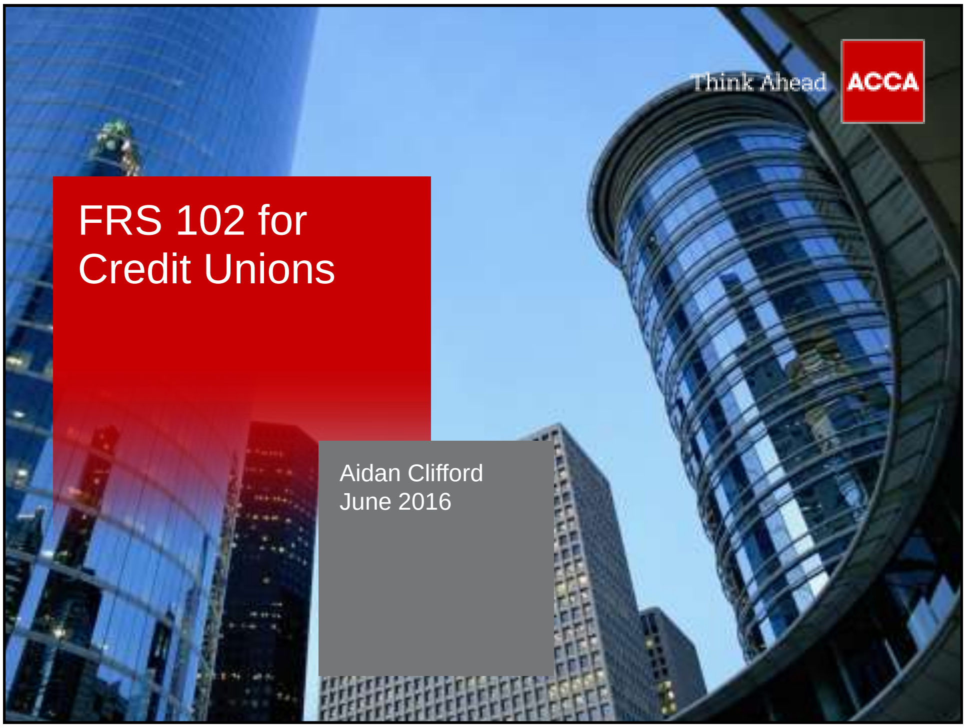

FRS 102 FOR CREDIT UNIONS

- Investments
- The ILCU DB pension
- Bad debts
- Holiday pay accrual
- Interest income under an accrual model
- Other matters

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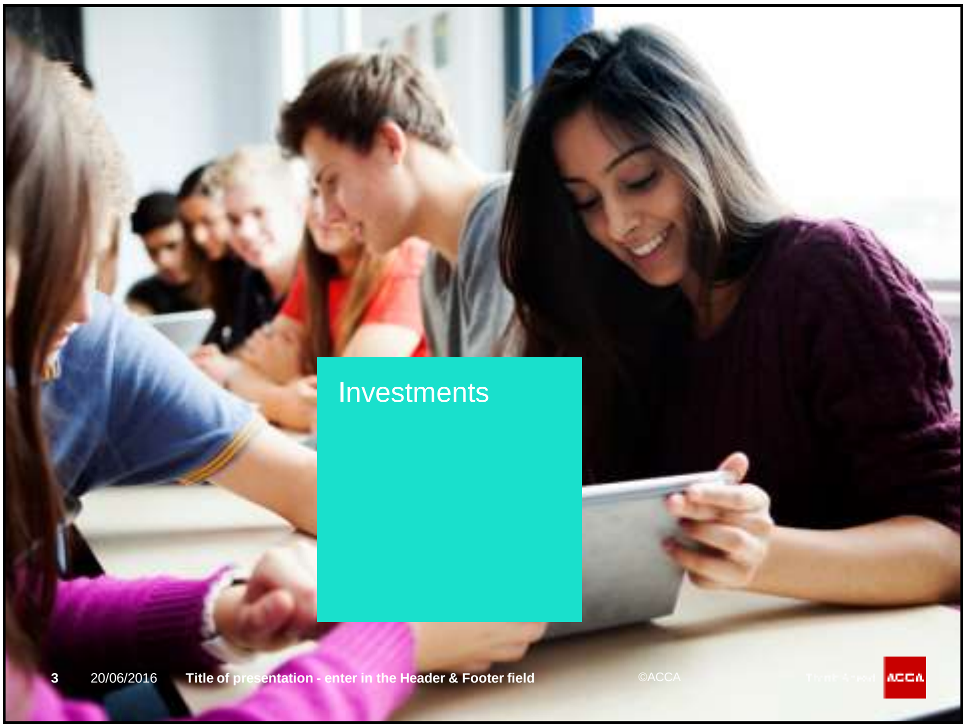

