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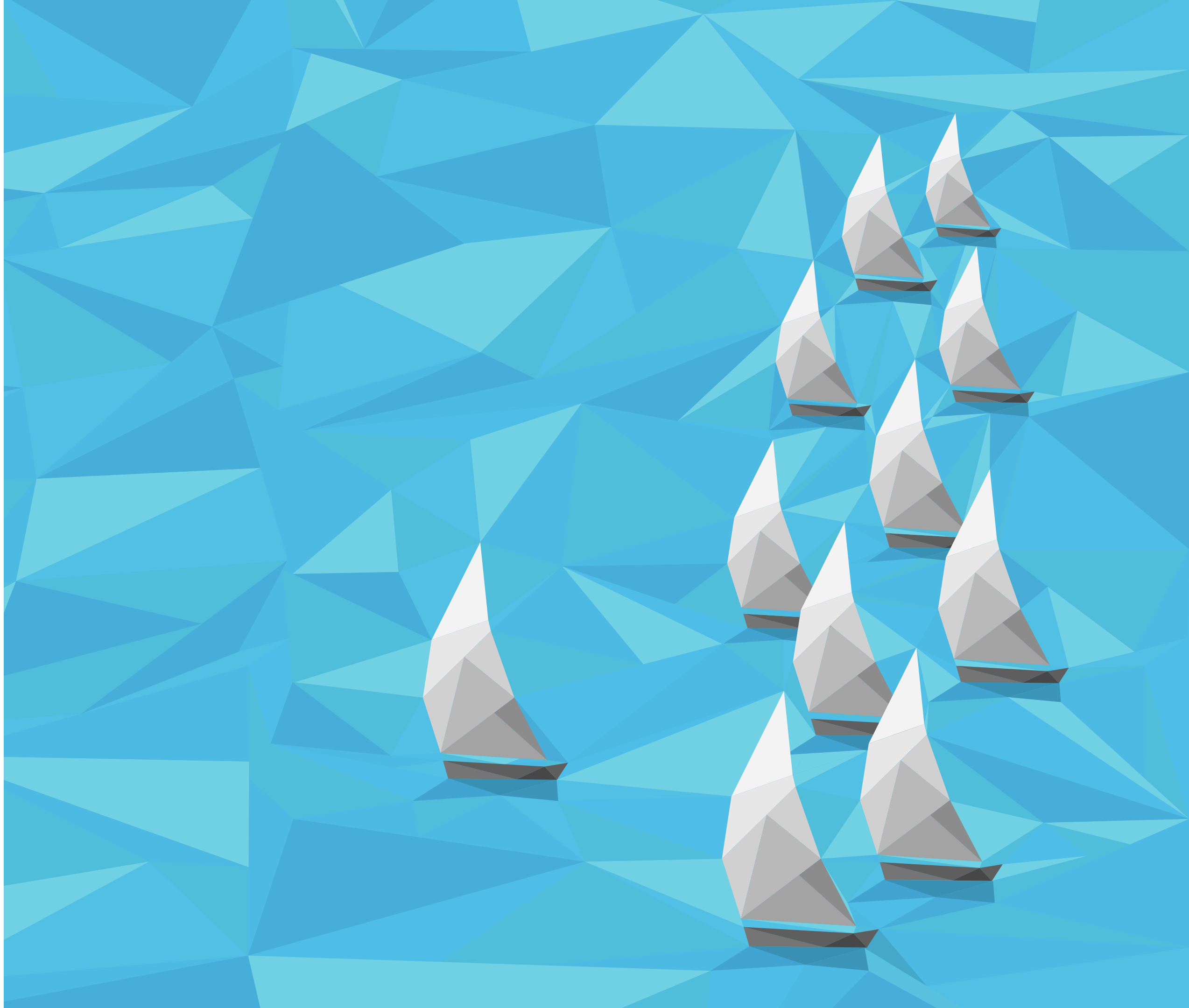
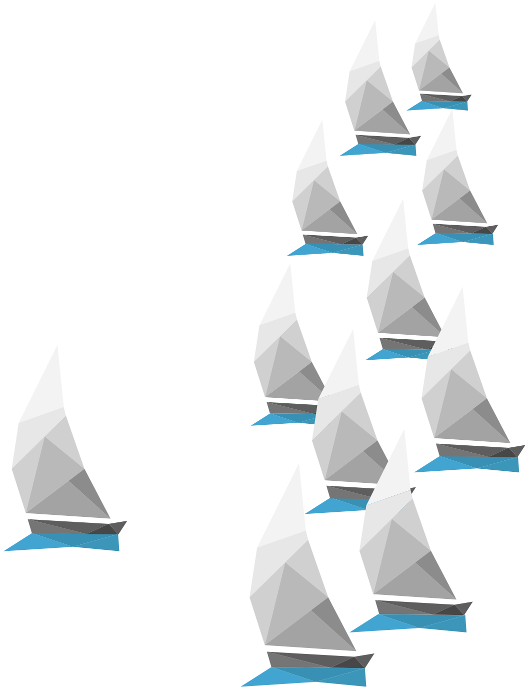
Annual Financial Reporting Seminar
The Winds of Change



