FRS 102 Triennial review - beyond the headlines

18 October 2018

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FRS 102 Triennial review - beyond the headlines

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Introduction

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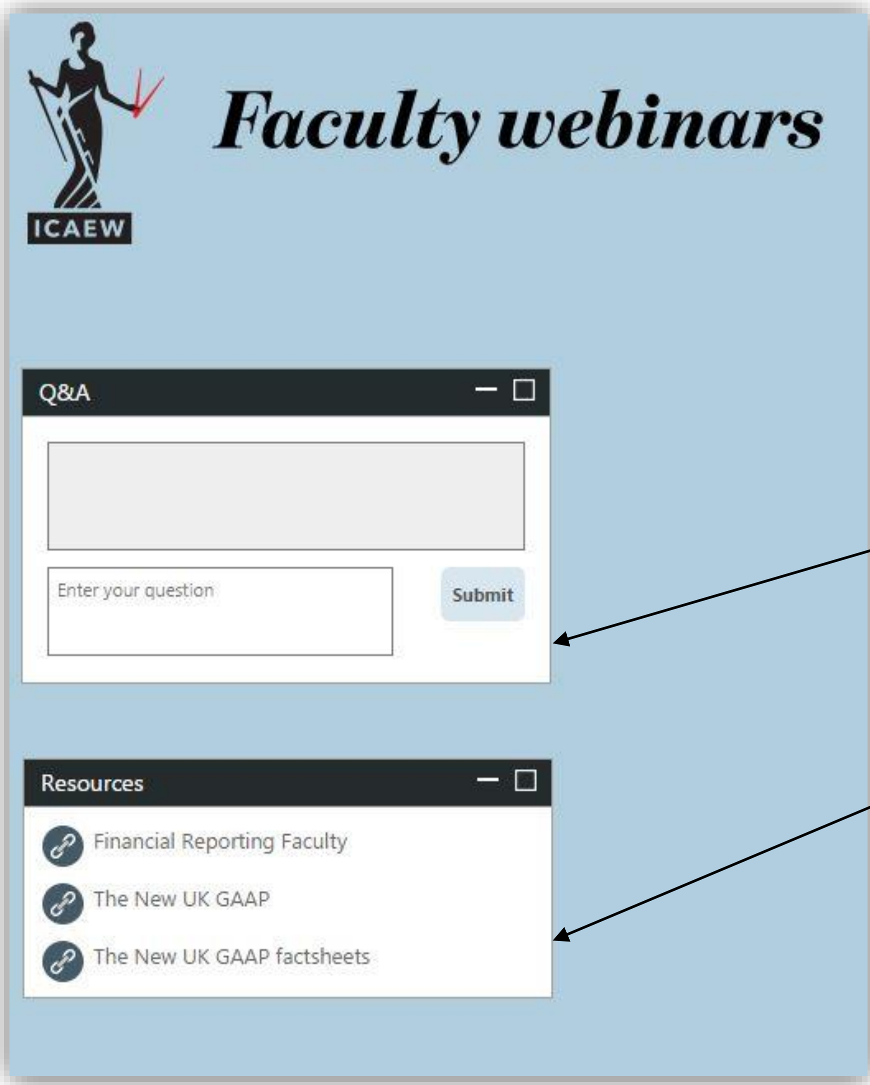
Ask a question



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Ask a question

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Contents

Poll question

Which of the following best describes your current position in relation to the Triennial review amendments?

Intangible assets in business combinations – pre Triennial review

Intangible assets must be identifiable

- Separable; *or*
- arises from contractual or other legal rights

General recognition criteria

- Probable expected future benefits will flow to entity
- Cost or value can be reliably measured

Intangibles as part of a business combination

- Recognise separately from goodwill unless cannot be reliably measured

Intangible assets in business combinations – Triennial review amendments

Must capitalise

- Separable; **and**
- Arises from contractual or other legal rights.