Old Investment Accounting

No mix and matching of models

Cost Model

Long term investments
- Cost less impairment

Short term investments
- Lower of cost and NRV

Fair value Model

Choose one for each investment
- Fair value
- Available for sale
- Held to maturity

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Old Investment Accounting

Never allowed by GAAP

- Expense premium on bond purchase in year of purchase
- Defer discount on purchase to maturity

Investment FRS 102

3 Options
- Use FRS 102
- Use IAS 39 and disclosures per FRS 102
- Use IFRS 9 and discloses per FRS 102

- Old “cost model” no longer allowed

Investment Accounting options under FRS 102

FRS 102 (Standard options)	IAS 39 (allowable option)	IFRS 9 (allowable option)
Amortised Cost	Fair value	Amortised Cost
Fair value	Held to maturity	Fair value
	Available for sale	

IFRS 9 replaces IAS 39 for reporting periods beginning on or after 1 January 2018 – early adoption allowed

Investment Accounting FRS 102

FRS 102 accounting – standard option

- Simple investments - amortised cost less impairment
- Complex investments - fair value

Investment Accounting Issues

Basic Financial instruments

Cash
Bond (debt instrument)
- fixed amount
- fixed rate of return or linked to single index "LIBOR")
- no loss allowed (but subordination is allowed)
- No put or call other than in default
- No conditional return

Investment in ordinary shares (non convertible, non-puttable)

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Investment Accounting Issues

Complex Financial instruments

With profit bond
Investment fund
Commodity bond
Tracker bond
Structured products
…insurance product attached
…conversion options, derivatives attached…
Anything you don't 100% understand the T&C's of

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FRS 102 Basic Financial Instruments S11

- Amortised cost:
  - Initial cost
  - Less repayments
  - +/- amortisation of discount / premium
  - Less impairment

And in English….

Money out to purchase the investment
Money in over life of investment
Difference spread out over life of investment

if the price of the investment goes down
write it down to market value

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Amortised cost – Example

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Issued 2009
Coupon 5.9%
Redemption 2019
Price today 126.4
Yield to maturity 0.118%

Accounting for Investments

Irish State Securities - purchase at a premium
Amortised cost

- Say CU purchased €1m at a cost of €1,260,000
- Maturity 2019

- March 2015 Investment at cost 1.26m
- October Coupon of 55k (reduces investment capital)
- Total coupon 55 X 5 = 275,000

- Paid 1.26m
- Got back 1.275m
- Total interest 0.015m divide over 4 years

Accounting for Investments

Irish State Securities - purchase at a premium
Amortised cost

- March 2015 Investment at cost 1.26m
  - Cr bank 1.26m
  - Dr investments 1.26m
- October Coupon of 55k
  - Dr bank 55k
  - Cr investment 50k
  - Cr Income 5k (est.)

OR
  - Dr bank 55k
  - Cr Income 55k
  - Dr income 50k (schedule out amortisation of 260k premium)
  - Cr investment 50k

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Accounting for Investments

Irish and EMU State Securities - purchase at a premium

Lets be really clear

- Purchase a €1m bond for €1.1m
- Investment is €1.1m (not €1m)
- There is not an expenses of €100k
- Coupon is a cash flow number and irrelevant to the income statement
- Yield (to maturity) is the key number

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FRS 102 complex Financial Instruments

- Fair value:
  - Look to market
  - Look to similar product on market (observable)
  - Model cash flows and discount
    - Engage an expert to value

Gains - to income - all recognised
split out as to realised or unrealised profits
Loss – to expenses

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Fair value – Example

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Accounting for Investments

Corporate bond, interest linked to the return on ISEQ

- Say CU purchased €1m
- Maturity 2020

	Growth in ISEQ	Market value	Gain / loss
• 30 September 2014	1.1m	0.8m	loss (0.2)
• 30 September 2015	1.8	1.2	gain 0.4
• 30 September 2016	1.9	1.2	gain nil