Tuesday 21 October 2014

Convention Centre Dublin

The New Irish GAAP



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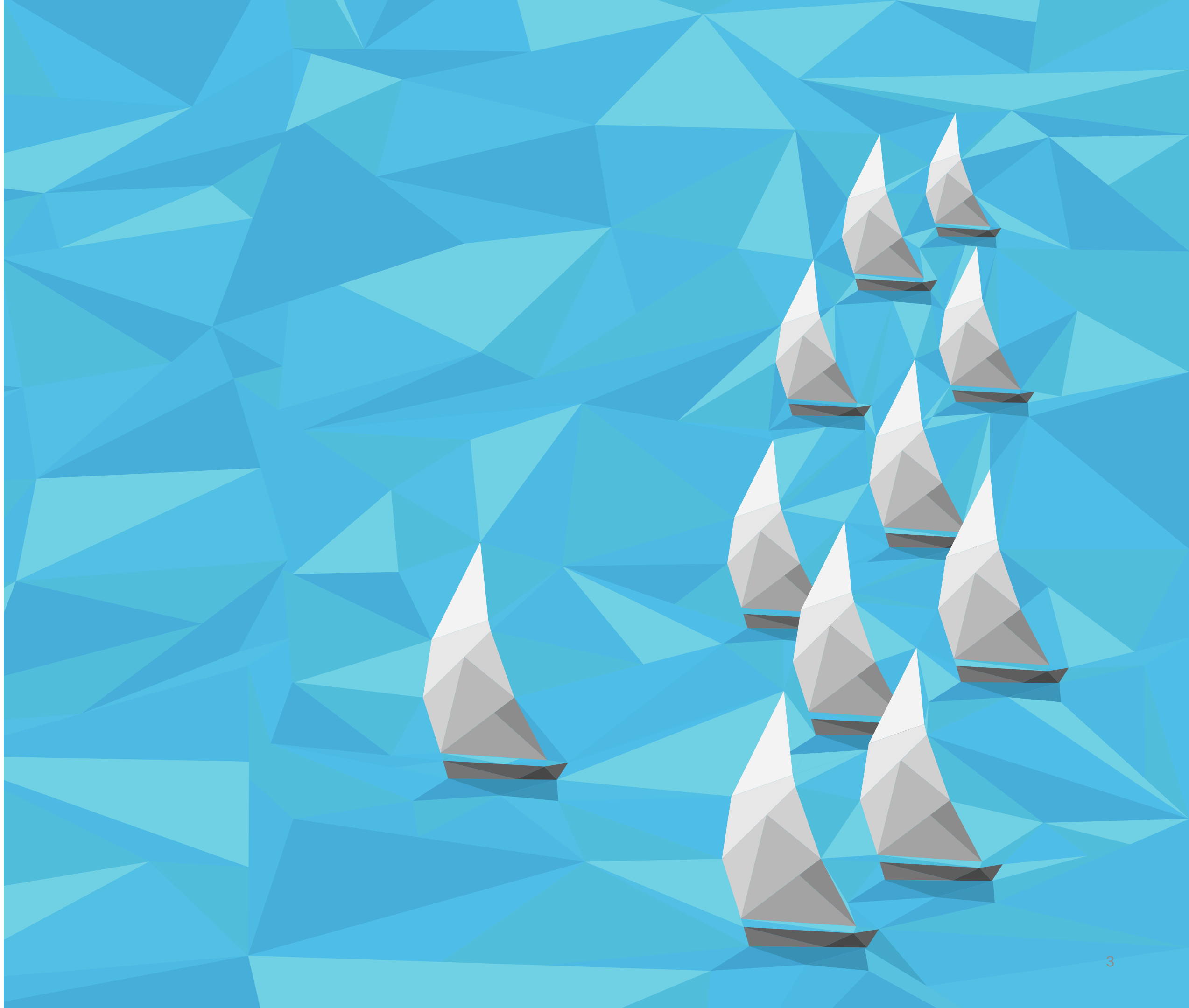
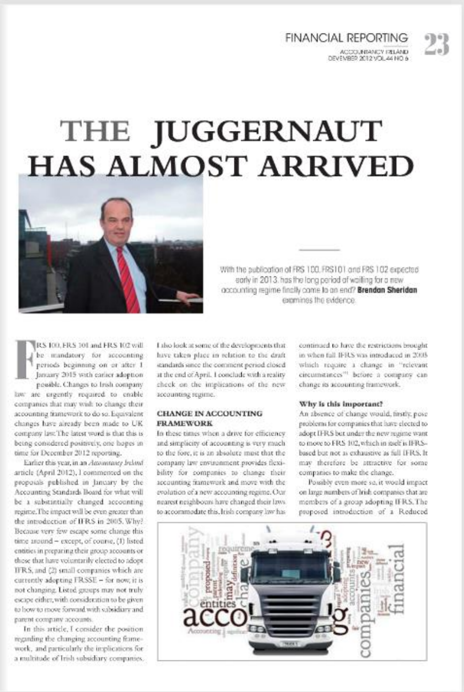
The New Standards:
A Recap & Implementing Change

Glenn Gillard
National Technical Partner
&
Emer O'Shaughnessy
Audit Partner



The New Irish GAAP



FINANCIAL REPORTING 23
ACCOUNTANCY IRELAND
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THE JUGGERNAUT HAS ALMOST ARRIVED

With the publication of FRS 100, FRS101 and FRS 102 expected early in 2013, has the long period of waiting for a new accounting regime finally come to an end? **Brendan Sheridan** examines the evidence.

