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Executive Summary

The Financial Reporting Council (FRC) has introduced major amendments to FRS 102, effective for accounting periods beginning on or after 1 January 2026, with early disclosure requirements for supplier finance arrangements required for periods commencing on or after from 1 January 2025.

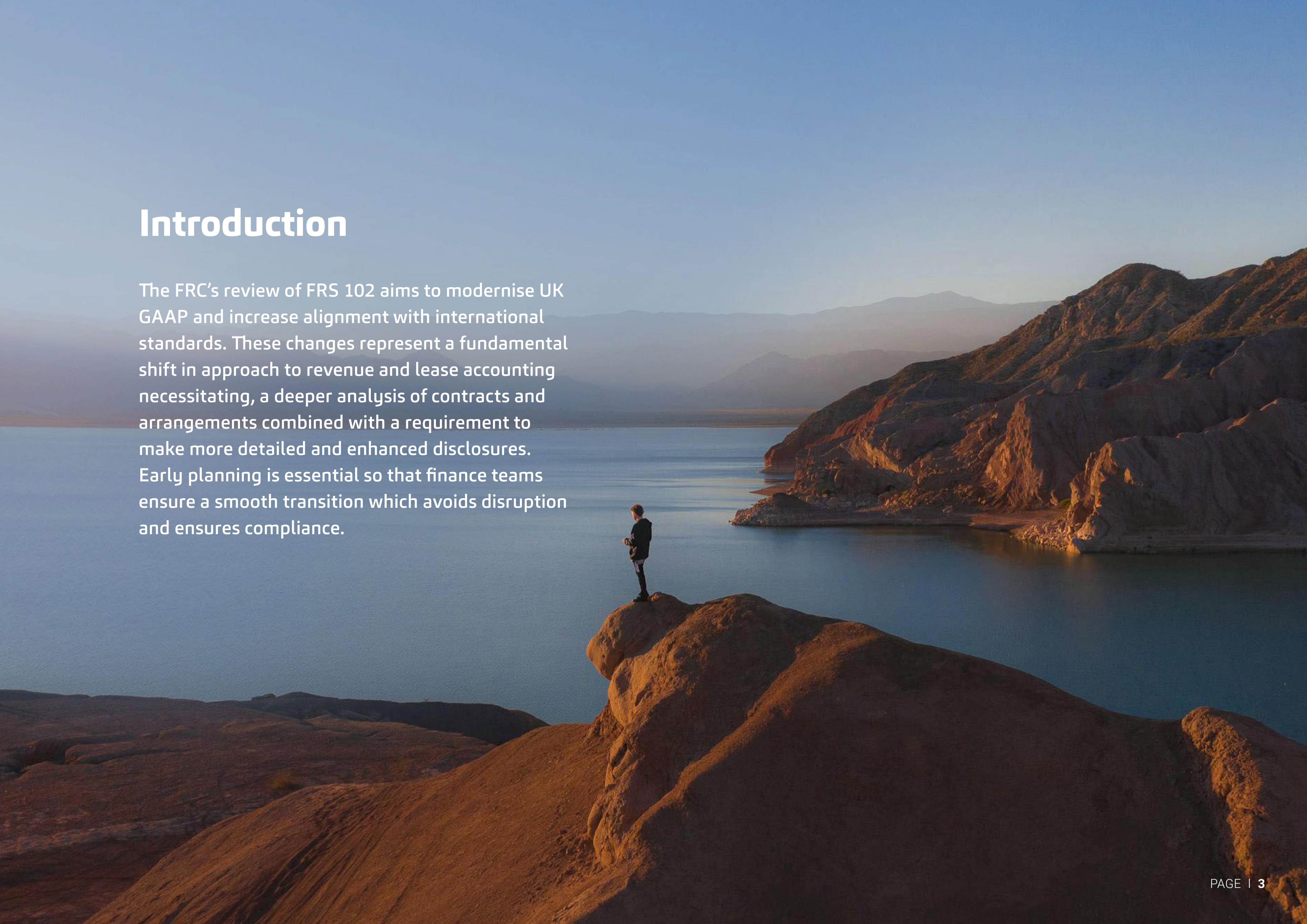
These changes align UK GAAP more closely with IFRS and will significantly impact revenue recognition, lease accounting, and other areas such as fair value measurent and the accounting treatment for uncertain tax positions.

