing to the customer; over time or at a point in time. Furthermore, it requires an assessment to be undertaken for each performance obligation within the contract or service provided and this may impact the timing of when revenue is recognised.

The Group has assessed the impact of IFRS 15 using the five-step model framework defined in the standard and determined that there is no significant impact on the financial statements.

Variances in information:

- Throughout the review, variances in the quality and detail of disclosure information provided in respect of the two new financial standards were found
- Inconsistencies in disclosure clarity occurred within some individual entity's annual reports and accounts (i.e. the level of detail provided by the same entity on IFRS 9 and IFRS 15 was different)
- Inconsistencies were also identified between different entity's accounts (i.e. some entities provided more detail on the new concepts whereas others limited their explanation)

Strand 2
Context: transitioning to the new standards

? Why is this important?

- It is important for users of annual reports and accounts to know and understand the specific impact a new standard has on an organisation and its financial statements. This differs across organisations and can be significant.
- There were three main focuses when reviewing the disclosures on the impact of transition. Explanations were reviewed for:
  - Clarity about the transition method used and why
  - Clarity of the materiality of the impact of transition
  - Clarity of the reconciliation between the original opening balance and the restated opening balances (if relevant)

Mandating the transition method?

- Both standards allow two different methods of transition reporting – either to fully restate the prior years figures, or to only restate the appropriate opening balances with the cumulative effect shown in retained earnings
- For both, the FReM stated that the choice to retrospectively restate the previous years' figures had been withdrawn, and that entities should "recognise the difference between the previous carrying amount and the carrying amount at the beginning on the annual reporting period that includes the date of initial application" in the opening retained earnings (for IFRS 9) or within taxpayers equity (for IFRS 15)
- Whilst the FReM removes this choice on transition, users of the annual reports and accounts should expect to be able to use them as stand alone documents so disclosures of the transition method is appropriate

Cabinet Office (2018-19 annual report and accounts, page 70):

The Department conducted an impact assessment and upon adoption, a transitional adjustment has been made within the general fund in taxpayers' equity to recognise the difference between the carrying amount as reported at 31 March 2018 under IAS 18 and the opening balance as reported under IFRS 15. This is in accordance with IFRS 15 and FReM. Income was recognised earlier (at a point in time) in 2017-18 than it would have been under the new Standard (over time), and so a transitional adjustment has reduced the level of reserves brought forward into 2018-19; see Note 14.1.

Strand 2
Findings: impact of transition of the new standards

Good practice:

- ✓ *Explanation of transition method* – It was very easy to understand that entities were following the FReM-mandated transition method and what that method was
- ✓ *Materiality of impact* – In the majority of annual reports and accounts sampled, for both IFRS 9 and IFRS 15, it was clear whether the impact of the transition to the new standards had a material or an immaterial impact on the balance sheet (and therefore opening balances)
- ✓ *Reconciliations* – Where there was a material impact on transition, some entities did a full, clear and well explained reconciliation

Department for Culture, Media and Sport (2018-19 annual report and accounts, page 157-158):

Upon first time adoption of IFRS 15, the group has reclassified revenue to revenue from contracts with customers and current grant income the Statement of Comprehensive Net Expenditure

IFRS 15: Revenue from Contracts with Customers - Reclassifications

	31-Mar-18		Reclassifications		01-Apr-18	
	Core department £'000	Departmental group £'000	Core department £'000	Departmental group £'000	Core department £'000	Departmental group £'000
Income from sale of goods and services	(7)	(88,009)	7	88,009	-	-
Other operating income	(217,369)	(3,439,534)	88,123	468,904	(129,246)	(2,970,630)
Revenue from contracts with customers	-	-	(7)	(370,726)	(7)	(370,726)
Current grant income	-	-	(88,123)	(186,187)	(88,123)	(186,187)
	(217,376)	**(3,527,543)**	**-**	**-**	**(217,376)**	**(3,527,543)**