FRS 100, FRS 101 and FRS 102 will be mandatory for accounting periods beginning on or after 1 January 2015 with earlier adoption possible. Changes to Irish company law are urgently required to enable companies that may wish to change their accounting framework to do so. Equivalent changes have already been made to UK company law. The latest word is that this is being considered positively, one hopes in time for December 2012 reporting.

Earlier this year, in an *Accountancy Ireland* article (April 2012), I commented on the proposals published in January by the Accounting Standards Board for what will be a substantially changed accounting regime. The impact will be even greater than the introduction of IFRS in 2005. Why? Because very few escape some change this time around – except, of course, (1) listed entities in preparing their group accounts or those that have voluntarily elected to adopt IFRS, and (2) small companies which are currently adopting FRSSE – for now, it is not changing. Listed groups may not truly escape either, with consideration to be given to how to move forward with subsidiary and parent company accounts.

In this article, I consider the position regarding the changing accounting framework, and particularly the implications for a multitude of Irish subsidiary companies. I also look at some of the developments that have taken place in relation to the draft standards since the comment period closed at the end of April. I conclude with a reality check on the implications of the new accounting regime.

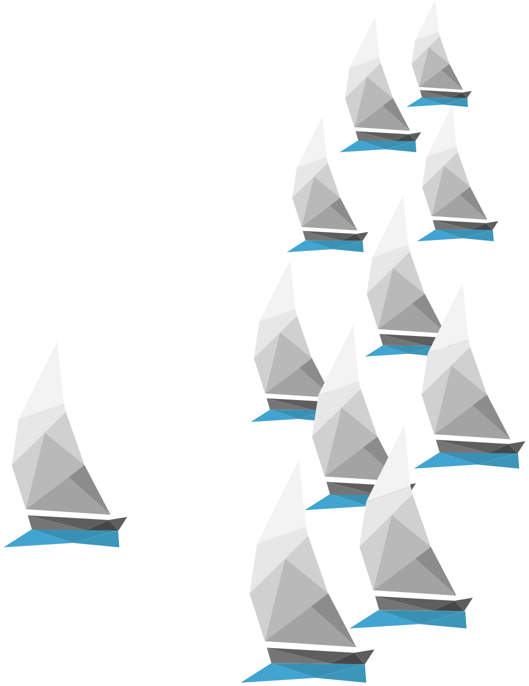
CHANGE IN ACCOUNTING FRAMEWORK

In these times when a drive for efficiency and simplicity of accounting is very much to the fore, it is an absolute must that the company law environment provides flexibility for companies to change their accounting framework and move with the evolution of a new accounting regime. Our nearest neighbours have changed their laws to accommodate this. Irish company law has continued to have the restrictions brought in when full IFRS was introduced in 2005 which require a change in "relevant circumstances"[1] before a company can change its accounting framework.

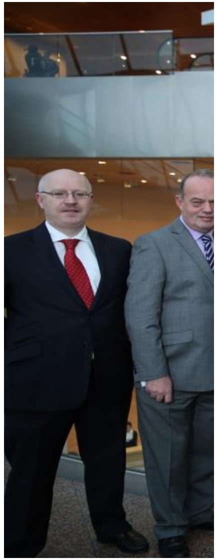
Why is this important?

An absence of change would, firstly, pose problems for companies that have elected to adopt IFRS but under the new regime want to move to FRS 102, which in itself is IFRS-based but not as exhaustive as full IFRS. It may therefore be attractive for some companies to make the change.

Possibly even more so, it would impact on large numbers of Irish companies that are members of a group adopting IFRS. The proposed introduction of a Reduced



The New Irish GAAP



TO LEAD OR TO FOLLOW? THE TRANSITION TO NEW ACCOUNTING STANDARDS

Transition date is just around the corner! If you haven't already begun planning how to meet the challenges of moving to a new accounting framework, it's time to start sorting out what it means for you. **Brendan Sheridan** provides some guidance.

Entities will have a choice of framework between FRS 102 and IFRS and some may also have a choice of FRSSE or, indeed, FRS 101. A recent Deloitte survey of CFOs of Irish entities indicated that almost 60% of those surveyed had not decided on which accounting framework to use from 2015 onwards.

It is likely that the vast majority of Irish entities will be implementing FRS 102, the new *Financial Reporting Standard Applicable in the UK and Republic of Ireland* for periods beginning on or after 1 January 2015. Comparatives will be required and for calendar year end reporters this means transition date is 1 January 2014. If an entity is new, why bother with current Irish standards? If it is an existing company, why not meet the challenge head on and lead the way?