Finance teams should:

- Understand the new five-step revenue recognition model and its practical implications
- Prepare for the changes to lease accounting which bring most leases onto the balance sheet
- Review any transition options available and plan for any necessary system and process updates
- Engage with stakeholders early and avoid common pitfalls such as underestimating the time and effort required regarding data capture.

Five step revenue recognition model

1. Identify the contract(s) with the customer
2. Identify separate performance obligations
3. Recognise revenue when or as an entity satisfies performance obligations
4. Allocate transaction price to performance obligations
5. Determine transaction price



Introduction

The FRC's review of FRS 102 aims to modernise UK GAAP and increase alignment with international standards. These changes represent a fundamental shift in approach to revenue and lease accounting necessitating, a deeper analysis of contracts and arrangements combined with a requirement to make more detailed and enhanced disclosures. Early planning is essential so that finance teams ensure a smooth transition which avoids disruption and ensures compliance.

Understanding the FRS 102 Transition Timeline

In terms of applying the changes to FRS 102 the transition requirements and reliefs available are designed to give businesses time to prepare, but first and foremost it is important to understand how the requirements will apply in practice.

The first milestone is 1 January 2025, when disclosure requirements for supplier finance arrangements come into effect for accounting periods commencing on or after that date. This early change is designed to improve transparency around such arrangements also known as reverse factoring, following a high-profile cases where such arrangements were not clearly reported.

The more significant amendments, covering revenue recognition, lease accounting, and all other changes become mandatory for accounting periods commencing on or after 1 January 2026. This means that entities should begin planning now, as these changes may impact systems, various processes, and as well as financial reporting.

When it comes to comparatives, the approach varies by topic. For leases, the standard requires a modified retrospective approach, meaning you do not restate prior-year figures but instead, recognise right-of-use assets and lease liabilities on the first day of the period of first implementation, with an adjustment to opening reserves.

For revenue, there is flexibility: in that an entity may choose to restate comparatives for consistency or apply a catch-up adjustment on the first day of the period of first implementation.

Other amendments have specific application rules. Fair value changes apply prospectively from the date of adoption, while uncertain tax positions are generally applied retrospectively unless hindsight is involved.

In short, the timeline is not just about dates, it reflects different transition methods for different areas. Understanding these nuances early will help you plan disclosures, manage stakeholder expectations, and avoid surprises during implementation.

Transition Requirements - FRS 102

Uncertain tax treatments – fully retrospective unless hindsight involved

Fair value amendments – prospectively from 1.1.2026

Other amendments – retrospectively

Comparative Period

Must **NOT** restate comparatives for leases. Catch up adjustment made on first day of current period.

MAY restate comparatives for revenue or make catch up adjustment on first day of current period.

1 January 2025

31 December 2025

1 January 2026

31 December 2026

Amendments to FRS 102 – Supplier Finance Arrangement disclosures

Amendments to FRS 102 – All other amendments to FRS 102

No requirement to disclose comparatives

Revenue from customer contracts

The revised standard introduces a five-step model based on the principles, contained in IFRS 15 Revenue from Contracts with Customers ("IFRS 15") moving away from transaction-based recognition principles to a contract-focused approach. This applies to all contracts with customers for goods and services, including construction, professional services, and software licensing.

Five-step model explained

1. **Identify the contract(s):** Confirm enforceable agreements, including master and side contracts. Ensure completeness of documentation and consider whether multiple agreements should be combined into one contract for accounting purposes or separated into distinct components.

2. **Identify separate performance obligations in the contract:** Break down promises into distinct goods or services. For example, a software license and ongoing maintenance and updates might be separate obligations if they are distinct.

3. **Determine the transaction price:** Assess fixed and variable forms of consideration, discounts, rebates, and contact penalties payable to the customer. Apply judgment to estimate the amount of variable consideration to recognise ensuring that it is 'highly probable' that there won't be a significant reversal of such amounts recognised in future periods.

4. **Allocate transaction price to performance contracts:** Allocate based on standalone selling prices. If these are not observable, estimate using market data, an approach based on expected cost-plus margin, or residual allocation approach.

5. **Recognise revenue when (or as) performance obligations are satisfied:** Decide whether control transfers at a point in time (e.g., delivery of goods) or over time (e.g., ongoing services). Apply input or output methods for 'over-time' recognition reflecting the stage of completion of performance obligations.

