All change for accounting standards FRS 102

Effective: 1 January 2015

FRS102 is one of the biggest changes to UK medium and large company reporting for many years.

The first changes affect balance sheets prepared on or after 31 December 2013.
So now is the time to begin your preparations to convert to the new regime.

What is the change?

Early in 2013, the Financial Reporting Council issued three new accounting standards for medium and large companies and groups, replacing everything that has gone before. The intention is to make UK Generally Accepted Accounting Principles (UK GAAP) suitable and rigorous enough for modern businesses.

The three new standards are:

- FRS 100 – Application of Financial Reporting Requirements
- FRS 101 – Reduced Disclosure Framework
- FRS 102 – The Financial Reporting Standard applicable in the UK and Republic of Ireland

Although the standards are mandatory for all medium and large companies and groups, small companies and groups do not avoid changes as the Financial Reporting Standard for Smaller Entities (FRSSE) will undergo some revisions to bring it into line with the new standards.

Why the change?

In an increasingly global world, the new standards aim to improve reporting for modern transactions (including financial instruments), improve consistency with international accounting standards, and amend some areas of conflict with existing UK company law.

How the change affects you:

- Compliance with the new standards for all medium and large entities is mandatory
- Changes first affect accounting periods beginning on or after 1 January 2015 – but the transition rules require representation of balance sheets from 31 December 2013 onwards
- Amended presentation of the accounts, including extended disclosure requirements
- Alterations to tax computations and returns to reflect the new standards.

How we can help

Managing the change to the new accounting framework in-house could have a high impact on both your training requirements and the time of your staff. Garbutt & Elliott can help businesses to understand and apply the complexities associated with the accounting and financial reporting requirements, and aim to provide practical as well as technical advice.

Our expertise can assist you through this change by:

- Advice on the accounting changes relevant to you
- Assisting with accounting policy selections
- Considering the practical implications of the changes, such as how they could impact bank covenants, taxation, distributable reserves and credit ratings

Working with you to manage the transition process, starting now through to your first filing under the new standards, and beyond.

Our support will be tailored to your needs, from a high level overview on how the changes impact your business through to performing the full conversion on behalf of your company.

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A guide to the new accounting standards

Your account options

Which standard should I use?

Accounting options	Must be used by	Can be used by
Full International Financial Reporting Standards (IFRS)	Full listed groups, most commonly preparing consolidated accounts	Any other entity if they choose
FRS 101 – Reduced Disclosure Framework	Optional only	Subsidiaries of listed groups or other entities who have voluntarily adopted IFRS
FRS102 - The Finance Reporting Standard	Non-listed, large and medium sized companies and groups	Any other entity unless required to use IFRS
FRS 102 – Reduced Disclosure Framework	Optional only	Subsidiaries of non-listed large and medium groups
Financial Reporting Standard for Smaller Entities (FRSSE)	Optional only	Small companies and groups

In this guide we clarify the key accounting changes and highlight what we consider to be the key commercial and practical considerations.

Our forward thinking approach can help your company manage the change.

In the table above, 'companies' applies to all incorporated entities, including LLPs.

If you are unsure as to whether your company qualifies as small, medium or large, please contact us for clarification.

When is my implementation date?

The first set of accounts prepared will be for your first reporting period beginning on or after 1 January 2015; assuming a normal reporting year is used then the first FRS 102 accounts will be prepared for years ended 31 December 2015 and after.

Under these, the balance sheets at 31 December 2013 and 31 December 2014 will need to be restated to comply with the new standards, as will the profit and loss account for the year to 31 December 2014. Early adoption is permitted.

ACCOUNTS PREPARED	31/12/14	31/12/14	31/12/15
	31/03/14	31/03/15	31/03/16
REPORTED ACCOUNTS	Current rules	Current rules	FRS 102 accounts
102 IMPLICATIONS	Opening restatement	FRS 102 comparatives	Full FRS 102 accounts

Your implementation date depends on your year end; please contact us for confirmation of how the implementation date applies to you.

Please note that short accounting periods are likely to accelerate the switch and the new regime.

Key changes arising from the introduction of FRS102

Terminology

Some aspects of the accounts are renamed. These are reflected in brackets where relevant. The first visible change is to the names of the profit and loss account (now "Income Statement") and balance sheet (now "Statement of Financial Position"). There is also a new statement, the "Statement of Changes in Equity", which presents information previously disclosed in the notes to the accounts. The standard also introduces and relies heavily on "fair value". This can generally be interpreted as a market value.

