Think Ahead ACCA

FRS102 implementation issues

Invitation to comment issued by Financial Reporting Council in March 2016

Comments from ACCA
28 October 2016

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Further information about ACCA's comments on the matters discussed here may be obtained from the following:

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ACCA welcomes the opportunity to provide views in response to the FRC's invitation. This response contains issues that members have raised with us and we are putting them forward to FRC for them to consider in their review of FRS102, without ACCA necessarily endorsing the need for any change on the different items raised. It has been put together with the assistance of the members of ACCA's Global Forum for Corporate Reporting, the ACCA Members' Advisory service and other ACCA members in UK and Ireland. The issues are described briefly and if further information is needed on them, please get back to us.

This request for implementation issues should try to capture as many issues as possible. However, we note that many companies have only applied FRS102 for one year and not yet applied FRS105, meaning that the implementation issues raised at this point are unlikely to be comprehensive.

We shall be responding separately to the FRC's Discussion Paper on the incorporation of changes to FRS102 derived from changes in IFRS.

THE FEEDBACK REQUESTED

Financial instruments at present value of future payments

ACCA members have often found the users of the accounts have a significant lack of understanding of the outcome of this approach – stating loans at less than the amounts expected to be paid/received and the imputing an interest income or charge against profits when no such cash flows will occur.

Preparers have faced significant issues with these often in the context of loans between group companies or with other related parties. Where there are no written terms for loans or inter-company balances there has been uncertainty whether to assume they are repayable on demand or otherwise. There have been difficulties in determining the appropriate discount rate to apply.

Many have assumed that without evidence to the contrary, loans are repayable on demand. Preparers and auditors, however, have then faced the issue of when the substance of the arrangement might change that – intercompany balance building up over many years or loans outstanding for many years, or whether loans with rolling 53 week terms are appropriately classified as long-term but without discounting.

Staff Education Note 16 does provide guidance on the application to financial instruments, but the existence of this note is not well understood. FRC should consider promoting the status of this guidance and to draw more attention to it.

The language of Section 11 dealing with basic financial instruments should be reconsidered as many preparers and accountants find this very complicated and hard to understand and communicate.

Distributable profits

A number of the accounting changes emerging from the application of FRS102, including the financial instruments issues above, are raising increasing questions about distributable and non-distributable reserves. Difference in practice is emerging with some companies recording separate reserves on balance sheet and others tracking it through file notes. What is clear is that some tracking of this distinction is perhaps more important than before.

The guidance on distributable profits is lengthy and complex. Others have suggested that the guidance is not easily understood or accessible. Some have noted that the FRC have disagreed with the view of some investors and their Counsel's Opinion that this analysis is required by the true and fair view. There may be scope for clarification by FRC.

Business combinations

There is less experience with this so far. While in many cases the rationale of the approach works well, there is concern that many intangibles (especially software development and other forms of intellectual property which, some argue, account for an increasingly large portion of value in today's technology-driven business models) are not being captured based on the guidance in FRS102. On the other hand, in some cases the extensive recognition of these intangibles has led to negative goodwill being recognised as a credit to profit and loss.

Too many companies are taking the 10 year amortisation period (when a useful life cannot be determined) as a rule when it is intended to be by exception. The wording of the standard seems unclear in this regard.

Many are finding the distinction between remuneration and contingent consideration hard to make when entrepreneurial companies are acquired. They would like guidance from FRC, which some would like not to replicate what the IASB have done in this regard.

Deferred tax

Members find in many cases that non-accountant users do not understand the concept or objective of deferred tax. As companies start to consider FRS102 or FRS105, the ability to not provide deferred tax is influencing the choice as to which standard they might adopt.

Credit unions

In Ireland this is a relatively important sector. Credit unions may be charging rates of interest that do not equate to market rates, especially considering the sub-prime sector of the market that is often served by them. The credit unions have not been able to claim public benefit entity (PBE) status. This has meant that an extra interest rate has to be imputed and there may be 'Day 1' losses to recognise. Some of their loans may include features which would make them complex financial instruments. FRC should consider whether it would be most appropriate if the PBE concessionary loans treatment was available to the credit unions.

Leases

It would be helpful if FRS102 could deal specifically with the accounting treatment of leasehold improvements and lease premiums.

Related party transactions

There are some clarifications that should be considered.

Key management personnel are defined more widely than statutory directors, but it seems that disclosures are simply being made for the latter and ignoring the wider potential group.

There is a difference between the definition of close family members between FRS102 and the Charity SORP which seems hard to justify and it might be better if they were aligned.

As more companies start to consider FRS105, further guidance may be requested on what are normal market conditions which might lead to non-disclosure of directors' remuneration and other transactions. This might consist of a direction that disclosure in cases of doubt should be the answer.

Employee numbers

There has been diversity in practice and among the software providers as to whether disclosure of the number of employees is required when the reduced filing requirements are utilised. Section 1A clearly identifies this disclosure as one of the profit and loss account rather than of the balance sheet note and so need not be disclosed. This seems at odds, however, with indications that were issued by BIS as the government department. Clarification from FRC would be helpful.

Undue cost or effort

There may be more instances where the FRC should allow certain requirements, whether recognition, measurement or disclosure, to be avoidable where otherwise undue cost or effort might be expended on fulfilling this. There may well be others in the future. FRC should define what 'undue cost or effort' means.

Accounting software issues

These were frequently raised with us on a number of issues including:

- Companies House and HMRC not being able to handle early applications of the standard
- Software not being available for early adoption

- Significant changes to accounting and tax happening at the same time meaning that updated versions of software were not available
- Errors in software such as dealing with investment property fair value gains, or not providing sufficient accounting policy notes to fit with FRS102

Some of these issues have been felt to be avoidable by better co-ordination between the FRC, the software providers, Companies House and HMRC. The lead time allowed for FRS105 has been especially short.

We note that the timing of some significant upcoming changes to FRS102 may coincide with both HMRC's Making Tax Digital ini tiative and Brexit.