Market value can be based on sentiment, underlying guarantee, liquidity, credit rating, relative performance etc…

More options available under FRS 102

Investment Accounting – IAS 39 option

FRS 102	IAS 39	IFRS 9
Amortised Cost Fair value	Fair value Held to maturity Available for sale	Amortised Cost Fair value

IFRS 9 replaces IAS 39 for reporting periods beginning on or after 1 January 2018

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Investment Accounting Issues

IAS 39 option

- Government bonds can be at "fair value" or held to maturity
- Amortised cost not available
- Held to maturity available
    - "Tainting" rules on HTM –sell early and HTM will not be available in future
- AFS not used by credit unions

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Investment Accounting Issues

IAS 39 option

Available for sale

- Mark to fair value
- book gains and losses to reserves (Available for Sale reserve)
- Recycle gains and losses to profit and loss account when sold.
- Take permanent impairments

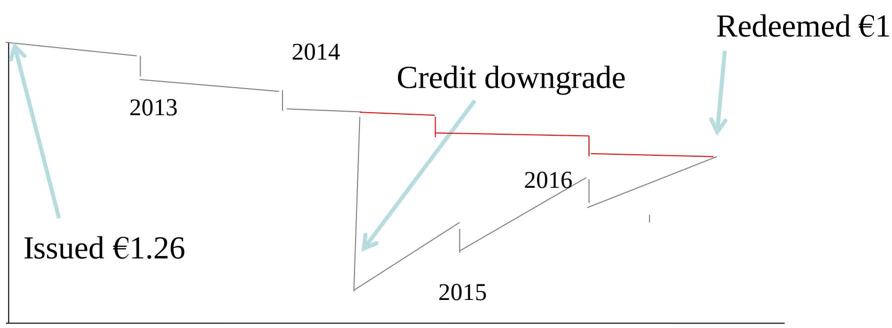
Spend most of AGM explaining what you have done.

Investment Accounting

FRS 102	IAS 39	IFRS 9
Amortised Cost Fair value	Fair value Held to maturity ~~Available for sale~~	Amortised Cost Fair value

IFRS 9 replaces IAS 39 for reporting periods beginning on or after 1 January 2018

Accounting for Investments
Held to maturity V's cost less impairment



Held to maturity: ignore downgrade (but consider impairment)
Cost less impairment: book downgrade – increased yield in future years

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FRS 102 Government Bond accounting

Nominal €1,000,000
Cost €1,200,000
Maturity 18/10/2020
Coupon 5%
Yield 1%

	Market value	HTM income	Amortised cost Income
Purchased	1.20	12	12
30/9/2015	1.17	11.7	11.7
2016	1.13	11.3	11.3
2017	1.10	11	11
2018	1.07	10.7	10.7
2019	1.03	10.3	10.3
2020	1.00	10	10
Total		77	77

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FRS 102 Government Bond accounting

Nominal €1,000,000
Cost €1,200,000
Maturity 18/10/2020
Coupon 5%
Yield 1%

	Market value	HTM income	Amortised cost Income
Purchased	1.20	12	12
30/9/2015	1.17	11.7	11.7
2016	0.95	11.3	(11.3-220 =) loss 208
2017	0.96	11	64 (yield now 6.7%)
2018	0.98	10.7	65
2019	0.99	10.3	66
2020	1.00	10	67
		77	77

Cash each year in coupon is 50,000

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A few sums……

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Investments at "held to Maturity" change to amortised cost

Prior year adjustment

carrying balance at 1/1/2014	10,000 (cost)
Market value at 1/1/2014	6,000
Market value 31/12/2015	9,000
Market value 31/12/2016	10,000

Retained earnings as previously stated	XXX
Change in accounting policy	
Accrual for holiday pay	XXX
HTM Investments restated	4,000
Retained earnings brought forward	XXXX

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The Journals

Investments (held to maturity)	10,000 old accounting
Investment (amortised cost)	6,000 new accounting

Journals to 30 September 2014 opening balance sheet
Cr investments 4000
Dr retained earnings 4000

Journals to 30 September 2015
Cr income 3,000 (reversal of impairment)
Dr investments 3,000 (reversal of impairment)

Journals to 30 September 2016
Cr income 1,000 (reversal of impairment)
Dr investments 1,000 (reversal of impairment)

