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Mind the GAAP: the new reporting standards

The introduction of new UK GAAP (Generally Accepted Accounting Practice) makes significant changes to the form and content of company accounts. Your bottom-line profit or loss may consequently be different – there could be an impact on the balance sheet and changes could lead to higher or lower tax bills. Here we outline some of the main aspects of the changes that companies should be aware of.

The exact impact of the switch will depend on the nature of your company activities and the types of assets the company has. We can help you to conduct an impact assessment.

For medium-sized and larger companies

For these companies, the changes result from the introduction of FRS 102 ('Financial Reporting Standard 102 – The Financial Reporting Standard applicable in the UK and Republic of Ireland'). FRS 102 replaces all existing UK accounting standards – other than the Financial Reporting Standard for Smaller Entities (FRSSE) (see below). The new standard is applied for periods commencing on or after 1 January 2015, and all periods thereafter.

Small companies – do you qualify?

FRS 102 does not have to be followed by small companies at this stage. Instead, you can continue to opt for the FRSSE. However, for accounting periods commencing on or after 1 January 2015 there are some 'consequential changes' to the FRSSE. In particular this affects related party definitions, the amortisation of intangibles and impairment reviews. To qualify as small, broadly, a company needs to satisfy two of the following three criteria on an ongoing basis:

	Current	Period commencing 1 Jan 2016
Turnover	£6.5m	£10.2m
Total assets	£3.26m	£5.1m
Employees	50	50

The FRSSE will no longer be in use for accounting periods beginning on or after 1 January 2016. For this year small companies will be brought into the scope of FRS 102, unless they qualify as a micro-entity. Micro-entities will be permitted to use a new simplified standard – FRS 105. Please contact us for further information.

How FRS 102 could impact on your accounts

FRS 102, including appendices, is less than 350 pages in length – significantly less than the previous rules.

Taxation

One of the most important impacts is on the tax payable on profits. Broadly, tax is payable on the profits given in the accounts. Consequently, if the accounting profits increase or reduce as a result of a new accounting standard, so does the amount of tax you need to pay. (There are certain exceptions to this, such as the change to investment property accounting described on page two.)

New GAAP does not affect continuing tax-related issues such as capital allowances.

The changes also mean that there will be more instances where deferred tax must be provided for. For example, the deferred tax on revaluations will now be provided for rather than just appearing in a note to the accounts.

Accounts presentation

Some of the detailed content within the accounts may be different and use slightly different terminology under FRS 102. For example, there is a greater chance that related party transactions can be disclosed by category without the need for the names of related parties.

Investment properties

These are properties held not for company use but to make money from, whether by rental income or by eventual sale proceeds. The definition has been widened such that properties which were excluded from the definition (owner occupied investment properties and properties rented to other group companies) are no longer excluded.

Investment properties are required to be revalued each year. However, rather than taking annual gains or losses directly to reserves on the balance sheet via the statement of recognised gains and losses (the STRGL), the gains or losses now have to be taken to the profit and loss account for the period.

Even though included in the profit for the year, these gains and losses are not realised gains or losses, are not available to pay out as dividends, and will not be taxable until the properties are actually sold.

Goodwill (and other intangibles)

This is an area where new UK GAAP is more complicated. It is more likely that 'intangible assets' (other than goodwill) will appear in the accounts. In principle, an intangible should be written off over its estimated life and where that is being done already there may be no change.

Previous UK GAAP stated that intangibles should be written off over no more than 20 years, unless a formal impairment review is carried out. Under new UK GAAP, intangibles should be amortised over no more than five years (although this figure is expected to change to ten years when the FRS is revised this summer) unless a longer period can be justified.

In some circumstances, the annual amortisation may be much larger, reducing profits significantly.

Financial instruments

This is the technical name for a few items that may appear in your accounts such as cash, debtors, creditors, loans payable and receivable and derivatives. Companies may have had financial instruments where new UK GAAP requires a different treatment.

For example, some financial instruments are now required to be revalued each year to 'Fair Value' (roughly their market value at the balance sheet date) and any profits or losses have to be taken to the profit and loss account. Some of these, but not all, will also have an impact on taxable profits.

Financial instruments which will normally be included at their fair value include:

- certain investments in other companies
- forward foreign currency contracts
- exchange rate swaps
- futures.

There is also new treatment for certain loans payable and receivable (for which the effective interest rate basis needs to be applied) and financing transactions (where the present value basis should be used).

Related party disclosures

These can be disclosed by category without the need for the names of related parties, however additional disclosure of 'compensation of key management personnel' is required. This is additional to the company law requirement to disclose 'directors' remuneration'.

In many instances the disclosure required by FRS 102 and the Companies Act 2006 will be the same. Where key management exist in addition to the directors, additional disclosure will be needed.

Other key changes include:

- accruing for outstanding holiday pay
- spreading of lease incentives
- changes to tangible fixed assets (such as land and buildings)
- changes in group accounts
- changes to cash flow statements.

UK GAAP GOING FORWARD

The first year

The new standard must implemented for any accounting period beginning after 1 January 2015. For example, if your company year end is 31 March 2015, FRS 102 must first be adopted for the period beginning 1 April 2015. Your figures for the comparative period will need to be recalculated to comply with the new standard.

With a period end of 31 March 2016 your company is obliged to recalculate the comparative figures for the period ending 31 March 2015, and to restate the opening comparative net assets at 31 March 2014 – known as the 'date of transition'.

SOME COMPLICATIONS

Profits of the earlier periods may be increased or reduced as a result, and the impact of these changes will be entered into the tax computation for the first year of using FRS 102. The previous year's tax computations will not be reopened unless errors were made.

Certain exemptions or options can be chosen when you adopt the new standard. These include the possibility of using a deemed cost at transition for items of property, plant and machinery, which can provide greater strength on your balance sheet and avoid the need to have an ongoing policy of revaluation.

You are also required to include certain disclosures showing the impact of the new standard on your company.

The rules for both small and larger companies are complex, so contact us for more information and to discuss the impact of FRS 102 on your accounts.