Insurers await completion of FRS 103, with implementation also intended for 2015.

LESS INK FOR SOME!

For IFRS groups, why not avail of the advantages of the FRS 101 'Reduced Disclosure Framework' and eliminate those page-filling disclosures in the parent only and subsidiary financial statements? While the conditions for being a 'qualifying entity', as defined in the standard, will have to be met, the ability to do this may extend to groups preparing financial statements other than under IFRS, where they meet certain conditions. Most people know that little or no value is to be gained from those copious disclosures in such areas as financial instruments and share-based payment. A reduced disclosure framework is also available for 'qualifying entities' under FRS 102.

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April 2013

DRAMATIC CHANGES IN ACCOUNTING FOR INTERCOMPANY LOANS

Under FRS 102 complex accounting may be required for simple intercompany loans as **Oliver Holt** explains.

Under FRS 4 *Capital Instruments* accounting for an intercompany loan was fairly straightforward. The loan was booked on initial recognition at the amount of the net proceeds (fair value of consideration less issue costs), usually with mirror treatment in both sets of books. Thereafter, the finance costs of the debt were allocated to periods over the term of the debt at a constant rate on the carrying amount. In many cases as the loan was interest free there was no further accounting until the loan was repaid.

Depending on the terms and conditions of an intercompany loan the change in accounting under FRS 102 can be dramatic. This will come as no surprise to entities that have previously grappled with the transition to IFRS where initial accounting at fair value of the debt instrument as opposed to the consideration is well established under IAS 39.

Under section 11 of FRS 102 a reporting entity has a choice of recognition and measurement rules for its financial instruments being the relevant rules in either:

- Sections 11 and 12 of FRS 102; or
- IAS 39; or
- IFRS 9 and/or IAS 39 as amended following publication of IFRS 9.

This choice once made applies to all the entity's financial instruments and it is not possible to cherry pick among these rules for different financial instruments. In each case, the disclosure rules in sections 11 and 12 apply and if the entity is a financial institution as defined in FRS 102, section 34 disclosure rules also apply.

Table 1: Rules for Preference Shares and Other Debt Instruments

FRS 102 classification	Debt in the form of: Preference shares		Other debt instrument
	Holder's accounting treatment (FRS 102.11.14(d)(i))	*Issuer's accounting treatment*	*Holder and issuer's accounting treatment*
Basic (section 11)	FVTPL	Amortised cost	Amortised cost
Non-basic (section 12)	FVTPL	FVTPL	FVTPL

For the purpose of this article we will assume the reporting entity has chosen FRS 102's section 11 and section 12 for its financial instrument recognition and measurement rules. While the measurement rules for amortised cost discussed in the article apply to loans generally that are basic and accounted for at amortised cost, this article will focus on intercompany loans.

As intercompany loans fall within the definition of a financial instrument the starting point is to determine whether the instrument is required to be classified as basic or non-basic. Section 11 of FRS 102 indicates that many intercompany arrangements will be basic but it should not be assumed that this will always be the case – for example a convertible debt instrument is classified as non-basic for the holder. Classification as basic or non-basic is based on a set of rules rather than on any over-arching principle. Note also that FRED 54 (February 2014) proposes to broaden the range of instruments that will fall into the 'basic' category.

The classification matters. For debt instruments only those classified as basic can be accounted for at amortised cost under section 11. Note that debt instruments can be at FVTPL if designated as such on initial recognition. Non-basic debt instruments fall into section 12 of FRS 102 and are generally dealt with at fair value with changes in fair value reflected in profit or loss (FVTPL). Measuring at fair value is more onerous than measurement at amortised cost because it requires a valuation to be obtained at each reporting date and also introduces volatility into profit or loss.

It should be noted that there are different rules for preference shares and for other debt instruments as illustrated in *Table 1*.