May capitalise

- Separable; **or**
- Arises from contractual or other legal rights.
- Accounting policy choice per class of asset
- Consistently applied to all business combinations

Intangible assets in business combinations – Triennial review amendments

Amendments are applied prospectively

Previously recognised intangibles are not subsumed within goodwill

Examples

Type of intangible	Contractual or other legal rights?	Separable?	Capitalise?*
Trademarks	✓	✓	Must
Customer lists	X	✓	May
Customer contracts	✓	If transferable	Must if transferable
Construction permits	✓	If transferable	Must if transferable
Unpatented technology/ software	X	✓	May

* As long as probable expected future economic benefits and reliable cost/value

Investment properties

Investment properties
at fair value through profit or loss

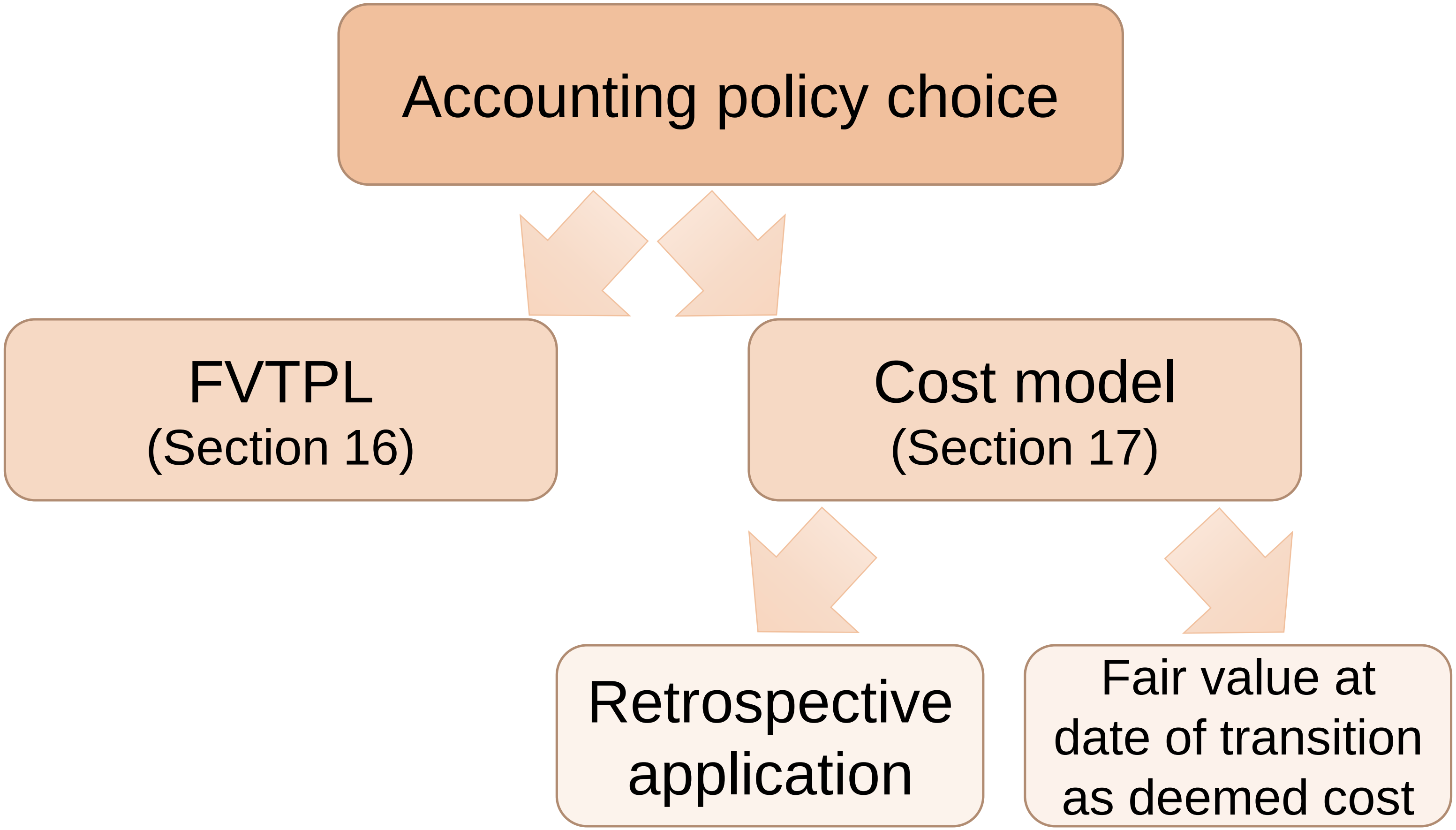
Pre-Triennial review

Undue cost or effort exemption

Triennial review

Accounting policy choice for IPs rented to other group entities

Investment properties rented to other group entity



Investment properties rented to other group entity – cost model

Retrospective application	Deemed cost
• Restate to original cost at date of purchase • Reverse fair value gains/losses since date of purchase • Adjust for depreciation from date of purchase • Adjust deferred tax	• Reverse fair value gains/losses since date of transition • Adjust for depreciation from date of transition • Adjust deferred tax • Revaluation reserve for fair value uplift between date of purchase and date of transition

Example

- Year end 31 December
- 1 January 2014, investment property purchased for £1m
- Rented to another group entity
- Useful economic life estimated at 20 years
- FRS 102 applied from 2015
- Fair values of property:

31 Dec 2015 and 1 Jan 2016	£1.6m
31 Dec 2016 and 1 Jan 2017	£2.2m
31 Dec 2017 and 1 Jan 2018	£2.4m

- Ignore deferred tax

Year ended 31 December 2018

Adopt Triennial Review 2017 amendments

Change accounting policy to account for property at cost

Date of transition:

1 January 2017

1. Apply new accounting policy retrospectively

Restate opening reserves (as at 1 January 2017)

Reverse out accumulated fair value gain	Recognise accumulated depreciation
£2.2m - £1m = £1.2m	£1m / 20yrs x 3yrs = £0.15m
Dr Retained earnings £1.2m Cr Property £1.2m	Dr Retained earnings £0.15m Cr Property £0.15m