IFRS 15: Revenue from Contracts with Customers - Transition Note – SoCNE

	As reported 2018-19		Adjustments made due to IFRS 15		SoCNE without adoption of IFRS 15	
	Core department £'000	Departmental group £'000	Core department £'000	Departmental group £'000	Core department £'000	Departmental group £'000
Income from Contracts with Customers	(38,080)	(605,747)	38,080	605,747	-	-
Current grant income	(91,092)	(196,254)	-	-	(91,092)	(196,254)
Other Operating Income	(27,263)	(2,519,856)	(38,080)	(605,747)	(65,343)	(3,125,603)
Total Operating Income	**(156,435)**	**(3,321,857)**	**-**	**-**	**(156,435)**	**(3,321,857)**

Areas for improvement:

- ➢ *Explanation of judgments* – It was not always clear why an entity had determined a financial standard did or did not have a material impact
- ➢ *Clarity of impact* – Some entities mentioned there was a material impact of a financial standard but only provided vague explanations as to what this meant for the entity and the financial statements
- ➢ *Inconsistencies of information* – There were examples where the explanations about the impact of transition varied within an annual report and accounts i.e. much clearer information was provided for either IFRS 9 or IFRS 15 only

Strand 2
Context: choosing a methodology within the standards

? Why is this important?

- Both IFRS 9 and IFRS 15 involve different methodologies for treating the transactions within scope of the respective standard
- For example, IFRS 9 has three different measurement categories for financial instruments and IFRS 15 has criteria to determine whether income should be recognised over time or at a point in time
- It is important that a user can understand how an entity has applied IFRS 9 and IFRS 15 to their specific circumstances

Department for Health and Social Care (2018-19 annual report and accounts, page 153):

Per the provisions of IFRS 9, the Department has elected to irrevocably designate its equity instruments to be measured at fair value through other comprehensive income. The Department's equity instruments relates to its investment in private limited companies as detailed in note 11. The election ensures that an accounting treatment consistent with prior financial years is maintained under transition to IFRS 9.

Department for Business, Energy & industrial Strategy (2018-19 annual report and accounts, page 126):

The Departmental Group's accounting policies on the classification of financial instruments under IFRS 9 are set out in note 1.20. The application of these policies resulted in the reclassifications … explained below:

- Cash and cash equivalents, receivables, loans to public sector bodies, and term deposits that were classified as 'loans and receivables' and 'held to maturity' are now measured at 'amortised cost'. There are no changes in terms of measurement for these assets upon transition.
- Loans to private sector entities that were classified as 'loans and receivables' under IAS 39 meet the solely payments of principal and interest test for cash flows characteristics. The objective of the business model is achieved by collecting the contractual cash flows only and therefore, they are classified as 'amortised cost' under IFRS 9. An adjustment for the impairment allowance of £2 million calculated under the ECL model was recognised in retained earnings at 1 April 2018.
- Bonds were classified as 'available for sale' and are now measured at 'amortised cost'. The Group's intention is to hold these bonds for collecting contractual cash flows only. Sale of the bonds only happens infrequently when there is an increase in the assets' credit risk. Their cash flows are solely payments of principal and interest. Upon transition, the cumulative gain previously recognised in OCI was removed from equity and applied against the fair value of the financial asset at the reclassification date resulting in an adjustment of £1 million to retained earnings and carrying amount of the asset at 1 April 2018.

Strand 2
Findings: methodology chosen within the standards

Good practice:

- ✓ *Quality explanations* – There were a number of high quality examples of explanations around the methodologies chosen
- ✓ *Adapting to fit* – Explanations differed across organisations, demonstrating that preparers were relating the disclosures to their specific scenarios and not following a set template
- ✓ *Summaries* – For IFRS 15, good disclosures included a summary of each material category of income, and whether the performance obligation was satisfied over time or at a point in time and whether this impacted the recognition point of the income and why (or why not).
- ✓ *Detail on impact* – For IFRS 9, some of the best examples for financial instruments explained whether a change was one of terminology or had a financial impact along with why the measurement category had been chosen
- ✓ *A new model* – There were also some clear explanations as to the impact of the forward-looking expected credit loss model had on the annual report and accounts, although this was less well explained that the changes in measurement category

Home Office (2018-19 annual report and accounts, page 129):

The table below sets out, for each income stream, when performance obligations are typically satisfied, the significant payment terms, and the nature of the goods or services which the Department supplies. All income streams usually have a contract of a duration of one year or less, and therefore transaction price allocated to remaining performance obligations is not disclosed, applying the practical expedient in IFRS 15.121.