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Investments with premium expensed, changed to amortised cost

Prior year adjustment

Purchased Government bonds	11,000*
Expensed premium on purchase	1,000 (2014)
Carrying balance 2013-2015	10,000
Market value at 1/1/2014	10,100
Market value 31/12/2015	10,300
Market value 31/12/2016	10,600

- Purchased 30 September 2014, 1000 premium expensed in year ended 30 September 2014.
- Assume premium amortised over 3 years at 400, 360, 340

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The Journals

Investments ("cost" model)	10,000 old accounting
Investment (amortised cost)	11,000 new accounting

Journals to 30 September 2014 opening balance sheet
Dr investments 1000
Cr retained earnings 1000

Journals to 30 September 2015
Dr income 400 (reversal of premium)
Cr investments 400 (reversal of premium)

Journals to 30 September 2016
Dr income 360 (reversal of premium)
Cr investments 360 (reversal of premium)

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FRS 102 Impairment

- Fair value – no impairment review needed
- Amortised cost – impairment review needed – but almost all simple investments have increased in value
- Held to maturity - impairment review is N/A for price changes unless there is a risk to total default or substantial loss

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FRS 102 Impairment of financial Instruments

Check for Objective Evidence of impairment at each reporting date e.g.

- significant financial difficulty or likely bankruptcy
- breach or default in meeting contract terms
- grant of an unlikely concession from the creditor
- observable decrease in estimated future cash flows

- Only losses incurred from past events can be reported as impairment losses
- Losses expected from future events, no matter how likely, are not recognised

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FRS 102 Basic Financial Instruments S11

Disclosure
- Significant accounting policies and measurement basis
- Separate disclosure of each category of FI
- Information to evaluate the significance of financial instruments
- How FV arrived at
- Details of de-recognition, collateral, contingent liabilities
- Details of FIs in P/L

- Financial Institutions have more disclosures to make

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Investment Accounting Issues

Auditor:
- Will want independent valuations of any unusual investment products.
- The seller of the product can not do the valuation
- Sellers often provide independent valuations
- If a valuation is not possible, consider writing it down to nil.

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FRS 102 first time application

- Is the change material
- Can you use a transition option to continue the existing accounting
- For investments consider option to use IAS 32 and 39 (with FRS 102 disclosures) and then continue fair value or HTM accounting until 2018

FRS 102 - Investments

Test your knowledge

- Client purchased 10 year Government bonds some years ago at 7% yield and is now sitting on a capital profit of 200k with 3 more years to maturity.
  1. They want to book the profit what can they do
  2. They don't want to book the profit, but prefer to continue to book 7% income every year – what can they do

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FRS 102 - Investments

Test your knowledge – answers

They want to book the profit what can they do
Sell the investment prior to the year end
Adopt IAS 39 and fair value on transition to FRS 102

They don't want to book the profit,
Continue HTM using IAS 39 option on transition until 2018

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FRS 102 and pensions

Defined benefit pension deficits are on balance sheet
Group pension deficits are not on balance sheet – however, commitments to make up a deficit on a group scheme are on balance sheet.

Projected Contributions (€)	Actual Employer Contributions at 27.7% (€)	Annual Contribution relating to past service (€) Assumed to be 5.5%
1 March 2015	100,000	19,856
1 March 2016	100,000	19,856
1 March 2017	100,000	19,856
1 March 2018	100,000	19,856
Balance Sheet Provision		Provision €
As at 30 September 2014		79,422
Aa at 30 September 2015		59,567
As at 30 September 2016		39,711
Aa at 30 September 2018		19,856

The Journals

Journals to 30 September 2014 opening balance sheet
Cr pension deficit provision 79,422
Dr retained earnings 79,422

Journals to 30 September 2015
Cr wages expense 19,856
Dr pension deficit provision 19,856

Journals to 30 September 2016
Cr wages expense 19,856
Dr pension deficit provision 19,856

FRS 102 and bad debts

General bad debts provision not allowed
Specific bad debts allowed
Incurred but not reported (IBNR) is allowed

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FRS 102 and bad debts

Bad debts	Old GAAP	FRS 102	
Specific	500,000	500,000	
General	1,500,000	nil	
IBNR	Nil	300,000	
Total	2,000,000	800,000	
2014	2,000,000	800,000	(1.2m)
2015	1,500,000	700,000	(0.8m)
2016	n/a	650,000	

