

FRS 102 Periodic Review 2024

1. Introduction

The Financial Reporting Council (“FRC”) has made major revisions to sections of FRS 102, “The Financial Reporting Standard applicable in the UK and Republic of Ireland” as part of their “Periodic Review 2024”. Most of the amendments are effective for accounting periods beginning on or after 1 January 2026, with early application permitted provided that all amendments are applied together.

This factsheet provides a high level overview for UK finance teams, advisers, and other stakeholders of the most significant changes. This factsheet is designed to support preliminary impact assessment, initial application planning, and early discussions with stakeholders.

The revisions have three objectives:

- i. To increase alignment with international best practice where proportionate;
- ii. To enhance transparency through targeted disclosure improvements; and
- iii. To simplify application where possible.

2. Executive summary of the revisions

The following changes are expected to be the most significant, with those in pink expected to be most impactful, those in yellow having more limited impacts to reported numbers or specific disclosure effects:

| | |
|---|---|
| New 5 step model for revenue recognition | New on balance sheet model for lessee accounting |
| New disclosure requirements for small companies | New concepts and pervasive principles |
| Changes to some definitions of fair value | Supplier finance arrangements disclosure requirements |
| Financial instruments | Guidance on uncertain tax treatments |
| Enhanced guidance for business combinations | Corresponding guidance for specialised activities |

Since the revisions were announced, the new model for recognising revenue (Section 23 of FRS 102) and the requirements for lessee accounting (Section 20) have grabbed the most attention as these will have the biggest impacts on financial statements. As explained below, the changes to Section 23 apply a wholly new model for recognising revenue, while Section 20 as applied to lessees will bring most leased assets and their associated liabilities on to balance sheets.

Beyond these, there are substantive changes to concepts and materiality (Section 2), a new fair value framework (Section 2A), supplier finance disclosure requirements (Section 7), refined going-concern and judgement disclosures (Section 3), tighter options and added disclosures for financial instruments (Sections 11/12), enhanced guidance on business combinations (Section 19), and explicit requirements on how to treat uncertain tax treatments (Section 29).

There are also expanded mandatory disclosures for UK small entities that follow Section 1A of FRS 102. These expanded mandatory disclosures have the potential to significantly expand the disclosures within a set of small company financial statements.

3. Revenue from Contracts with Customers (Section 23)

FRS 102 now incorporates a new five-step approach for all contracts with customers which is broadly aligned with IFRS 15. This is an entirely rewritten section within FRS 102 with a new approach to revenue recognition that replaces the previous risks-and-rewards approach

The five steps :

The five steps are more prescriptive than the old section 23 and require more structured assessment of contract terms and more informative disclosure.

At a high level, the five steps involve:

- ✦ **Identifying contracts:** Entities must identify in scope contracts and apply the new requirements to those contracts
- ✦ **Identifying performance obligations:** Entities must determine distinct goods or services promised in contracts, and consider where those are closely related or independent of other goods or services in the contract.

Example – Identifying performance obligations

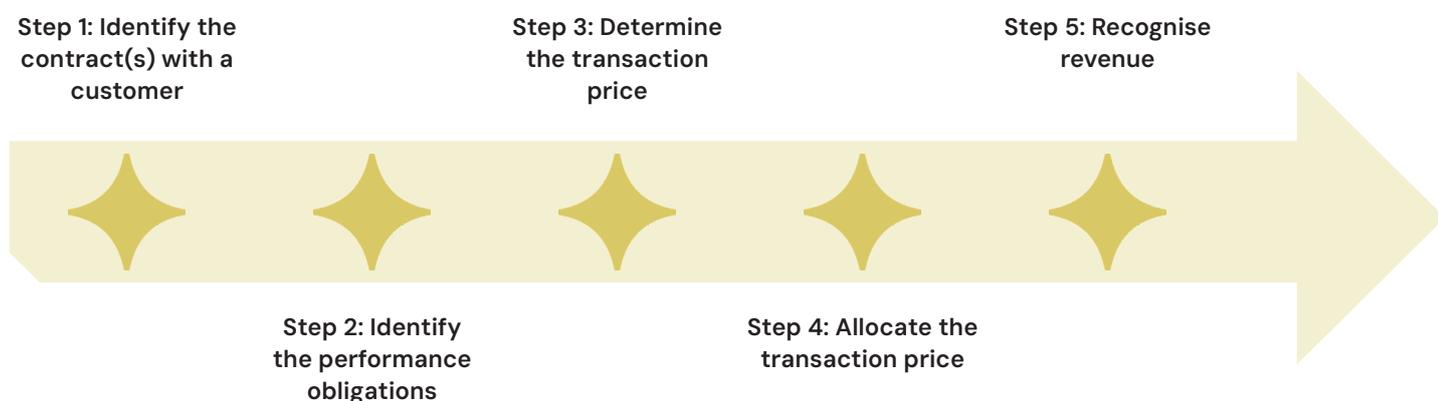
Up In The Air Software Limited (“Up In the Air”) sells a software product. A typical customer contract includes:

- ✦ A licence to use the software
- ✦ Initial set up and configuration services
- ✦ Ongoing customer support (help desk and updates) for a year

Up In the Air must assess which promised goods or services are distinct performance obligations.

In this case, the set-up and configuration do not provide a separate distinct benefit to the customer – the software cannot be used without the service. These services are bundled with the licence to form a single performance obligation.

The ongoing support is a separate service from which the customer benefits. It does not change or modify the software or impact on the configuration service. It is distinct from the licence and set up services.



- ✦ **Determining the transaction price:** Entities must determine the price included in the contract which will involve making assessments where there is variable or contingent consideration
- ✦ **Allocating the transaction price:** The total contract price is allocated to performance obligations based on their standalone selling prices

Example – Allocating the transaction price

Following on the previous example, Up In the Air has identified the following performance obligations:

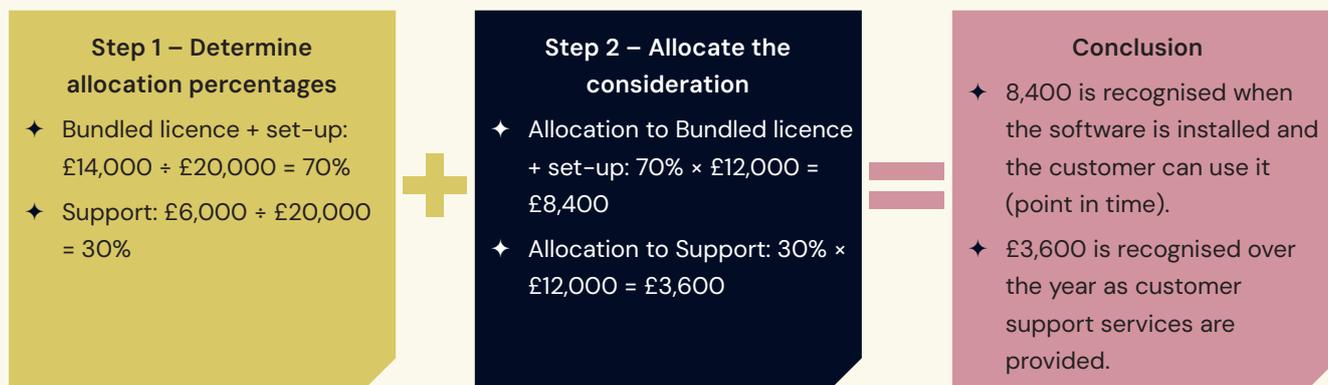
- ✦ Performance Obligation 1: A bundled obligation comprising the software licence and the initial set up and configuration services (not distinct).
- ✦ Performance Obligation 2: Ongoing customer support for one year (distinct).

Up In the Air charges a total transaction price of £12,000 for the combined contract.

The standalone selling prices (“SSPs”) of the components—if sold separately—are:

- ✦ Software licence (annual) – £10,000
- ✦ Set up and configuration – £4,000
- ✦ Ongoing support – £6,000

The total SSP is £20,000. Up In the Air must allocate the £12,000 transaction price across the performance obligations in proportion to their relative standalone selling prices.



- ✦ **Identifying how to recognise revenue:** Revenue is recognised either at a point in time or over time depending on when control transfers and how customers receive benefits.

The most significant changes in practice are expected where entities have complicating factors such as “bundled” offerings of products and services, variable consideration, extensive price concessions, significant financing components, warranties, options or principal–agent considerations.