Income stream	Description of income stream	Performance obligation	Payment terms
Passport fees	Supply of passports and other services by HM Passport Office	On delivery of the passport to the customer.	Payment in advance
Visa and immigration fees	Supply of visas and immigration documents	On delivery of the visa or immigration decision to the customer.	Payment in advance
Asset recovery income	Recovery of proceeds of crime	The powers for the Home Office to recover this income is set out in legislation. Income is recognised when a court order is issued.	Penalty payment by court order
Certificate services	Supply of copies of birth, marriage and death certificates	Delivery of the certificate to the customer	Payment in advance
DBS income	Supply of criminal records checks by the Disclosure and Barring Service	Delivery of the information to the customer	Payment in advance
EU income	Grants from the Asylum, Migration and Integration Fund (AMIF)	Work done to meet the criteria for grant payment.	Payment in arrears on satisfaction of grant obligations
Hendon Data Centre Income	Supply of IT services to police forces.	The supply of IT services over time.	Payment quarterly in accordance with the agreement

Areas for improvement:

- ➢ *Clarity of explanations* – In some instances it was not clear how or why a measurement category had been chosen. This was especially common for explanations for irrevocable designations as per IFRS 9
- ➢ *Be specific not generic* – Some of the annual reports and accounts gave generic explanations as to the methodology options, without then relating these to the entities specific financial instruments

Strand 2
Context: concepts, judgements and conclusions

Why is this important?

- The disclosures in annual reports and accounts enable an organisation to explain the specific decisions made that impact on the financial statements
- Both IFRS 9 and IFRS 15 have principles in them which require judgements on the measurement of assets, liabilities, revenue or expenditure
- For IFRS 9 there are criteria that set out how financial asset should be measured. The entity will need to determine whether their financial assets meet these criteria
- For IFRS 15, an entity will use judgement to decide the income recognition points for each contract they have
- Therefore, it is important for a user to be able to understand these decisions. There were three interlinked aspects that were reviewed as part of this:
    - Were the concepts and their impact on the accounts explained?
    - Were the judgement and their impact on the accounts explained?
    - Were the conclusions and their impact on the accounts explained?

Department of Environment, Food & Rural Affairs (2018-19 annual report and accounts, page 125):

Significant Estimates and Judgements
Satisfaction of performance obligations

The key area of judgement for most entities is around the timing of revenue recognition for sales of services … Defra satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

- The entity's performance does not create an asset with an alternate use to Defra, and Defra has as an enforceable right to payment for performance completed to date. Defra's scientific projects are commissioned with a view to providing evidence and furthering research, and are not of direct use or relevance to another customer. In many cases, there is a right to payment for performance to date, in the event of contract cancellation.
- The entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced. This is relevant, for example, for partnership funding arrangements at EA, with income recognised on progress on the construction of the asset.
- The customer simultaneously receives and consumes the benefits provided by Defra's performance as it performs.

For performance obligations where one of the above conditions are not met, revenue is recognised at the point in time at which the performance obligation is satisfied.

Strand 2
Findings: concepts, judgements and conclusions

Good practice:

- ✓ *Good examples* – Both the desktop review and responses from the users' questionnaire agreed there were high quality examples of good explanations of the concepts, judgements and conclusions within central government annual reports and accounts
- ✓ *Impact on financial statements* – These clear explanations enabled a user to easily understand the impact of both financial standards on the annual report and accounts and where an entity had had to make a decision based on the criteria set out in the respective financial standard
- ✓ *Impact on conclusions* – It was also possible to understand the impact the concepts and judgements had on the conclusions made
- ✓ *Strongest on concepts and conclusions* – It was also common for the concepts and the conclusions to be more thoroughly explained than the judgement

Areas for improvement:

- ➢ *Clarity of explanations* – In some instances it was not clear what the concepts, judgement and conclusions were, and the numbers in the financial statements were left to stand alone with more generic supporting detail
- ➢ *Consistency of disclosures* – It was common for the annual report and accounts to include more detailed explanations as to the concepts and conclusions with little or no detail provided on the judgements made
- ➢ *Understanding the thought process* – In some instances there were conclusions that were given but it was unclear as to how these conclusions had come about, and therefore this information, whilst detailed, did not aid the understanding of the annual report and accounts as it came with no context

Department for Education (2018-19 annual report and accounts, page 126):

One area of potential judgement associated with adoption of IFRS 15 has been removed through FReM's adaptation to IFRS 15. The adaptation brings into scope for IFRS 15 all revenue received by departments other than tax surrenderable to the Consolidated Fund or covered by other standards. Consequently, revenue recognised by the Department, other than that recognised under other standards such as IAS 17, IAS 20 or IFRS 4 Insurance Contracts (IFRS 4) is within the scope of IFRS 15.

Management has applied judgement in two main areas:

- to identify performance obligations across IFRS 15 income streams
- to assess how the obligations have been satisfied; at a point in time or across a period of time

Strand 2
Context: overall appropriateness of disclosures

Why is this important?

- Disclosures are a key way for an organisation to support the users of annual reports and accounts understanding of the financial information provided. Examples include providing trend data and explaining changes to prior year data
- However, it is also important that only relevant information is provided in the disclosures, and not information that clutters the accounts
- With this in mind, the review considered the supplementary disclosures in the annual reports and accounts and the ease of understanding the impact of financial standards as a whole
- This holistic view was an important part of the review as it considers how simple it would be for a user to understand the overall impact of both IFRS 9 and IFRS 15 and reflects that users do not look at each aspect of a disclosure in isolation

Disclosure requirements

- Within financial standards, the IASB sets out the minimum disclosure requirements which entities must follow
- In central government, an entity must also follow the additional disclosure requirements set out in the FReM
- Organisations have some flexibility on how to present this information and on what additional information they disclose above the minimum requirements, based on their unique circumstances and what they think will be useful to those who use their annual reports and accounts

Competition and Market Authority (2018-19 annual report and accounts, page 106-107):

IFRS 15 'Revenue from Contracts with Customers' was introduced in the public sector in 2018/19. All income is recognised when the service is provided or when a legal decision has been determined. Income recognised consists principally of:

- regulatory appeals;
- recoveries of accommodation expenditure; and
- appeal costs reimbursed (relating to recovered legal costs) and other income.

Regulatory appeals
… From a CMA perspective, the 5-step model framework does not change the revenue recognition point for Regulatory Appeals. Regulatory Appeals income is recognised when an appeal has been considered by the CMA (service provided) and a decision made.

Recoveries of accommodation expenditure
… There is no change to the recognition of this income due to the implementation of IFRS 15.

Appeal costs reimbursed and other income
On the basis of materiality, the CMA has not assessed the impact of IFRS 15 on this category of income and therefore there is no change to the recognition of this income due to the implementation of IFRS 15.

Strand 2
Findings: overall appropriateness of disclosures

Good practice:

- ✓ *Understandability* – It was possible to understand the impact of both IFRS 9 and IFRS 15 on the annual report and accounts
- ✓ *Presence of supplementary disclosures* – Most entities had supplementary disclosures for both financial standards and where there were not, most entities provided an explanation why not
- ✓ *Materiality* – The clarity around the materiality disclosures gave a user an obvious steer as to whether to expect detailed further disclosures in respect of the new financial standard. The best examples made it clear that no assets, liabilities or transactions were in scope
- ✓ *Content of supplementary disclosures* – Where there were supplementary disclosures, high quality examples clearly related the information from IFRS 9 or IFRS 15, to the annual report and accounts and the information was methodically presented
- ✓ *Resilient reporting* – Where entities had missed information or given basic explanations for an area of disclosure, this often did not have a significant impact on the overall understandability of IFRS 9 and IFRS 15

Valuation Tribunal Service (2018-19 annual report and accounts, page 45):

IFRS 15 Revenue from contracts with customers

The standard establishes the principles that an entity shall apply to report useful information about the nature, amount, timing and uncertainty of revenue and cashflows arising from a contract with customers. The VTS is unaffected by the introduction of IFRS 15 a it earns no material income. The fees received by the VTS for appeals lodged on the 2017 ratings list (see Note 1.16) are remitted to the Consolidated Fund, and therefore do not form part of the VTS's own financial statements.