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The Journals

Journals to 30 September 2014 opening balance sheet
Dr Loan book 1.2m
Cr retained earnings 1.2m

Journals to 30 September 2015
Dr Loan book 100,000
Cr bad debt expense 100,000
Dr retained earnings 1.2m
Cr risk reserve 1.2m

Journals to 30 September 2016
Dr Loan book 50,000
Cr bad debt expense 50,000
Dr retained earnings 50k
Cr risk reserve 50k

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Holiday pay accrual

- 30 September year end
- Calculate the opening accrual 1 Oct 2014
- Calculate the prior year end accrual 30/9/2015
- Calculate the closing accrual 30/9/2016

Say

- 2014 5,000
- 2015 6,000
- 2016 7,000

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A holiday pay accrual only

Say
- 2014 5,000
- 2015 6,000
- 2016 7,000

- Comparison period
  - Cr accruals 6,000
  - Dr wages charge 1,000
  - Dr retained earnings 5,000

- Current period
  - Cr accruals 1,000
  - Dr wages charge 1,000

Interest income accrual

- "all income and charges relating to the financial year to which the accounts relate shall be taken into account without regard to the date of receipt or payment;"
- "In determining how amounts are presented within items in the income and expenditure account and balance sheet, the directors of a credit union shall have regard to the substance of the reported transaction or arrangement, in accordance with generally accepted accounting principles or practice."

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Interest income accrual

Earned but not received until after the year end

- 2014 5,000
- 2015 6,000
- 2016 7,000

- Comparison period
  - Cr accruals 6,000
  - Dr Income 1,000
  - Dr retained earnings 5,000

- Current period
  - Cr accruals 1,000
  - Dr income 1,000

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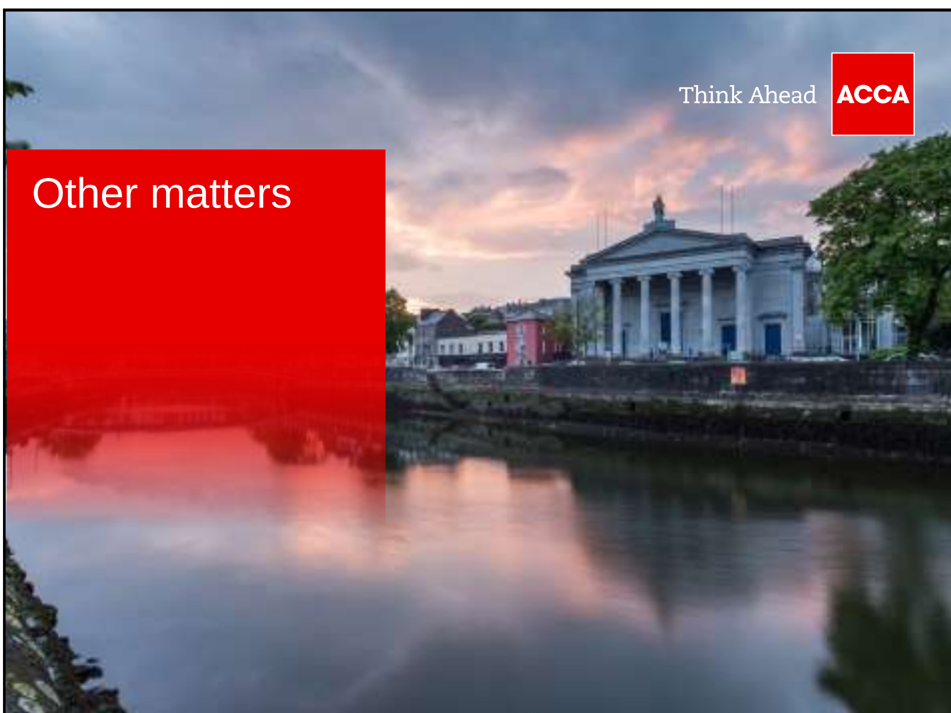
Interest income accrual

Earned but not received until after the year end

- Only amounts that will be received, exclude amounts that are doubtful
- It is an effective boost to retained earnings and should not have a material affect on profit for a particular year
- Student loans, bullet loans, deferred repayment loans