Similar types of adjustments as at 31 December 2017

2. Use FV at date of transition as deemed cost

As at 1 January 2017

£2.2m fair value will now become 'cost'

Transfer accumulated fair value gain to a revaluation reserve
£2.2m - £1m = £1.2m

Dr Retained earnings £1.2m
Cr Revaluation reserve £1.2m

Only start recognising depreciation from 1 January 2017
'Cost' £2.2m / remaining UEL 17yrs = £0.129m

2. Use FV at date of transition as deemed cost

As at 31 December 2017

£2.4m fair value needs to be reduced to £2.2m ‘cost’

Dr Retained earnings £0.2m
Cr Property £0.2m

Recognise a year’s worth of depreciation

2. Use FV at date of transition as deemed cost

For 31 December 2018 and future periods
until property disposed

Additional disclosures required (as for all revalued assets)

See FRS 102.17.32A

Investment properties - Transfers

IP to PPE / Inventory	• Fair value at date of change becomes deemed cost for treatment under Section 17 / Section 13
PPE to IP	• Charge depreciation up to date of change, then revalue under Section 17, then transfer to IP
Inventory to IP	• At date of change, difference between carrying value and fair value is taken to profit or loss

Poll question

Which of the following choices are you likely to take / recommend to clients in respect of investment properties rented to other group entities?

Debt for equity swaps – general requirements

Financial liability

- Carrying value derecognised

Equity

- Recognised at fair value of cash / other resources received, net of transaction costs

FV of liability extinguished?

FV of equity issued?

Difference

- Gain or loss recognised in profit or loss

Debt for equity swaps – exceptions to general requirements

Financial liability

- Carrying value derecognised

=

Equity

- Measured at carrying value of liability

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Debt for equity swaps – Triennial review

No gain or loss recognised

Original terms	With shareholders	Under common control
• Eg, convertible debt	• Direct or indirect • In shareholder capacity	• Before and after transaction • Substance is equity distribution / contribution

Example 1 – transaction with a shareholder

- Issue ordinary shares with FV of £50m to extinguish liability to ultimate parent
- Such a settlement was not envisaged in the original loan terms
- Amortised cost and carrying value of liability is £55m