Key judgments and challenges

- Understanding and applying new terminology consistently across contracts
- Accounting for costs of obtaining and fulfilling contracts (e.g., sales commissions)
- Identifying distinct goods/services and dealing with enhanced guidance on accounting for contract modifications
- Assessing variable consideration and the recognition threshold
- Determining whether obligations are satisfied over time or at a point in time.

Disclosure Requirements

- Disaggregate revenue by product line, geography, customer type, timing, and whether acting as principal or agent
- Explain unsatisfied performance obligations and expected timing
- Disclose contract assets, liabilities, and impairment losses separately.

Lease Accounting

Overview

The new model brings most leases onto the balance sheet, removing the operating vs finance lease distinction for lessees. Exemptions apply for short-term leases (≤12 months duration with no purchase option) and leases of low-value underlying assets.

Right-of-Use Assets ("ROU") and Lease Liabilities

- **ROU Asset** measured as:Lease liability + prepaid lease payments – lease incentives received + initial direct costs + estimation of restoration/rehabilitation costs.
- Depreciate either over the shorter of the lease term or useful life, or useful life if ownership of the underlying asset is intended to transfer at the end of the lease.
- **Lease Liability** = present value of lease payments, discounted using:
  - Implicit rate (if readily determinable); otherwise
  - Incremental borrowing rate; or
  - Obtainable borrowing rate.

Lease accounting implementation plan

1. Focus on identifying leases (including arrangements containing leases), capturing existing lease data and review existing processes and systems in order to capture leases going forward.
2. Assess the lease population to determine which leases are outside of the scope or will be off balance sheet (low value, short term, variable).
3. Generate calculations and populate lease disclosures.
4. Do not reinvent the wheel every year so opt for a sustainable solution.
5. Embed the above processes to setup your ongoing lease management.

Key judgments

- Applying definition of lease term and assessing reasonable certainty of exercising extension and/or termination options
- Determine discount rate for each lease
- Identify variable lease payments (only index-linked or interest-based variable lease payments are included when calculating the lease liability).

Impact

- EBITDA improves as operating lease expenses are replaced by depreciation and interest charges
- Profit profile changes: higher costs in early years, lower costs in later years.

Disclosure

- Unless investment property present ROU assets and lease liabilities separately from other assets and liabilities either on face of balance sheet or in the notes.
- Detailed information such as nature of lease arrangements, restrictions and covenants imposed by leases, types of discount rate used and proportion of leases accounted for using each type of discount rate, extension and termination options, leases not yet commenced, variable lease payments.
- Provide reconciliation of movements in ROU assets.
- Disclosure also includes exemptions applied, variable payments expensed, expense for short term leases and leases of low value underlying asset, lease interest expense, sub-letting income, total cash out flows for lease payments.

Implementation:

Avoid reliance on complex spreadsheets for large lease portfolios - consider system solutions.

Other important changes

1. **Fair Value Definition:**
Updated to align with principlesdefinition of fair value to be consistent with IFRS 13 Fair Value Measurement.

2. **Uncertain Tax Positions:**
Entities must recognise and disclose uncertain income tax treatments where a settlement is probable by, applying either a probability-weighted approach (expected value of settlement) or a most likely approach (most likely settlement amount).