Other matters

Building
- Buildings at cost can stay at cost
- Buildings at market value can stay at market value
- Buildings at market value, provide for inherent CGT on revaluation

Options
- Buildings at market value can be restated back to cost model
  - Lower depreciation charge
  - Less likely to have an impairment
  - Less volatile depreciation and valuations
  - Bigger profit on sale, if they are ever sold
- Buildings at market value can be set at "deemed cost"
  - Freeze current valuation as if it were cost
  - No need to keep valuation up to date
  - Less volatile depreciation and valuations

Other matters

Mergers
- See REBO web site fro technical guidance
- Negative Goodwill is a Dr to retained earnings
- Opportunity for future earnings management in acquisition process

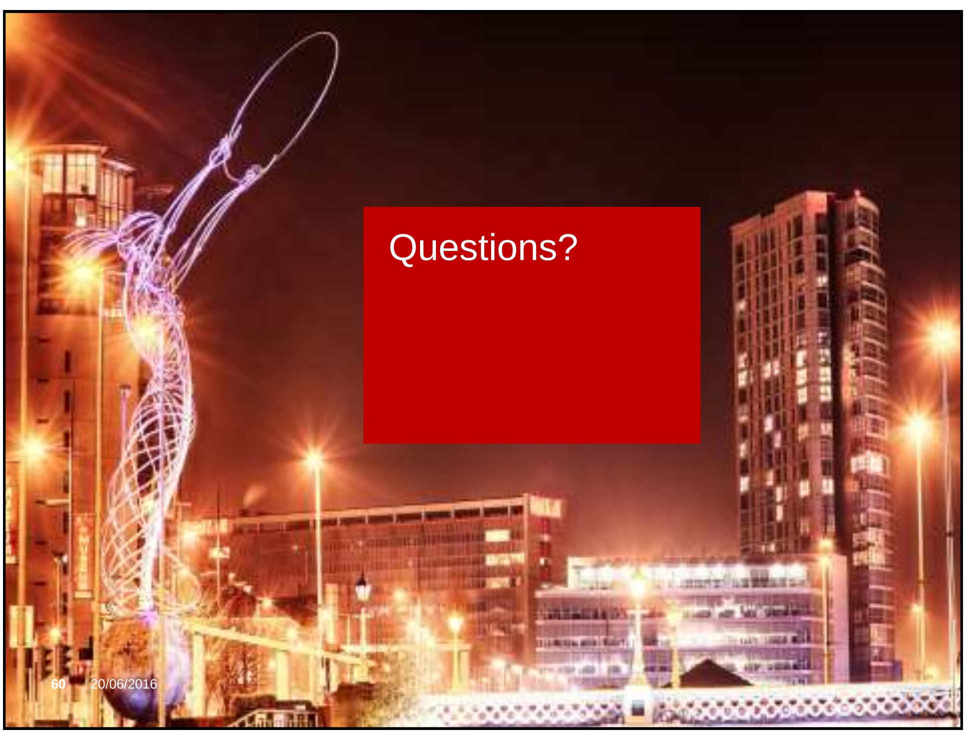
Related party Disclosure
- Disclose key management remuneration

Related Party Disclosure

Disclosure of key management personnel compensation

33.6 Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity. Compensation includes all **employee benefits** (as defined in Section 28 *Employee Benefits*) including those in the form of share-based payments (see Section 26 *Share-based Payment*). Employee benefits include all forms of consideration paid, payable or provided by the entity, or on behalf of the entity (eg by its parent or by a shareholder), in exchange for services rendered to the entity. It also includes such consideration paid on behalf of a parent of the entity in respect of goods or services provided to the entity.

33.7 An entity shall disclose key management personnel compensation in total.



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Example 1 – Government bond purchased at a discount.

Issuer	Coupon	Maturity	Price on 01/10/2014	Yield	Price on 01/10/2015	Yield	Current Price	Yield
Irish Government	4.40%	18/06/2019	118.51	1.43%	116.43	0.79%	114.41	0.40%

Purchased €1m nominal value at say December 2011 for 0.80 total cost €800,000.

- 30 September 2014 value 118.51,
- 30 September 2015 116.43,
- 30 September 2016 (say) €114.41

Accounting used by Credit Union

- Booked investment at cost of €800,000 in 2011 – no change booked to this in intervening period
- Booked coupon as income

What is the correction?

200,000 amortised over period from purchase to maturity in June 2020.