Example 1 - solution

- Lender is an indirect shareholder
- So even though this is not a conversion in accordance with the original loan terms, the Triennial review amendments will apply

Dr Liability	£55m	
Cr Equity		£55m

- Note that the fair value of the shares makes no difference to this double entry

Example 1 – under common control

Accounting treatment would be same if

Entity and lender under common control before and after transaction

And

This is in substance an equity transaction

Recognition in equity

- Depends on redemption amount of liability at settlement date (the ‘liquidated sum’ or face value)
- As a matter of UK law, this is the amount that must be credited to share capital and premium
- This might not be the same as the carrying amount or the fair value
- Review supporting documentation and obtain legal advice if liquidated sum is not clear

Example 2

- Issue ordinary shares with FV of £50m to extinguish liability to an unrelated third-party lender
- Such a settlement was not envisaged in the original loan terms
- Transaction costs on the loan of £1m
- Loan is (approximately) half way to maturity, so half the transaction costs have been amortised ie, amortised cost and carrying value of loan at extinguishment was £54.5m

Example 2 – continued

- Loan was originally for £55m
- Bullet repayment at maturity
- No interest outstanding at extinguishment
- No early termination penalty
- Nominal value of shares issued is £10m

Example 2 – solution

Dr Liability	£54.5m
Cr Profit or loss	£4.5m
Cr Equity	£50m

Cr Share capital £10m

Cr Share premium £40m

But….

The total credit to equity needs to equal the liquidated sum of £55m (ie, the face value, not the carrying value)

Example 2 – solution (continued)

- So…

Dr Retained earnings (£45m - £40m)	£5m
Cr Share premium	£5m

- Net debit of £500k to retained earnings, representing the unrecognised transaction costs

Example 2 – solution (continued)

Statement of changes in equity (extract)

	Share capital	Share premium	Retained Earnings	Total
Profit for the year	-	-	4.5	4.5
Conversion of loan	10	45	(5.0)	50
	10	45	(0.5)	54.5

Other FRS 102 issues

- Net debt reconciliation
- Key management personnel disclosures
- Revenue: agent or principal
- Contract costs on construction contracts
- Small companies
- Key disclosure removals

Net debt notes – FRS 1

27	Reconciliation of net cash flow to movement in net debt	2014	2013
		£000	£000
	Decrease in cash in the year	(750)	(1,810)
	Cash outflow from decrease in deb	1,500	1,500
	Change in net debt r flows	50	(310)
	Other non-cash New finan		(1,000)
	Movement		(1,310)
	Net debt a		(8,190)
	Net debt		(9,500)

28	**Analysis o**			n h es 00	At 31 December 2014 £000
	Cash in hand, a			-	1,000
	Overdrafts			-	(250)
				-	750
	Debt due after 1 year				
	Debt due within 1 year		00	-	(9,000)
	Finance leases	(1,)	500	(1,000)	(1,500)
	Total	(9,500)	750	(1,000)	(9,750)

Net debt reconciliation – FRS 102

Not quite the same thing!

	At 1 Jan	Cash flows	New finance lease	Acquisition of subsidiary	Movements in market value and foreign exchange	Other non-cash changes	At 31 Dec
Overdraft	(150)	(63)	-	-	-	-	(213)
Bank borrowings due within 1 year	(4,000)	4,000	-	-	-	(4,500)	(4,500)
Bank borrowings due in more than 1 year	(19,900)	-	-	-	-	4,450	(15,450)
Finance leases	(8,426)	2,726	(1,239)	(404)	-	-	(7,343)
Cash	7,412	845	-	132	(746)	-	7,643
Cash equivalents	2,847	(204)	-	-	-	-	2,643
Net debt	(22,217)	7,304	(1,239)	(272)	(746)	(50)	(17,220)

Key management personnel compensation disclosures

Exemption from disclosing key management personnel compensation in the following circumstances:

- The entity is subject to a legal or regulatory requirement to disclose directors' remuneration (or equivalent), e.g. the Companies Act 2006 requirements for UK companies; and
- The key management personnel and directors are the same.