The new Section 23 also provides more prescriptive and comprehensive guidance across various revenue areas including:

Licensing income classification: Licenses are categorised as rights to use intellectual property at a point in time or rights to access over a period, affecting whether revenue is recognised immediately or over time.

Contract modifications: Modifications changing scope or price may be treated as separate contracts if they add distinct goods or services at standalone prices; otherwise, they adjust the original contract’s revenue recognition.

Other enhanced guidance areas: The revised standard includes detailed guidance on principal versus agent roles, contract assets and liabilities, non-refundable upfront fees, customer options, contract costs, and disclosure requirements.

For initial application of the revenue changes entities may choose a full retrospective approach, where comparatives are restated or a modified retrospective approach under which comparatives are not restated and the cumulative effect is recognised in opening equity. Choosing the modified approach will require careful narrative to explain year-on-year movements and to prevent misinterpretation of trends by stakeholders.

4. Leases (Section 20)

The changes to Section 20 for leases are likely to have the greatest impact in terms of the number of entities affected as under the changes lessee accounting moves to a single on-balance-sheet model (Lessor accounting is largely unchanged). The distinction between operating and finance leases has been removed and, subject to limited exemptions (see below), leased assets and lease liabilities will be included on balance sheet, similar to the finance lease model under the existing standard. The intention of these changes is to provide enhanced and more transparent information for the users of financial statements by better reflecting the assets controlled by the entity and the related liabilities.

This change aligns with, but isn't identical to, the treatment of leases under IFRS 16 "Leases", the international accounting standard as FRS 102 includes some important simplifications and "practical expedients" designed to make initial recognition of the requirements simpler to apply.

The available exemptions from on balance sheet recognition are for short-term leases (less than one year) and leases of low-value assets. The FRC's approach to low-value assets is principles-based, with examples of items that would not qualify (such as vehicles and real estate), rather than a fixed monetary threshold.

Unless the exemptions explained apply, the new model requires lessees to recognise a Right-of-Use asset representing the leased assets they control and a corresponding lease liability for the financial commitment. The standard explains how lessees should apply the new requirements to new leases. These can be summarised in five stages:

Stage 1: Entities are required to assess whether a contract is or contains, a lease

Stage 3: Entities should consider if the leases are exempt

Stage 5: Entities calculate the Right-of-Use asset

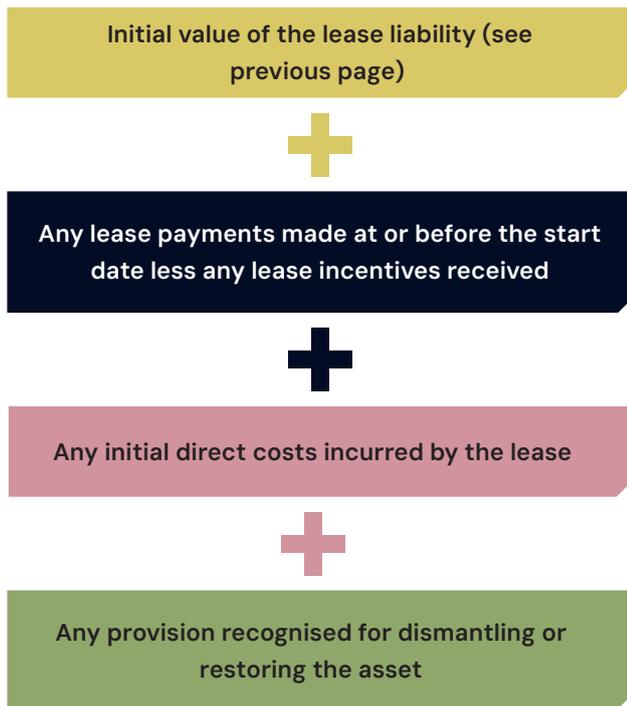
Stage 2: Entities should determine the lease term

Stage 4: Entities must measure the lease liability

At the start of the lease, a lessee is required to calculate the lease liability at the present value of:



At the start of the lease, lessees are required to measure the Right-of-Use asset at cost. Cost comprises:



The impact of the changes to Section 20, will of course be different for each entity, reflecting variables such as the nature of the industry, the type of assets leased, the detailed contract terms, the normal duration of lease contracts used, standard industry business practices, commercial and operational factors. Management teams will need to be aware of the potentially significant impacts of the new Section 20 on reported debt, profits, EBITDA and profitability and consider how those in turn affect the entity and its stakeholders.