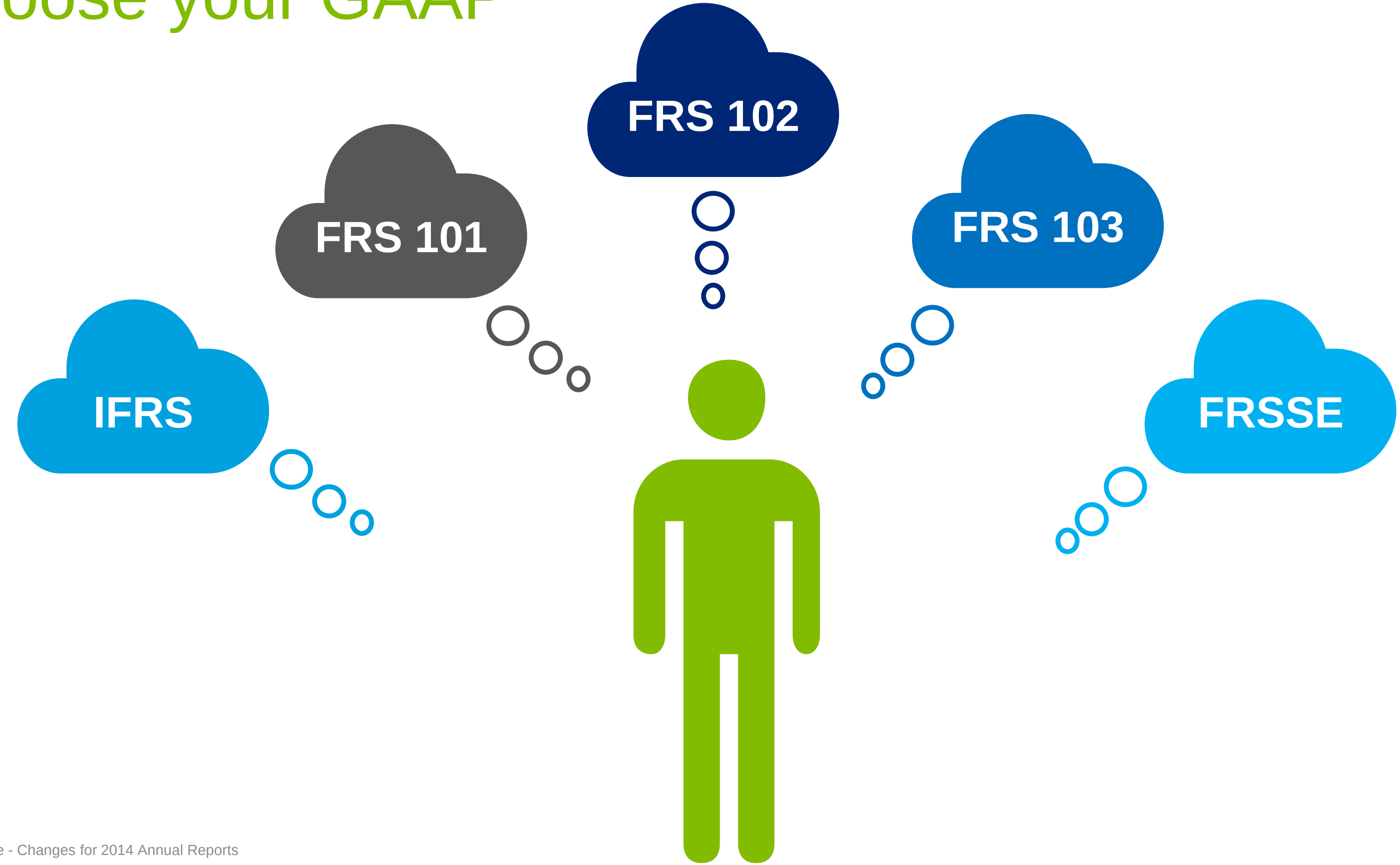
Where basic preference shares are accounted for differently by the holder in the group from the issuer the consolidation adjustments necessary to eliminate the intercompany loan are more complex.

INTERCOMPANY LOANS AT AMORTISED COST

On initial recognition, as an intercompany loan is a financing transaction, FRS 102 section 11 requires that it is measured at the present value of future cash flows. The standard requires use of the market rate of interest for a similar debt instrument at the

The New GAAP Quiz

Choose your GAAP



Answer 1

FRS 102 must be implemented for accounting periods beginning on or after 1 January 2015.

TRUE

The three new standards, FRS 100-102, come into mandatory force for periods beginning on or after 1 January 2015, with comparatives required for periods beginning on or after 1 January 2014.

Answer 2

Implementation of FRS 102 earlier than 2015 is not permitted.

FALSE

Yes, any entity with a financial period ending on or after 31 December 2012 may adopt FRSs 100-102 in advance of their mandatorily effective date (period commencing 1 January 2015).

Answer 3

On implementation, balance sheets for three years are required in the first financial statements.

FALSE

A third balance sheet is not required to be presented at the beginning of the comparative period

Answer 4

All entities listed on the Irish Stock Exchange are required to prepare financial statements in accordance with full IFRS.

FALSE

Groups that are currently required to apply IFRS as adopted in the EU will continue to be required to apply IFRS, either under law or under the rules of the respective Stock Exchange in their group financial statements. The parent company financial statements may be prepared under IFRS, FRS102, or FRS 101, subject to certain conditions.

Listed companies that are not group holding companies may elect to prepare their financial statements under IFRS, FRS102, or FRS 101, subject to certain conditions.

Answer 5

FRS 101 may only be availed of by companies where the holding company and group financial statements are prepared using IFRS.

FALSE

There is no requirement, if using FRS101, for the group financial statements into which the entity is consolidated to be prepared under IFRS. They could be prepared under, for example, US GAAP or Japanese GAAP.

Some of the disclosure reductions are only available if ‘equivalent’ disclosures are made in the consolidated financial statements.

Answer 6

FRS 101 accounts are considered ‘Companies Act Accounts’.

TRUE

Because of the reduced disclosure requirements, financial statements prepared under FRS 101 are ‘Companies Act accounts’ as they are not prepared in accordance with IFRS. They are therefore subject to the requirements of Irish Company law, with regard to both format/presentation and certain disclosure requirements.

