Changes to UK GAAP
Are you ready?

FRS 102 is the third of three new standards which will form the bulk of UK GAAP. FRS 102 is expected to be the standard of choice for most unquoted large and medium sized companies. The rules for determining a company’s size are quite complicated but typically it will be those which exceed more than one of the following criteria: turnover £6.5m per annum, total assets of £3.26m and 50 employees.

Whilst the new standard can be adopted early it is mandatory for accounting periods commencing on or after 1 January 2015. However, since accounts must include comparative information, companies really need to be ready for the new standards from the year ended 31 December 2014. Early consideration of the impact of FRS 102 is vital.

What are the other implications?

- **Banking covenants** – increased profit volatility as well as changes to balance sheet valuations may all have an impact on bank covenant criteria. We recommend discussing the potential impact with your bank at an early stage to manage expectations.
- **Distributable reserves** – substantial changes (for example in relation to pensions) may significantly alter distributable profits. Consider the impact on future dividend policy or re-structuring plans.
- **Timing of tax payments** – some companies may find that they fall in or out of the quarterly instalment payment regime, so the timing of their corporation tax may change. Given that taxable profits may also be subject to greater volatility, this could put a strain on cashflow.
- **Employee benefits, earnouts & key performance indicators** – where these are linked to company results, the impact on existing plans and future proposals may need to be addressed.
- **Small companies** – whilst this accounting standard does not apply to small companies, it is important for small growing companies especially, to be aware of the thresholds to become a medium sized company.

Dafferns can help in your transition process by:-

- Identifying differences between FRS 102 and your current GAAP and assessing the impact on your primary statements, distributable reserves and your tax cash flows.
- Identifying any additional information needed for the transition process and any potential system changes.
- Assisting in the preparation of journals and drafting of accounting policies.
- Assisting in the drafting and preparation of your FRS 102 financial statements including comparative financial information.
### Changes to UK GAAP

**The key changes**

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<thead>
<tr>
<th>Area</th>
<th>Current UK GAAP</th>
<th>FRS 102</th>
<th>Tax treatment</th>
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</thead>
<tbody>
<tr>
<td><strong>Intangible assets acquired in business combination</strong></td>
<td>Many intangibles are included within residual goodwill as they are not separable.</td>
<td>The definition of intangibles has changed therefore more intangibles are likely to be recognised separately from residual goodwill.</td>
<td>The tax treatment follows the accounts treatment in terms of the amortisation of goodwill.</td>
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<td><strong>Other goodwill and intangible assets</strong></td>
<td>Maximum useful economic life (UEL) is 20 years or less but it can be rebutted where longer or indefinite life can be justified.</td>
<td>Maximum UEL is presumed to be 5 years where no reliable estimate can be made.</td>
<td>As the presumed UEL is shorter under FRS102, there may be an acceleration of amortisation charges, leading to tax cash flow advantages.</td>
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<td><strong>Investment properties</strong></td>
<td>SSAP 19 currently requires revaluation of all investment properties, with no exemption for cost or effort. Gains and losses go to the STRGL. The cost less depreciation model is not allowed.</td>
<td>FRS 102 requires revaluation each year to fair value with value changes taken to profit or loss. The cost less depreciation model is used only if fair value cannot be measured reliably without undue cost or effort.</td>
<td>Any such gains and losses will be capital and hence ignored for tax purposes. Tax will only generally be relevant when a gain or loss arises on the sale of the property.</td>
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<td><strong>Investment in shares</strong></td>
<td>Measured at either cost or fair value. Where fair value is used, changes are recognised in STRGL.</td>
<td>Measured at fair value where it can be determined reliably (e.g. listed shares). Changes in fair value are recognised in profit or loss. Investments in unlisted shares, cost less impairment can be used.</td>
<td>Any such gains and losses will be capital and hence ignored for tax purposes. Tax will only generally be relevant when a gain or loss arises on the sale of the shares.</td>
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<td><strong>Financial instruments (e.g. interest rate swaps, hedging, share options)</strong></td>
<td>Unless a company uses FRS 26, financial assets are not usually held at market value and derivatives are not accounted for. Gains and losses are normally recognised at settlement.</td>
<td>FRS 102 divides instruments into: • Basic (to be measured at amortised cost, except for listed shares or shares with reliable fair value) • Others (mostly at fair value)</td>
<td>Default rule is that tax follows the accounts treatment. The tax rules for financial instruments are currently being reviewed, with more changes anticipated in 2015.</td>
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<td><strong>Deferred tax</strong></td>
<td>Based on timing differences. FRS 19 does not require deferred tax on revalued assets if no binding contract for sale.</td>
<td>Deferred tax recognised on revaluation of assets under FRS 102. Increased deferred tax charge may reduce distributable profits.</td>
<td>Consider the impact of any rollover claims.</td>
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<td><strong>Holiday accrual</strong></td>
<td>Accounting for holiday accruals is not mandatory.</td>
<td>Accounting for holiday accruals is mandatory.</td>
<td>Tax relief is given on this accrual if paid within 9 months of the year end.</td>
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<td><strong>Lease incentives</strong></td>
<td>Lease incentives are recognised over the period to the first market rental review or first break clause.</td>
<td>Under FRS 102, incentives to enter into a lease will be recognised as a reduction to the expense passing through the profit and loss account over the whole lease term.</td>
<td>The payment of tax could be deferred under FRS 102 as revenue incentives are spread over a longer time period.</td>
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<td><strong>Defined benefit pension plans</strong></td>
<td>Current UK GAAP requires recognition in the profit or loss account for the current service cost, interest cost and expected return on plan assets and in the STRGL for actuarial gains and losses.</td>
<td>FRS 102 requires recognition in profit or loss for current service cost and net interest cost and recognition of the re-measurement of the net defined benefit asset or liability.</td>
<td>No change to timing of tax relief – pension contributions are still only allowed when paid.</td>
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<td><strong>Defined benefit pension plans – multi employer schemes</strong></td>
<td>Under FRS 17 group entities can use the multi employer exemption to avoid recognising their share of the group plan in their individual financial statements.</td>
<td>This exemption will continue under FRS 102. However, a key change to multi employer schemes is where an agreed plan for deficit funding is implemented, full provision must be made for the amount of that deficit funding.</td>
<td>No change to timing of tax relief – pension contributions are still only allowed when paid.</td>
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This publication is intended for general guidance only. This publication contains a summary of the key differences between existing UK GAAP and FRS 102 and is not an exhaustive list of all differences. No responsibility is accepted for loss occasioned to any person acting or refraining from actions as a result of any material in this publication.