Amortised cost

€200,000 discount amortised over 104 months
2.6% (IRR)
Amortisation of discount December 2011 to 30 Sept. 2014 = €61,090
Amortisation of discount 30 Sept. 2014 to 30 Sept. 2015 = €22,657
Amortisation of discount 30 Sept. 2015 to 30 Sept. 2016 = €23,253
(See spread sheet calculation)

2015 journals

Dr Government bond investment	61,090 + 22,657
Cr retained earnings	61,090
Cr investment income	22,657

(note: book value at September 2015 is €954,675 and market value is €1.16m and therefore the value is not impaired)

2016 journals

Dr Government bond investment	23,253
Cr investment income	23,253

Closing balance on Government investment €907,000 (800,000+61,090+22,657+23,253) and market value is €1.14m.

Held to maturity option
Same answer as amortised cost because there was no impairment in the value.
Where there is no impairment, HTM and amortised cost give the same answer.

Fair value option (under IAS 39)

Cost	800,000
Market value at 1/10/2014	1,185,100 (385,100)
Market value at 30 September 2015	1,164,300 (-20,800)
Market value at 30 September 2016	1,144,100 (-20,200)

2015 journals

Dr Government bond investment	385,100 - 20800
Cr retained earnings	385,100
Dr Investment income	20,800

2016 journals

Cr Government bond investment	20,200
Dr Investment income	20,200

Corporate bonds purchased at a premium

Issuer	Coupon	Maturity	Issue Date	Price on 01/10/2014	Yield	Price on 01/10/2015	Yield
Bank of Ireland	3.25%	30/01/2019	15/01/2014	105.44	2.09%	106.33	1.61%

Purchased €1m nominal value at say December 2014 for 1.08, total cost €1,080,000.
- 30 September 2015 106.33,
- 30 September 2016 (say) €106.65

Accounting used by Credit Union
- Booked investment at nominal value €1,000,000 in December 2014 and expensed the premium of 80,000 at that date – no change booked to this in intervening period
- Booked coupon as income

		interest	0.0184	-235.56
Dec-14	1080000	1656	1078344	
Jan-15	1078344	1653.46	1076691	
Feb-15	1076691	1650.93	1075040	
Mar-15	1075040	1648.39	1073391	
Apr-15	1073391	1645.87	1071745	
May-15	1071745	1643.34	1070102	
Jun-15	1070102	1640.82	1068461	
Jul-15	1068461	1638.31	1066823	
Aug-15	1066823	1635.8	1065187	
Sep-15	1065187	1633.29	1063554	18446.2
Oct-15	1063554	1630.78	1061923	
Nov-15	1061923	1628.28	1060295	
Dec-15	1060295	1625.79	1058669	
Jan-16	1058669	1623.29	1057046	
Feb-16	1057046	1620.8	1055425	
Mar-16	1055425	1618.32	1053807	
Apr-16	1053807	1615.84	1052191	
May-16	1052191	1613.36	1050577	
Jun-16	1050577	1610.89	1048966	
Jul-16	1048966	1608.42	1047358	
Aug-16	1047358	1605.95	1045752	
Sep-16	1045752	1603.49	1044149	19405.2
Oct-16	1044149	1601.03	1042548	
Nov-16	1042548	1598.57	1040949	
Dec-16	1040949	1596.12	1039353	
Jan-17	1039353	1593.67	1037759	
Feb-17	1037759	1591.23	1036168	
Mar-17	1036168	1588.79	1034579	
Apr-17	1034579	1586.35	1032993	
May-17	1032993	1583.92	1031409	
Jun-17	1031409	1581.49	1029827	
Jul-17	1029827	1579.07	1028248	
Aug-17	1028248	1576.65	1026672	
Sep-17	1026672	1574.23	1025097	
Oct-17	1025097	1571.82	1023526	
Nov-17	1023526	1569.41	1021956	
Dec-17	1021956	1567	1020389	
Jan-18	1020389	1564.6	1018825	
Feb-18	1018825	1562.2	1017262	
Mar-18	1017262	1559.8	1015703	
Apr-18	1015703	1557.41	1014145	
May-18	1014145	1555.02	1012590	
Jun-18	1012590	1552.64	1011038	
Jul-18	1011038	1550.26	1009487	
Aug-18	1009487	1547.88	1007939	
Sep-18	1007939	1545.51	1006394	
Oct-18	1006394	1543.14	1004851	
Nov-18	1004851	1540.77	1003310	
Dec-18	1003310	1538.41	1001772	
Jan-19	1001772	1536.05	1000236	

80,000 amortised over period from purchase to maturity in January 2019.