Answer 7

Various disclosure exemptions, including those on financial instruments and capital management, are available to all ‘qualifying entities’.

FALSE

A range of disclosure exemptions are available to ‘qualifying entities’ under both FRS 101 and FRS 102. The exemptions from financial instrument and capital management disclosures are not available to a ‘financial institution’ which is defined in the standards.

Answer 8

In a group of companies, it is acceptable practice for some to adopt FRS 101 while others adopt FRS 102.

TRUE

Financial statements prepared in accordance with either FRS 101 or FRS 102 both constitute Companies Act accounts, so both may be used by different companies within a group without recourse to the ‘good reasons’ exception.

Answer 9

SORPs in such areas as charities and pension schemes will no longer be relevant.

FALSE

The majority of SORPs will remain in use and work is in progress to update them in line with FRS 102.

Certificate of GAAP knowledge

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Answer 10

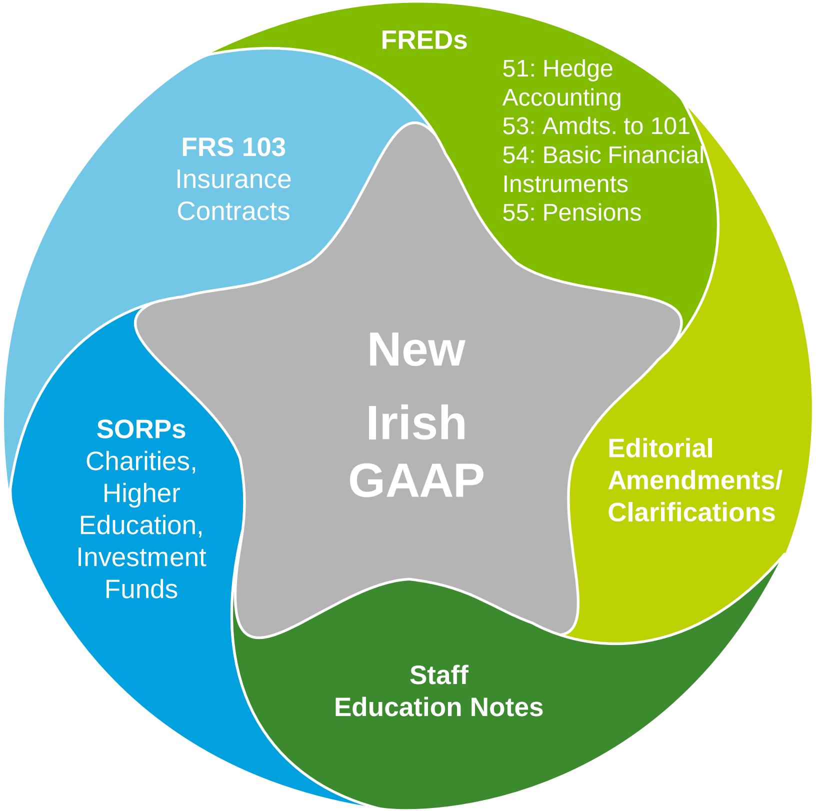
If there is an objection to the use of FRS 101, and its disclosure exemptions, by more than 25% of total shareholders or 50% of any minority shareholders, a company cannot adopt FRS 101.

FALSE

The reduced disclosure framework in FRS 101 or the exemptions in FRS 102 are available if certain requirements are met, including (a) no more than 5% of shareholders or 50% of minority shareholders object (b) the company must be a ‘qualifying entity – a member of a group where consolidated financial statements are prepared and are publicly available for inspection, (c) the company must disclose details of its exemption in its financial statements

Developments 2013/2014

Developments in Past Year



The Tax Impact

Starting point Profit Before Tax (PBT)

- On-going compliance
- Transition

Transition

- Double counting
- Amounts dropping out

Schedule 17A

Schedule 17A – Taxable amount – Profits drop out

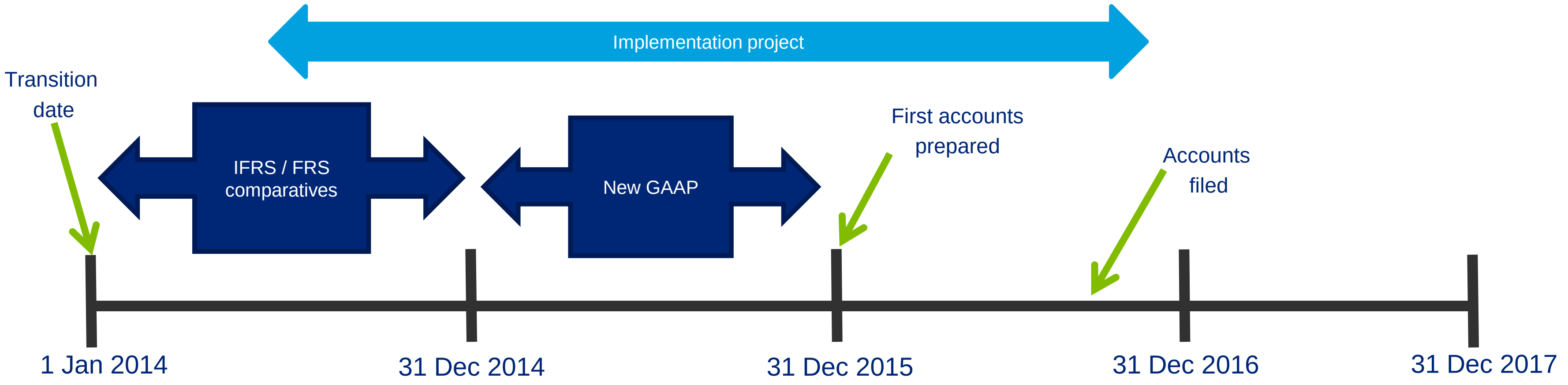
Schedule 17A - Taxable amount - profits dropped out	
Cost of financial instrument during FY1	100,000
Fair value at end of FY1	130,000
Instrument Sold in FY2	150,000