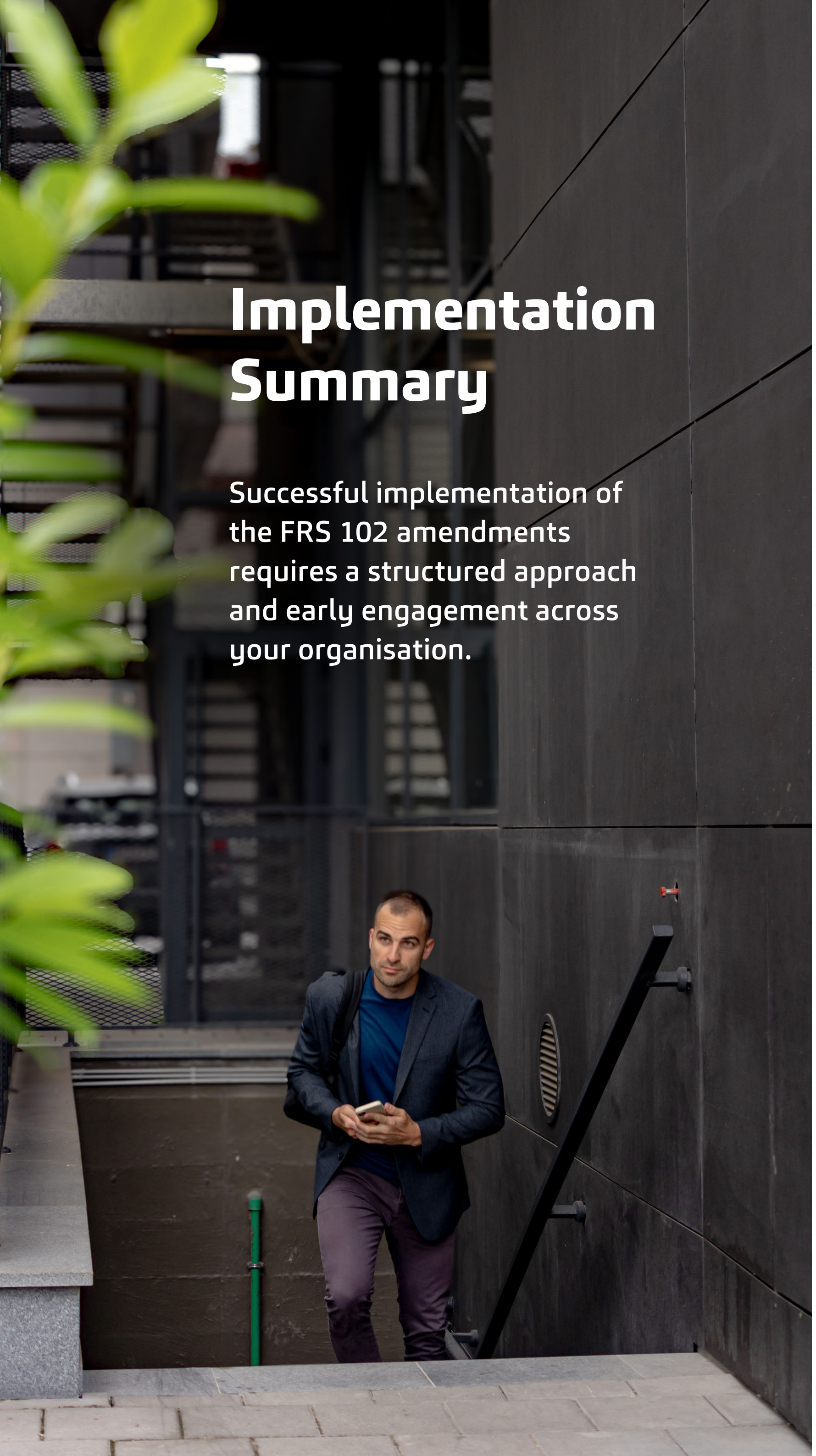
3. **Business Combinations:**
Various clarifications including whether amounts payable are consideration (affecting goodwill) or are instead remuneration for future services which are expensed separately.

4. **Increased disclosures for Small Entities applying Section 1A of FRS 102:**
Increase in level of disclosures required to show a true and fair view.

5. **Lessor Accounting**
While the operating lease vs finance lease model is retained for lessors new terminology introduced as well as in-depth guidance on accounting for sub-letting.