Fixed assets (property, plant & equipment)

- Land and buildings are strictly separate assets and must be accounted for separately. This means that when buying a property, it is mandatory for the amount paid to be separated between the cost of the land and the cost of the buildings.
- There is a mandatory requirement to look for indicators of impairment to fixed assets at each year end. For example, changes in market conditions or exceptional deterioration in the state of the asset.
- Assets must also be reviewed on a "cash generating unit" basis where relevant, e.g. all machines producing a specific product would create a unit. The future profits of this unit must be considered in deciding whether that asset unit is excessively valued.
- Fixed assets can be carried at valuation/fair value, but the fair value must be reviewed each year.

Intangible assets

- Any software previously shown as a fixed asset must be reclassified as an intangible asset.
- Intangible assets must now be written off over five years, unless there is a solid demonstrable basis for another useful life.

Stock (inventories)

All stock lines must be reviewed for impairment at the balance sheet date.

Investment properties

An investment property is one kept for capital appreciation or for renting out, rather than for use in the business.

Properties with mixed use must be 'split' e.g. a 10 floor building with 6 floors used for business and 4 floors rented out would be 60% fixed asset and 40% investment property, giving rise to a significantly different accounting treatment.

All investment properties must now be valued at fair value, with any year on year changes being recognised in the profit and loss account.

Revaluation gains are not distributed, which means that retained profits will need to be analysed to identify cumulative profits and revaluation. This could affect a company's ability to pay dividends.

Key changes arising from the introduction of FRS102

Leases

- Assets bought under finance lease, which now includes hire purchase, must be valued at the lower of cost or 'fair value of the minimum lease payments'.
- Disclosure of operating leases is now more onerous, being total payments due on a lease rather than amounts to pay in the next year, as at present.

Revenue

- "Split" revenue streams must be accounted for separately, e.g. if an alarm is sold with a 3 year warranty, the accounts must reflect the fair value sales price of the alarm immediately, and the fair value sales price of the warranty spread over 3 years.
- Similarly, any customer loyalty schemes must separate revenue used for providing loyalty benefits and recognise the income as the benefits are used, e.g. buy 6 coffees get 1 free – then one seventh of each coffee's revenue is for the "free" coffee.

Government grants

- Entities now have a choice of how to account for government grants.
- The cost model recognises grant over its life (or life of the asset to which it relates); the performance model allows the entity to recognise the total grant income at the point of completion of the grant's performance conditions.

Employee benefits

- Employee costs must now be accounted for as the benefit is derived from those employees. For example entities must accrue staff costs where unused holiday entitlement exists at the year end.
- The cost of providing long term benefits, including long service awards, must be recognised over the period of employment prior to payment of the benefit.
- There are a number of adjustments to accounting treatment and disclosure for defined benefit principles, including clarification for group defined benefit plans.

Prior period errors

- An adjustment must now be made for any material prior period error. At present, only fundamental errors need to be revised. This means a higher likelihood of prior period adjustments.
- Any adjustment must include full disclosure of its nature and reason – even if there is no effect on profits or reserves.

Financial instruments

- Derivatives, forward contracts, interest rate swaps etc. can no longer be netted off.
- A derivative has to be recognised on the balance sheet at its fair value at the start date.
- The standard introduces a hierarchical system for measuring fair value.

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Key changes arising from the introduction of FRS102

Consolidations

- Goodwill on consolidation shall now be written off over 5 years - against 20 years at present.
- All assets in an acquired company must be valued at fair value, including any intangible assets such as brands.
- Deferred tax must be provided for on any consolidation differences.
- Non-owned special purpose entities may be required to be consolidated.
- Accounting for associates is revised.
- Exemptions are in place for historical business acquisitions, however the above is mandatory for any new acquisitions on or after the effective conversion date.

Specialist activities

- Agricultural produce must be valued at fair value at the balance sheet date – difficulties may exist in this e.g. what is the value of a 25% grown potato?
- There are revised disclosure and accounting requirements for public benefit entities (i.e. an entity which provides goods or services on a not-for-profit basis).

Related party transactions

- The definition of a related party has been revised.
- There is now a requirement to disclose amounts paid to key management personnel – who qualifies under this is a key judgement point for directors.
- Long term intercompany loans must be shown using an "effective interest" method – so companies are required to recognise implied interest income and associated charges.

Deferred tax

- All revaluations must include provision in full for deferred tax.
- Disclosure requirements have been increased.

For further information please contact a member of the Financial Reporting team.

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