Areas for improvement:

- ➢ *Clarity of explanations* – In some instances it was not clear why there were no disclosures or what the impact of the financial standards were
- ➢ *Sufficiency of explanations* – In some annual reports and accounts the information provided in the disclosures could have gone further to give a fuller explanation. Missing information did affect the ability to fully understand the impact of IFRS 9 and IFRS 15 on the entity
- ➢ *Specific disclosures* – Some entities provided generic disclosures, making it harder to understand the impact of IFRS 9 or IFRS 15 to the financials. Some disclosures made it clear the new financial standard had an impact but not what that impact would be
- ➢ *Coherence* – In some annual reports and accounts the information in the disclosures was not cross-referenced or did not follow a logical path. This made it difficult to relate some of the revised concepts disclosed in the annual reports and accounts to the new standards, or to easily follow through the disclosures in the annual reports and accounts

Strands 1 & 2
Summary of findings and conclusions

Overall findings:

- ✓ *Positive response to implementation plan* – The feedback from the preparers' questionnaire gave positive responses for both the timing and content of the Treasury implementation process and associated guidance
- ✓ *No new adaptations needed* – Neither the questionnaires nor the desktop review found any need for further amendments to the existing adaptations and interpretations for IFRS 9 or IFRS
- ✓ *The implementation plan was effective* – This review suggests that the implementation process led by the Treasury was effective for implementation of IFRS 9 and IFRS 15 in central government
- ✓ *Improvements can be made* – This review has identified areas where improvements to the implementation plans for new standards can be made which are set out in the next steps
- ✓ *Limited focus on organisations' plans* – Organisations' individual implementation plans were not looked at as part of this review

Treasury engagement with users of annual reports and accounts:

- Despite actively reaching out to users, it was disappointing that the Treasury was unable to engage a wide range of users in this thematic review
- The creation of the new users / preparers group should mean in the future, the Treasury will be working with a broader group of users which should encourage more engagement in thematic reviews

Areas for improvement or review:

- ➢ *Earlier publication of the application guidance* – Preparers indicated that earlier publication of the application guidance would have enabled more opportunity to review it before the year end preparation process
- ➢ *Budgeting guidance* – Where relevant additional budgeting guidance would benefit preparers of annual reports and accounts
- ➢ *Communication of a forward plan* – Key features of the implementation timeline was not fully understood by all
- ➢ *More disclosure guidance* – Access to more guidance and examples relating to disclosures would have been beneficial to preparers of annual reports and accounts, especially in the first year of implementation
- ➢ *External guidance and the NAO* – Entities used multiple sources of guidance for the implementation of the new standards. The NAO played a vital role, working with entities to ensure compliance with the new standards
- ➢ *Training on offer* – Positive feedback was received on the content of training but access to training was highlighted by some preparers as an issue
- ➢ *Early engagement* – Preparers suggested some areas of best practice and areas for improvement within their own entities which focus around the early engagement with the implementation plan

Strands 1 & 2
More detail and next steps

Earlier publication of the application guidance

- Entities should begin implementation of new financial standards once published by the IASB and not wait for more detail to be provided by the Treasury
- It is important that the Treasury's application guidance is published with enough time to allow entities time to review and implement the guidance
- Earlier publication would also allow parent departments more time to support their arm's length bodies and share guidance

- ➢ The Treasury will aim to publish final application guidance for new standards by the autumn of the year preceding implementation.
- ➢ Early engagement with preparers is a key part of the implementation plan so the Treasury will
    - ➢ Continue to give early sight of application guidance through the exposure draft process
    - ➢ Incorporate advance notice of publication of application guidance into the communication strategy so that entities can incorporate this into their individual implementation plans
    - ➢ Effectively and quickly communicate any changes to interpretations and adaptations

More budgeting guidance

- For central government entities, budgeting is a key element of implementing new financial reporting requirements
- Whilst the Treasury aims to issue relevant budgeting guidance as early as possible, the publication of final budgeting guidance for IFRS9 was delayed which caused difficulty for some preparers