Other transactions with directors will still need to be disclosed (Section 33) apart from share based payment arrangements

Revenue: agent or principal

Based on the guidance included in IAS 18 Revenue

Acting as principal if has exposure to significant risks and rewards, for example:

- Primary responsibility for providing goods or services to the customer or fulfilling the order
- Has inventory risk before or after the customer order, during shipping or on return
- Latitude in establishing prices
- Bears the customer credit risk on the receivable

Revenue: agent or principal

Acting as agent if **do not** have exposure to significant risks and rewards

- Amount entity earns is predetermined – fixed fee or stated percentage

Contract costs

Costs incurred in securing a contract

Included as part of contract costs if:

- Relate directly to the contract
- Separately identifiable and capable of reliable measurement
- Probable the contract will be obtained

Small companies

Accounts not prepared on a going concern basis

Departure from principles set out in company law

Disclose

- Particulars of departure
- Reasons for it
- Its effects

Small companies

Disclosure of loans from directors and from shareholders with a participating interest

In the basis for conclusions on the Amendments, the FRC notes that if such loans are at non-market rate, the disclosure requirements of 1AC.35 apply. Certain particulars about such loans must therefore be given in the notes.

Disclosure removals

5. SHARE CAPITAL

	2016	*2015*
	£	*£*
Allotted, called up and fully paid		
138,839,291 *(2015: 131,893,199)* Ordinary shares of £0.001 each	**138,840**	*131,893*

During the year 6,946,092 Ordinary £0.001 shares were issued for total consideration of £746,010.

Disclosure removals

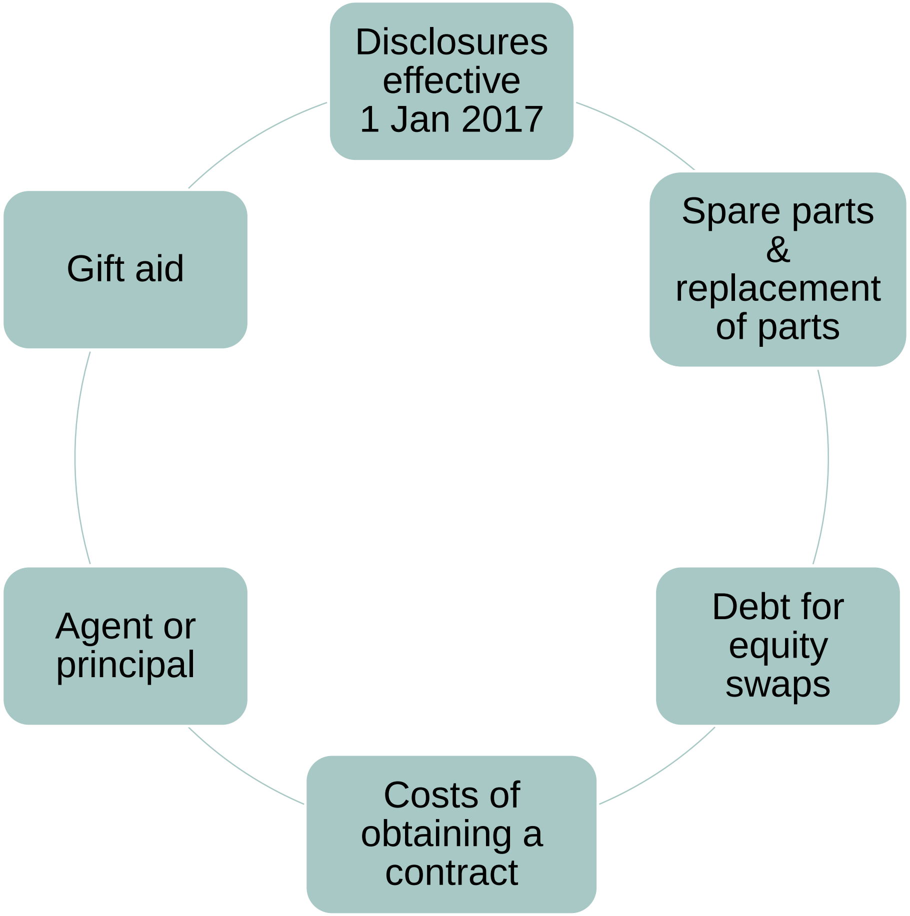
12. STOCKS

	31 December 2016 £	*31 March 2016 £*
Raw materials and consumables	**524,670**	*595,471*
Finished goods and goods for resale	**8,453,828**	*5,149,441*
	8,978,498	*5,744,912*

Stock recognised in cost of sales during the period as an expense was £19,701,555 (*31 March 2016:* £20,339,913).