Management must also consider the areas requiring judgement in the new section, including the requirements to determine the incremental borrowing rate (or other discount rate), identifying low value assets and assessing whether contracts include leases in scope of the new requirements.

Lessees are required to apply a “modified retrospective” approach on initial application of the new requirements. This means that a lessee must not restate its comparative figures and, instead, it recognises the cumulative effect of initially applying the amendments as an adjustment to the opening balance of retained earnings on the date of initial application (the beginning of the annual reporting period in which an entity first applies the amendments).

Under the modified retrospective approach, an entity measures its right-of-use assets and lease liabilities at the date of initial application. Under this approach comparatives are not restated with any cumulative effect of initial application of the amendments recognised as an adjustment to opening equity.

5. Small entities (Section 1A) – expanded mandatory disclosures for UK small companies

Following the UK’s exit from the EU, the UK is no longer subject to the “maximum harmonisation” principle of the EU Accounting Directive which prohibits member states from imposing additional presentation and disclosure requirements that were not required or allowed for in the Directive (the plan of the harmonisation principle was to keep financial reporting burdens on small companies to a minimum).

As part of the Periodic review, the FRC has taken the opportunity to add more disclosure requirements and mandated additional disclosures which it believes should be required by small entities in the UK for their financial statements to provide a true and fair view (these were generally encouraged but not mandatory previously).

The major and most impactful changes are:

Going concern

Previously a small entity was presumed to be a going concern and only if it departed from this principle, it was required to disclose this fact, the reasons for it and its effect. This presumption has been removed for UK small entities and FRS 102 now requires specific disclosure of the fact that the UK small entity's financial statements have been prepared on a going concern basis. The amendments make disclosure of any material uncertainties mandatory.

Related parties

The amendments change the related party disclosure requirements of Section 1A so disclosure is required of all related party transactions (subject to the exemptions applicable to all entities). Notably this removes the need for judgement in identifying those related party transactions that were not conducted under normal market conditions.

Provisions, contingent liabilities, contingent assets and financial guarantees

The amendments require small UK entities to make additional disclosures set out in Section 21 Provisions and Contingencies with the removal of the previous exemptions that only encouraged these disclosures.

Taxation disclosures

Section 1A now requires more granular information about tax, again more closely following the full FRS 102 approach. This will also see the inclusion of a tax charge reconciliation.

Share Based Payments

Small companies have recognised share based payment charges since FRS 102 was introduced. The revisions mean that the supporting disclosures are now required.

Dividends

Previously, it was not required for small companies to disclose dividends declared and paid or payable during the reporting period, however the revisions make this disclosure mandatory under the amended standard.

6. Concepts and Pervasive Principles (Section 2)

A less eye-catching example of FRS 102 aligning with IFRS is the introduction of the new Section 2 on concepts and principles which now reflects the IASB's Conceptual Framework for Financial Reporting, issued in 2018.

The purpose of Section 2 is to assist preparers in developing accounting policies for a transaction or balances that are not specifically addressed by FRS 102. The updated concepts and pervasive principles also provide a basis for future standard-setting and for the development of accounting policies for a transaction, other event or condition that is not currently addressed by the requirements of FRS 102.

When launching the revised FRS 102, the FRC stated that it does not expect the changes to Section 2 to lead to significant changes to existing practice. However, these changes crystallise how entities should develop accounting policies by providing stronger guidance in the area and strengthens the expectation that disclosures focus on decision-useful, entity-specific information rather than boilerplate text.

7. Fair value measurement (new Section 2A)

The changes have included the removal of the Appendix Fair Value Measurement to Section 2 and its replacement by a new Section 2A. This new section is intended to improve consistency and IFRS alignment in measuring fair value by aligning definitions and guidance with IFRS 13, which had replaced the international standard, IAS 39, that FRS 102 had been mostly consistent with.

