BOURNER BULLOCK
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The Changing Landscape for Small Entities

In 2013, the Financial Reporting Council ("FRC") issued a new suite of UK accounting standards to replace all existing FRS's, SSAP's and UITF Abstracts.

Within that set of new standards, FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" was the new standard applicable to entities not qualifying for small entity exemptions. An update to the FRSSE was announced at that time, meaning that the perceived impact for small entities was not particularly significant. However, in July 2015, as a result of EU-driven changes to Company Law, the FRC released Section 1A of FRS 102 which fundamentally changes the accounting landscape for small entities. For the smallest of entities qualifying as micro-sized, another new standard has been released, FRS 105 "The Financial Reporting Standard applicable to the Micro-entities Regime".

The Impact for Small Entities

For accounting periods commencing on after 1 January 2015, small entities will either use the FRSSE (effective January 2015) or voluntarily adopt FRS 102. The differences between FRSSE (effective April 2008) and FRSSE (effective January 2015) are relatively minor, really only causing concern where the entity has goodwill or other ineligible assets.

However, for accounting periods commencing on or after 1 January 2016, everything changes for small entities.

A New Accounting Standard - FRS 102 Section 1A

As a result of amendments made to FRS 102 that were issued in July 2015, a small entity will have to adopt the new Section 1A of FRS 102 for periods commencing on or after 1 January 2016 (assuming it either does not qualify for, or chooses not to adopt, the micro-entity regime (see below), IFRS or FRS 101). Please note that the FRSSE (effective January 2015) will not be available for use after this date.

FRS 102 Section 1A includes all of the same measurement and recognition principles as full FRS 102 (which applies to non-small entities), resulting in a more complex accounting framework being applied.

As noted above, the mandatory adoption date for FRS 102 Section 1A is for accounting periods commencing on or after 1 January 2016 (so, in most cases, for year ends of 31 December 2016 onwards). FRS 102 (and, therefore, Section 1A) requires entities to apply the accounting requirements of the standard from a "transition date", which is the opening day of the comparative period. This is likely to result in an amendment to brought forward reserves in the comparative period as well as a full restatement of the comparative figures. So, for a 31 December 2016 year end, the transition date will be 1 January 2015. A small entity will benefit from some transitional provisions over and above those for non-small entities, which can be discussed as required.

Contact us and speak to a Partner for more information

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So, what is going to change?

There could be significant changes to the numbers reported in a set of financial statements, not to mention differences in how the financial statements will look. The impact will be dependent on specific circumstances, but some of the headline issues are:

- **Amortisation of Intangibles**

Unless a different useful economic life can be supported, all intangibles including goodwill have a maximum useful economic life of 10 years (historically this was 20 years

- **Deferred Tax**

Deferred tax must be recognised on all revaluation gains – at present, such deferred tax is normally disclosed but not recognised on the Balance Sheet.

- **Longer Term Loans Not on a Commercial Basis**

The requirement to use the amortised cost method requires loans to be discounted to their present value and the adjustment for this to be unwound over the life of the loan. This may significantly impact the carrying value of these loans in the financial statements.

- **Financial Instruments (including foreign exchange contracts and interest swaps)**

The value of these at each year end must be obtained (often from the issuer) and their fair value included in the financial statements. These were normally not recognised under old UK GAAP and will result in an impact on profit for the period.

- **Investment Properties**

Any valuation movement, instead of being recognised as a revaluation reserve will be recognised in profit or loss under FRS 102. Also, a provision for deferred tax will be needed in respect of any uplift in valuation which would be taxable if the gain was to be realised.

- **Operating Lease Incentives**

The requirement to spread these over the entire life of the lease may result in a smaller credit to profit in the early years of the lease.

- **Valuation of Property Used by the entity**

The standard permits the freezing of existing valuations on transition, even if not previously recognised, allowing clients to bolster their Balance Sheet without the need to maintain the revaluation model going forward (NB - remember the deferred tax impact).

- **Acquisitions**

Each intangible asset that could be sold separately must be valued and capitalised as a separate asset. This will result is many more intangibles being recognised on consolidation and a far smaller goodwill figure.

- **The Unknowns and the Unknown Unknowns**

There are many other differences, e.g. holiday pay accruals, changes in definitions for leases, development costs etc. which could be very material to the financial statements.

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