Some remaining differences between FRS 102 and IFRS 16

	IFRS 16	New FRS 102 requirements
Discount rate	In calculating the lease liability, IFRS 16 requires the use of the lessor's implicit interest rate if determinable. IFRS 16 permits the use of a lessee's incremental borrowing rate (IBR).	FRS 102 also requires the use of the lessor's implicit interest rate if that rate can be readily determined. However, it introduces an additional option for when that rate is not readily determinable. This rate is called the "obtainable borrowing rate" (OBR).
Discount rate applications when lease modifications arise	The lessee must use a revised discount rate for all lease modifications that are not considered separate/new leases.	FRS 102 introduces scenarios that allow a lessee to not update the discount rate. The three modification scenarios that permit a lessee to use an unchanged discount rate are: 1. the additional consideration from the lease modification is insignificant relative to the total consideration of the original lease; 2. the lease modification decreases the scope of the lease by removing the right to use one or more underlying assets, and the consideration for the lease decreases by an amount commensurate with the stand-alone price for the decrease in scope, or; 3. the lease modification decreases the consideration payable for the remaining term of the lease but does not decrease the scope of the lease by removing the right to use one or more underlying assets.
Low-value leases	Lessees reporting under IFRS 16 may choose to take advantage of an optional exemption forleases of low-value assets, which The Basis for Conclusions cited as leases for which the underlying asset's fair value is generally less than $5,000.	FRS 102 does not provide guidance around a specific threshold under which leases are exempt. However, it does provide flexibility for organisations to determine whether or not other assets are of low value for their own organisation.
Transition methods	a choice between the full retrospective approach, and the modified retrospective approach.	FRS 102 only allows for the modified retrospective approach. If an entity already has IFRS 16 balances for group/consolidated reporting purposes, they are permitted to use the existing carrying values as its opening balances of right-of-use assets and lease liabilities at the date of initial application to FRS 102.



Implementation Summary

Successful implementation of the FRS 102 amendments requires a structured approach and early engagement across your organisation.

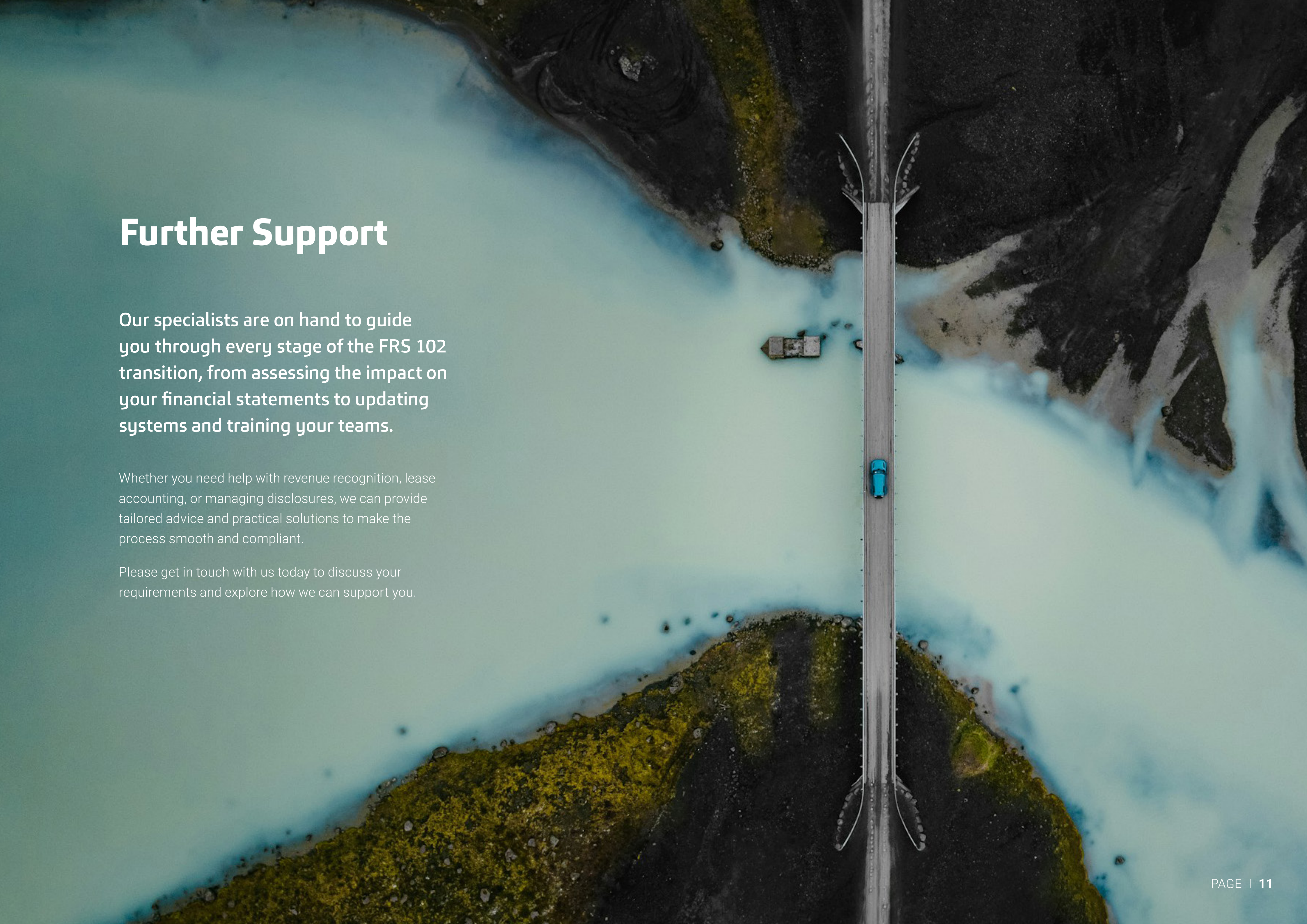
Below are the key steps and common risks to manage:

Key Actions

- **Confirm effective dates and scope** of all amendments to ensure compliance planning starts early.
- **Identify and collate all lease agreements and revenue contracts**, including any side agreements or contract modifications.
- **Decide transition methods** for revenue recognition, considering whether to restate comparatives or apply catch-up adjustments.
- **Quantify the impact** on bonus plans, distributable reserves, KPIs, and covenant calculations to inform relevant stakeholders.
- **Train finance teams and update systems** to handle new recognition and disclosure requirements.
- **Draft new disclosures early** to avoid last-minute issues and ensure audit readiness.
- **Engage stakeholders** such as auditors, lenders, and boards to manage covenant implications and expectations.

Common Pitfalls to Avoid

- **Underestimating data capture requirements,** especially for leases and complex revenue contracts.
- **Ignoring covenant and bonus plan implications**, which can affect financing and remuneration.
- **Delaying system updates**, leaving insufficient time for testing following implementation.
- **Treating implementation as a one-off project** rather than embedding ongoing compliance processes to ensure sustainable solutions and avoiding the need to re-invent the wheel.
- **Failing to involve procurement, legal, and operational teams**, which often hold critical contract and lease information.



Further Support

Our specialists are on hand to guide you through every stage of the FRS 102 transition, from assessing the impact on your financial statements to updating systems and training your teams.

Whether you need help with revenue recognition, lease accounting, or managing disclosures, we can provide tailored advice and practical solutions to make the process smooth and compliant.

Please get in touch with us today to discuss your requirements and explore how we can support you.

FAQs and Practical Scenarios

What are the key differences between FRS 102 and US GAAP for revenue and lease accounting for lessees?

FRS 102 amendments for revenue recognition are based on IFRS principles, which are broadly aligned with US GAAP for revenue recognition. Both frameworks use a five-step model for revenue. However, lease accounting differs: Under FRS 102, lessees recognise a right-of-use asset and lease liability, with depreciation and interest creating a ront-loaded expense profile.US GAAP uses a straight-line total expense approach, even when lease is on balance sheet, to avoid skewed costs.

Can we continue to use percentage-of-completion for revenue recognition?

Yes, you can continue to use percentage-of-completion methods for contracts that meet the criteria for revenue recognition over time. The revised standard allows input or output methods, provided they faithfully depict performance. More detailed guidance on the methods are included in the revised requirements.

Are 12-month vehicle leases exempt from balance sheet recognition?

Leases of 12 months or less qualify for exemption from balance sheet recognition, provided there are no extension options that the entity is reasonably certain to exercise.

What is deemed to be a 'low-value' underlying asset under FRS 102?

FRS 102 does not prescribe a fixed monetary threshold for low-value underlying assets. Instead, entities must apply judgment based on materiality and the nature of the asset. FRS 102 lists out assets that would not normally be considered to be of low value. The asset's value is considered at the inception of the lease whereas IFRS requires consideration of the value of an asset from the perspective of it being new.

Do salary sacrifice car leases need to be recognised on the balance sheet?

If the company is the lessee and controls the right to use the vehicle, the lease must be recognised on the balance sheet, even if costs are largely passed to employees. Such schemes will need to be evaluated in order to assess the correct accounting treatment.

Are supplier finance disclosures required for both parties?

Disclosure requirements apply to the entity providing the supplier finance facility, not the supplier benefiting from early payment.

What interest rate should we use for discounting lease liabilities?

If the rate implicit in the lease is not readily determinable, use the lessee's incremental borrowing rate. If no comparable borrowing exists, FRS 102 introduces the 'obtainable borrowing rate.'

Do cloud computing arrangements count as right-of-use assets?