The most important change in this section is an update to the definition of fair value. The most significant impact is for liabilities which involves a change in measurement basis to using the price that would be paid to transfer a liability, which differs from the previous approach that required measurement at the amount for which the liability could be settled. Additionally, the fair value of a liability must now reflect the effect of non-performance risk i.e., the risk that an entity will not fulfil an obligation. For example, adjustments for the entity's own credit risk may be required, with the consequence that the higher the entity's own credit risk, the lower the fair value of its liabilities will be.

This change is most likely to impact entities where a financial instrument (such as an interest rate swap or forward currency contract) is used. Depending on the valuation basis used by the counterparty (e.g. a bank), there may be a requirement to adjust the valuation if the valuation uses risk free rates as the new FRS 102 requires the calculation to take into account the entity's credit risk.

8. Supplier finance arrangements (Section 7)

Supplier finance arrangements (also called “supply chain finance” or “reverse factoring”) require new, aggregated disclosures for accounting periods beginning 1 January 2025 (this requirement applies a year earlier than the other amendments).

Entities which use supplier finance arrangements must describe key terms, disclose carrying amounts of liabilities within such arrangements, present ranges of payment due dates for both financed and comparable non-financed payables, and explain non-cash changes in the related liabilities. The aim is to illuminate effects on liquidity risk, working capital and cash flow presentation without being excessively disproportionate.

9. Financial instruments (Sections 11 and 12)

The old option to newly adopt IAS 39’s recognition and measurement is removed from the revised FRS 102 except where required for consistency of accounting policies within a group consistency.

Where entities adopt the IFRS 9 option, new explanatory disclosures are required about inputs, assumptions and estimation techniques for expected credit losses, including macroeconomic overlays and reconciliations of loss allowances.

10. Income taxes – uncertain tax treatments (Section 29)

FRS 102 now codifies how to reflect uncertainty over whether a tax authority will accept a tax treatment, based on the logic of the equivalent international guidance IFRIC 23.

Entities must evaluate whether acceptance by the tax authorities of the proposed tax treatment is probable. If not probable, the transactions or balances are measured using either the most likely amount or expected value, whichever better predicts the outcome. The guidance applies to both current and deferred tax, and estimates are updated for changes in facts and circumstances. Transition can be fully retrospective (without hindsight) or modified retrospective through equity at the date of initial application.

11. Business combinations and goodwill (Section 19)

There is new guidance to highlight the importance of applying judgement to determine whether a transaction that remunerates employees who are also vendors in a business combination is contingent consideration or remuneration for future services. The cost of a transaction that remunerates employees or former owners of the acquiree for future services is not part of the cost of a business combination.

Whether arrangements for contingent payments to employees or selling shareholders are contingent consideration in the business combination (and part of the consideration) or are separate transactions (e.g. remuneration for future services) depends on the nature of the arrangements.

Entities need to carefully consider the substance of the arrangement in order to determine what is part of the cost of the business combination. For example a common reason for such arrangements is that the acquirer would like to retain knowledge and expertise of key employees of the acquiree within the business after the acquisition. Where such an arrangement is initiated by the acquirer and is entered into as part of the negotiation of the acquisition, this may suggest that the substance of the arrangement is remuneration for services.

Additional disclosures are also introduced but FRS 102 retains differences from IFRS 3, including the absence of the concentration test and different outcomes for negative goodwill in some cases.



12. Specialised activities and other targeted revisions

Various amendments and clarifications have been made to Section 34 on Specialised Activities. These generally clarify existing requirements or reflect amendments made to other sections of FRS 102 as part of the Periodic Review 2024.

Key amendments include:

Additional guidance regarding what amounts should be included in the cost of a biological asset for agricultural activities;

Clarifications on the accounting treatment of service concession arrangements, to reflect the principles of IFRIC 12 Service Concession Arrangements, and new accounting requirements for revenue and leases (see further detail below);

Guidance on how to determine whether an asset is a heritage asset, measurement of such assets and related disclosures;

Clearer explanation of when incoming resources from non-exchange transactions should be recognised, and how they should be measured; and