- FY1 - accounts prepared under Irish GAAP and taxed on a realised basis
- FY2 - accounts prepared under IFRS and taxed in line with accounting profits
- In FY2, the company will be taxed on FV movement of €20k
- Profits of €30k will drop out
- 30k will be spread over 5 years commencing in FY2

Transition to New GAAP

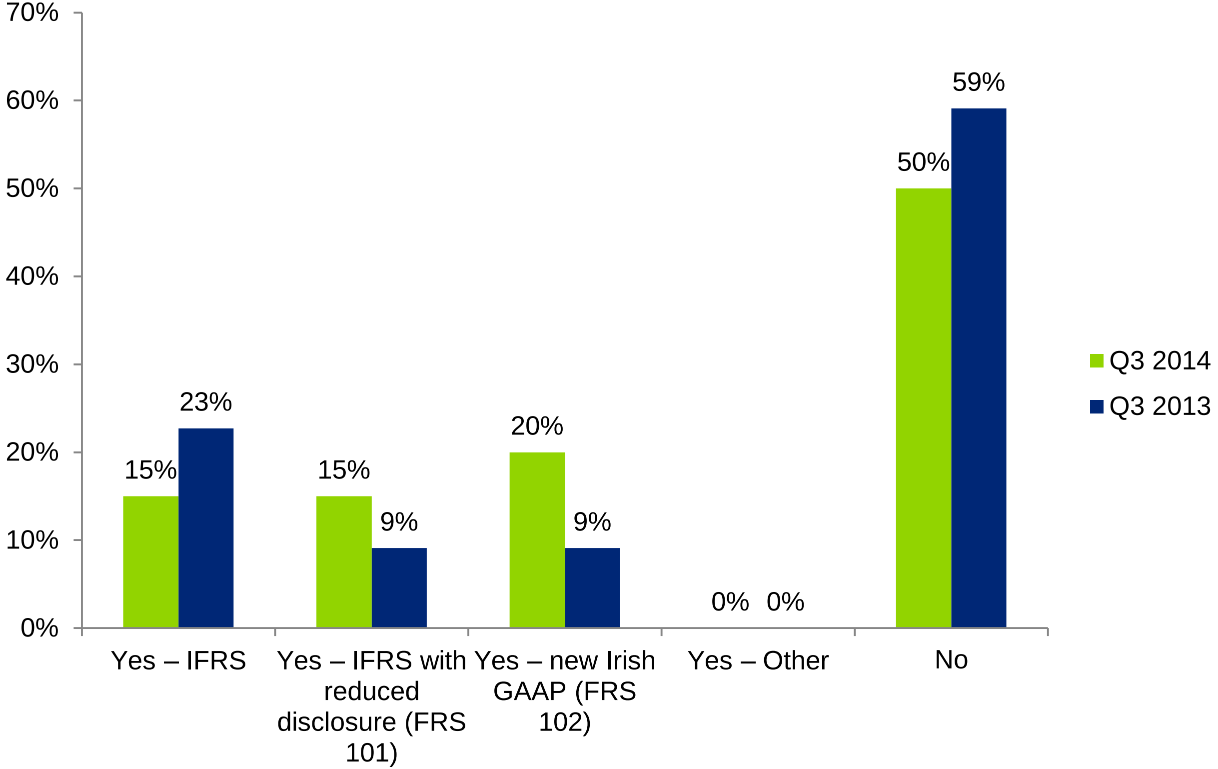
Conversion timeline for a December year end company