An impairment charge/(credit) of £323,883 (*31 March 2016:* £(99,605)) was recognised in cost of sales in relation to the movement in provision against stock during the period due to slow-moving and obsolete stock.

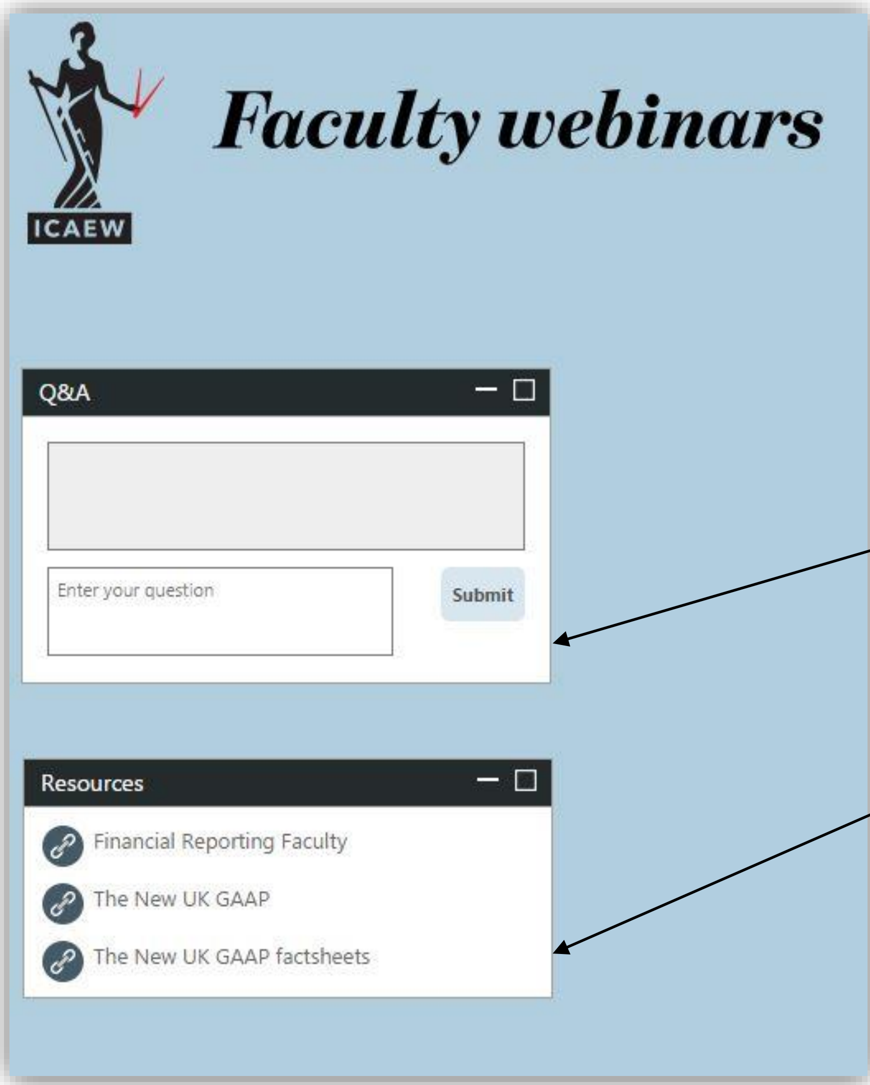
FRS 105 Micro-entity accounts



Consequential amendments to SORPs

- Pensions – updated SORP
- Charities – Update Bulletin 2
- LLPs – consultation period closed yesterday
- Social housing providers – updated SORP expected shortly
- Further and higher education – updated SORP
- Investment Companies – updated SORP