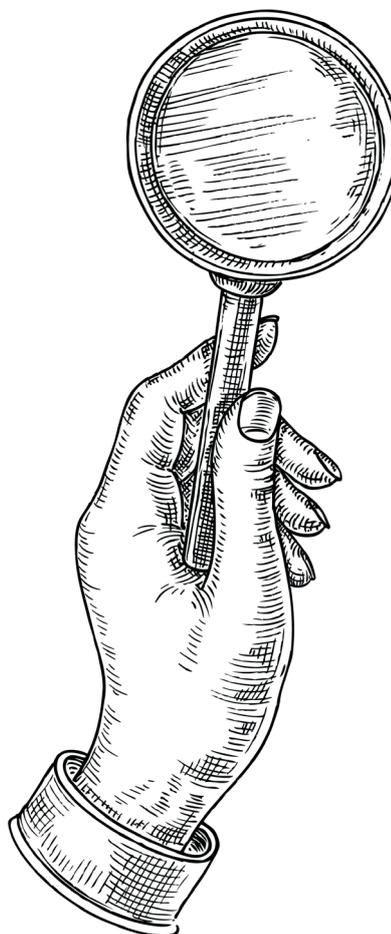
Other amendments to reflect changes to Section 2A Fair Value Measurement, Section 8 Notes to the Financial Statements, Section 20 Leases, Section 23 Revenue from Contracts with Customers and Section 11 Basic Financial Instruments.

13. Initial application

Initial application of revised FRS 102 is largely retrospective, with defined mandatory exceptions in some areas, optional exemptions in others, and specific transition requirements for revenue and leases. All transition adjustments are taken to opening equity at the date of initial application (being the beginning of the earliest period presented in which the revised requirements are applied)

Lessees are required to apply a “modified retrospective” approach on initial application of the new requirements. This means that a lessee must not restate its comparative figures and, instead, it recognises the cumulative effect of initially applying the amendments as an adjustment to the opening balance of retained earnings on the date of initial application (the beginning of the annual reporting period in which an entity first applies the amendments).

For initial application of the revenue changes entities may choose a full retrospective approach, where comparatives are restated or the modified retrospective approach under which comparatives are not restated and the cumulative effect is recognised in opening equity.



14. Impacts and implications

The impact of the changes to FRS 102, will of course vary by entity to entity, and sector to sector reflecting variables such as the nature of the sector or industry, business practices, commercial and operational factors.

However management teams will need to be aware of the potentially significant impacts of the changes on reported revenue, EBITDA, profitability, and net debt and consider how those in turn affect the entity and its stakeholders. Even where the end result is not a significant change in the reported figures, management will still need to have completed a process of assessing possible impacts, and demonstrating that fact for the entity's various stakeholders, particularly where the entity is also subject to external audit.

There are some practical steps to follow in order to prepare for the changes:

Sales Contract Review and Classification

- ◆ Review all contracts or standard contract types & map each revenue stream to the five-step model and identify bundled versus distinct obligations.
- ◆ Identify consideration, and assess and evaluate any complex terms including variable consideration, or contract modification terms.
- ◆ Consider any enforceable up-front fees and their impact.

Lease Contract Review and Classification

- ◆ Ensure listings of leases are complete and up to date.
- ◆ Review all arrangements for contracts that may include leases.
- ◆ Identify consideration, and assess and evaluate any complex terms including variable consideration, or contract modification terms..

Sales Systems and Processes

- ◆ Ensure systems track sales contract assets/ liabilities and the satisfaction of performance obligations.
- ◆ Align billing schedules with revenue recognition profiles.

Leases Systems and Processes

- ◆ Ensure details of new or revised leases are captured to ensure calculation of the RoU and liabilities.

Internal Reporting

- ◆ Consider and assess impact on revenue recognition and model the effects on performance measures such as EBITDA or Profit.
- ◆ Ensure that management accounts and other internal financial reports include the impact of the changes to revenue recognition and leases.

Internal Training & Governance

- ◆ Train finance teams on the new requirements
- ◆ Enhance controls over contract approval and modifications.

Policy Documentation

- ◆ Update accounting policies and disclose significant judgements and estimates in the annual financial statements.
- ◆ Document standalone selling price methodologies.

Communication with Stakeholders

- ◆ Explain expected changes in revenue patterns and KPIs to management, lenders, and investors.
- ◆ Consider impacts on financing covenants and remuneration metrics (including bonus and share based payment schemes) and discuss with relevant stakeholders.

Tax

- ◆ Consider the tax effects and discuss with your advisors where complex or material.

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