Cloud computing arrangements typically represent a service rather than a lease where there is no specified identified asset controlled by the customer however such arrangements will require assessment.

Will finance leases still be capitalised under the new rules?

Under the revised model, all leases previously classified as finance leases will now be recognised as right-of-use assets with corresponding lease liabilities.

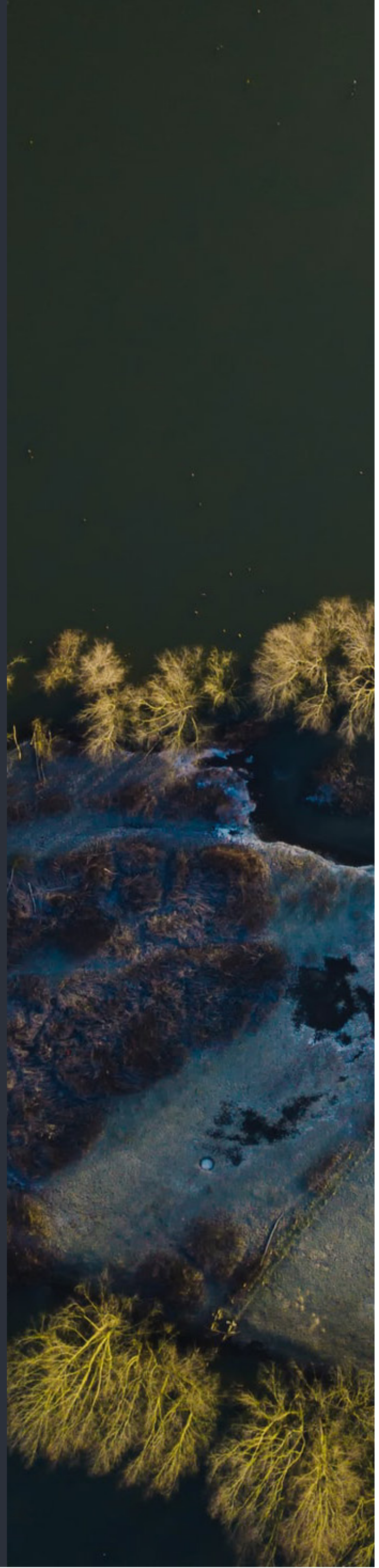
Do dilapidations or restoration costs need to be included in lease accounting?

Expected restoration or dilapidation costs at the end of a property lease must be included in the measurement of the right-of-use asset at inception, discounted to present value.

Can we use our existing IFRS 16 or management account models for FRS 102 implementation?

Yes, existing calculations currently applied where an entity provides information for group reporting of its leases under IFRS 16 can be used as the basis for the amounts of ROU assets and lease liability at date of transition. Where leases were previously recognised as finance leases those carrying amounts of asset and liability at date of transition may be applied (unless the IFRS 16 exemption previously discussed applies).

System Solutions for Lease Accounting



When managing a large portfolio of leases, relying on spreadsheets can quickly become inefficient and error-prone.

Spreadsheets often struggle with:

- Complex calculations for discounting and remeasurement.
- Handling multiple discount rates and lease modifications.
- Generating detailed disclosures required under FRS 102.

System solutions include:

1 Specialist Lease Accounting Software

- Tools like LeaseAccelerator, Nakisa Lease Administration, or Trullion are designed for compliance with IFRS 16 and FRS 102.
- Features include automated calculation of right-of-use assets and lease liabilities, handling modifications, and producing disclosure reports.

2 ERP Modules

- Many ERP systems (e.g., SAP, Oracle NetSuite, Microsoft Dynamics) offer integrated lease accounting modules.
- These modules link directly to your general ledger, reducing manual entries and improving accuracy.

3 Cloud-Based Platforms

- Solutions such as CoStar Real Estate Manager or Visual Lease provide cloud-based lease management with compliance reporting.
- Ideal for organisations with multiple locations or remote teams.

4 Mid-Tier Accounting Software Add-Ons

- For smaller entities, add-ons for platforms like Xero, QuickBooks, or Sage can provide simplified lease accounting functionality.

Benefits of system solutions:

- Automated calculations reduce human error.
- Built-in compliance checks for FRS 102 and IFRS 16.
- Scalable for growing lease portfolios.
- Streamlined reporting for auditors and stakeholders.

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