Ask a question



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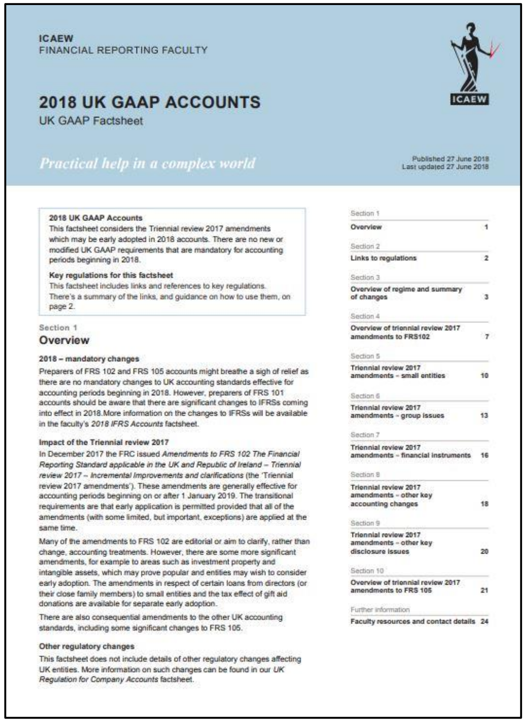

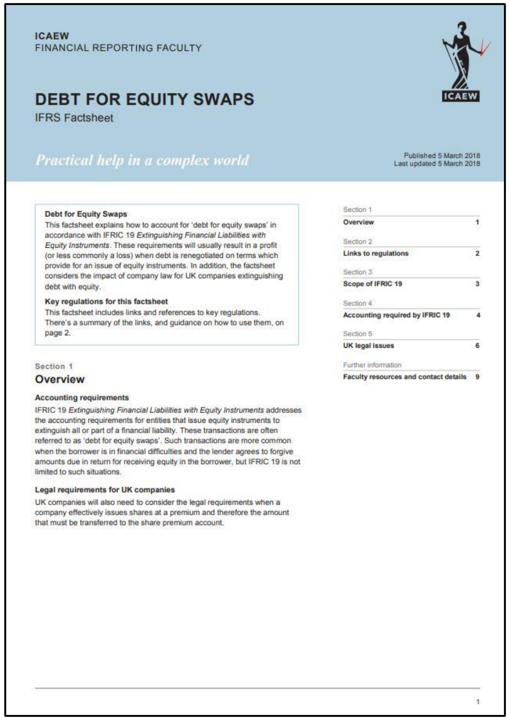

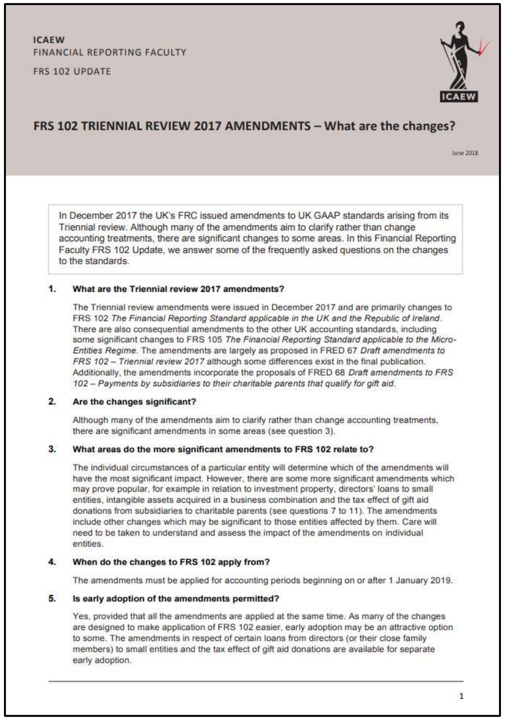

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Questions

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- 13 Dec - UK GAAP- untangling the knots

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Events

- From 26 Sept - Financial Reporting Essentials Roadshows
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