- ➢ Departments should continue to engage with their respective Treasury spending teams early to discuss the impact of new financial standards on the departmental budget
- ➢ The Treasury agrees that early sight of budgeting guidance is beneficial. As such, the budgeting guidance for IFRS 16 was published in July 2019. The Treasury also worked closely with those early adopting to give them sight of the expected guidance
- ➢ Any necessary amendments to budgeting guidance will be effectively communicated to stakeholders
- ➢ The Treasury will assess whether separate budgeting guidance will be issued. This decision will be based on the requirements of a new financial standard (as was the case with IFRS 16)

Strands 1 & 2
More detail and next steps

Communicating a forward plan

- Key features of the implementation timeline were not fully understood by all preparers even though the timetable was discussed multiple times and was accessible via the FRAB papers published on gov.uk
- Feedback suggests a 12 month forward look timeline would be useful to facilitate department's communication plan with its ALBs, which is an important relationship the Treasury is keen to support

- ➢ For IFRS 16, the Treasury has already implemented the 'lessons learnt'; and published an implementation timeline for both the 2019-20 and 2020-21 financial years which included some key milestones
- ➢ The Treasury will publish a timetable in 2020 setting out the anticipated key dates in 2020-22 for IFRS 17 (and any future standards) and will promote this widely to encourage early engagement

More disclosure guidance

- Disclosures are important as they provide users with more context and understanding of the annual report and accounts
- Differences were found in the quality of disclosures for new financial standards in the annual report and accounts so organisations accessing more disclosure guidance would be beneficial
- The Treasury avoids setting out boiler plate language wherever possible as entities are encouraged to "tell their own story"

- ➢ The revised 20-21 FReM has made the importance of the user more prominent. Entities within the remit of the FReM will are strongly encouraged to engage with users wherever possible
- ➢ The Treasury will issue some practical support on the disclosures for future standards including IFRS 16 through the illustrative statements, supplemented by the sharing of the good examples in this report and online

External guidance and the NAO

- External guidance, the financial standards and Treasury guidance were used in tandem with each other which is encouraging to see
- Working with the NAO was key to effective implementation of the new standards
- External guidance and the NAO should play a fundamental role in implementing new standards including the review of significant judgements and estimations

- ➢ The Treasury will continue to encourage entities to have early engagement with their audit teams as agreement of key balances and processes of these new standards with the NAO is essential
- ➢ The Treasury will also continue to encourage entities to ensure early familiarity with new financial standards including consideration of relevant guidance

Strands 1 & 2
More detail and next steps

Training on offer

- Training is a very important tool to increase capability across the public sector, which in turn leads to better quality annual reports and accounts and disclosures.
- Where training was accessed, there was no issue raised on the quality of it. However, some entities were not aware of the training on offer or did not find it accessible.
- It could be beneficial for training to include a greater focus on the importance of useful and easy to understand disclosures for new standards.

➢ To support continuous improvement in the training on offer the Treasury will:

  - ➢ Work with the Government Finance Academy to continue to extend the provision of training
  - ➢ Review the current training on disclosures for new financial standards and see how this can be improved
  - ➢ Promote training opportunities more widely, encourage departments to make staff (both in their core departments and arm's length bodies) aware of training offers, and encourage them to engage

Early engagement

- Early engagement with the implementation process is encouraged and it was good to see that this was identified by preparers as useful
- Entities highlighted areas of improvement and areas of best practice identified during the implementation of these standards including early engagement with the financial standards and embedding them as business as usual.
- Engagement can be done through joining working groups, being part of the Resource Account Special Interest Group (RASIG), sharing best practice and common issues and responding promptly to different stages of the implementation plan

➢ The Treasury will continue to encourage entities to follow the best practice behaviour identified including

  - ➢ Using existing resources to support their implementation plan, for example TACoE
  - ➢ Early engagement with an entities audit team including raising any potential issues as early as possible (including with the Treasury where relevant)
  - ➢ Learning from best practice examples and suggestions for how disclosures can be improved that have been included in this review