Amortised cost

€80,000 premium amortised over 49 months
Adjustment to coupon Yield 1.84%
Amortisation of premium purchase to 30 Sept. 2015 = €16,446
Amortisation of premium 30 Sept. 2015 to 30 Sept. 2016 = €19,405
(See spread sheet calculation)

2015 journals

Dr Corporate bond investment	80,000-16446
Cr investment income	80,000-16446

note: book value at September 2015 is €1,063,554 and market value is €1,054,400m and therefore the value is impaired by €9,154. By December the value had recovered to c€1.08m again and no impairment was needed.

However, for the purposes of illustration, assume that the bond did not recover in value and an impairment of €9,154 was required:

Additional impairment journal for 2015

Cr Corporate bond investment	9,154
Dr Investment income	9,154

The impairment triggers a recalculation of the amortisation of premium using the new capital value of €1,054,400 down to 1m over the remaining 41 months to maturity – the adjustment is now:

	######	0.0150	270.582	
Sep-15	270.582	0.356523	1054400	
Oct-15	1054400	1386.29	1053012	
Nov-15	1053012	1386.47	1051625	
Dec-15	1051625	1384.64	1050241	
Jan-16	1050241	1382.82	1048858	
Feb-16	1048858	1381	1047477	
Mar-16	1047477	1379.18	1046098	
Apr-16	1046098	1377.36	1044720	
May-16	1044720	1375.55	1043345	
Jun-16	1043345	1373.74	1041971	
Jul-16	1041971	1371.93	1040599	
Aug-16	1040599	1370.12	1039229	
Sep-16	1039229	1368.32	1037861	16539.4
Oct-16	1037861	1366.52	1036494	
Nov-16	1036494	1364.72	1035129	
Dec-16	1035129	1362.92	1033766	
Jan-17	1033766	1361.13	1032405	
Feb-17	1032405	1359.33	1031046	
Mar-17	1031046	1357.54	1029688	
Apr-17	1029688	1355.76	1028333	
May-17	1028333	1353.97	1026979	
Jun-17	1026979	1352.19	1025627	
Jul-17	1025627	1350.41	1024276	
Aug-17	1024276	1348.63	1022927	
Sep-17	1022927	1346.85	1021581	
Oct-17	1021581	1345.08	1020236	
Nov-17	1020236	1343.31	1018892	
Dec-17	1018892	1341.54	1017551	
Jan-18	1017551	1339.78	1016211	
Feb-18	1016211	1338.01	1014873	
Mar-18	1014873	1336.25	1013537	
Apr-18	1013537	1334.49	1012202	
May-18	1012202	1332.73	1010869	
Jun-18	1010869	1330.98	1009538	
Jul-18	1009538	1329.23	1008209	
Aug-18	1008209	1327.48	1006882	
Sep-18	1006882	1325.73	1005556	
Oct-18	1005556	1323.98	1004232	
Nov-18	1004232	1322.24	1002910	
Dec-18	1002910	1320.5	1001589	
Jan-19	1001589	1318.76	1000271	

Previous amortisation €19,405
After impairment in 2015 it is now €16,539

2016 journals

	Dr Government bond investment	16,539
	Cr investment income	16,539

Closing balance on Government investment €1,037,861 (1,000,000+80,000-16446-9154-16539) and market value is €1,066,500. So the bond has recovered in value at the end of 2016 and a reversal of the 2015 impairment can be booked

Additional reversal of impairment journal for 2016

	Dr Corporate bond investment	9,154
	Cr Investment income	9,154

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Held to maturity option
Same answer as amortised cost without any adjustment for impairment and reversal of impairment. Where there is no impairment, HTM and amortised cost give the same answer.

Fair value option (under IAS 39)

Cost	1,0800,000
Market value at 30 September 2015	1,054,400 (-16,700)
Market value at 30 September 2016	1,063,300 (+8,900)

2015 journals

Cr Government bond investment	16,700
Dr Investment income	16,700

2016 journals

Dr Government bond investment	8,900
Cr Investment income	8,900

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