Adopt for year ending 31 December 2015



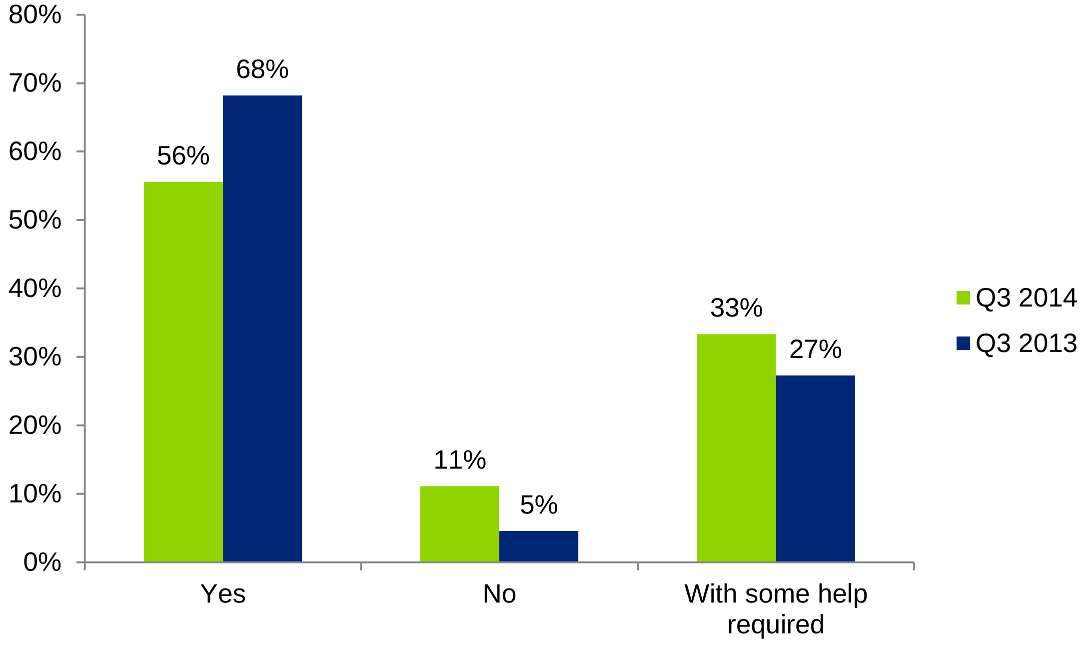
CFO Survey Q3 – Choosing your GAAP

1. Has your Board of Directors decided which accounting framework to adopt for 2015 and beyond?



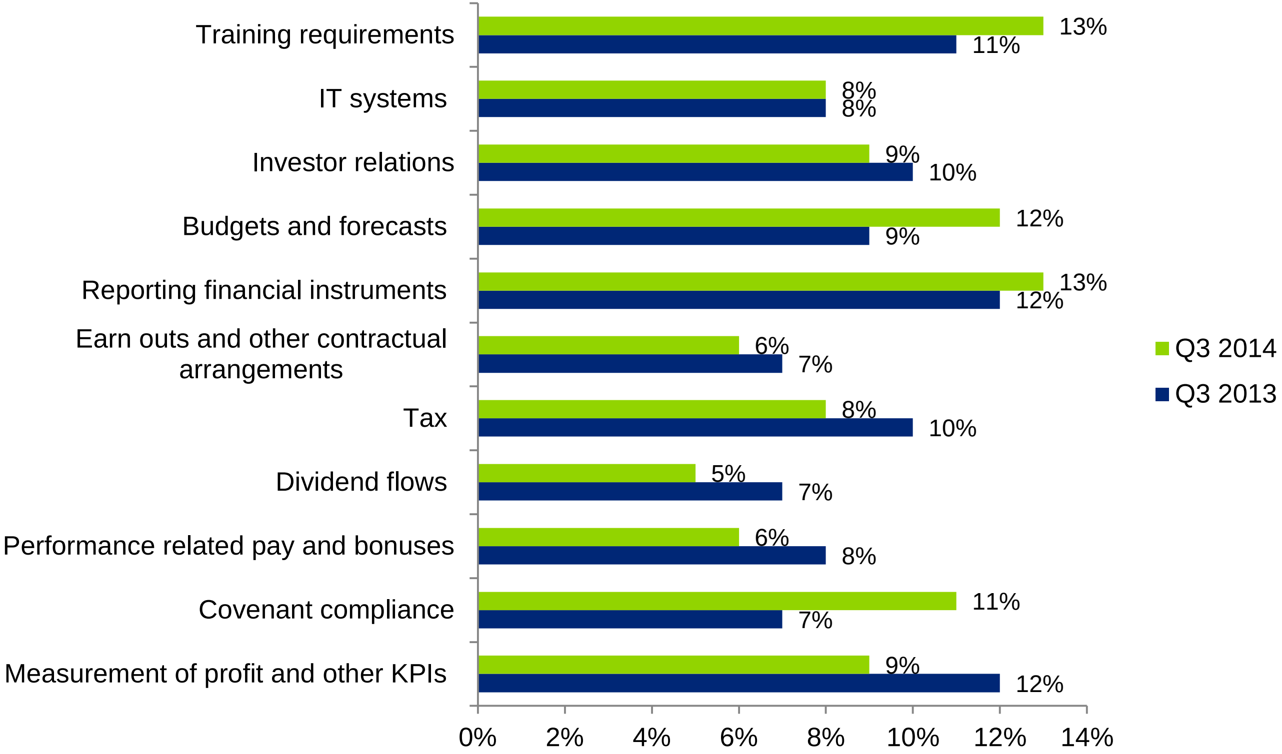
CFO Survey Q3 – Resources

2. Given the highly detailed nature of the work including but not limited to research into past transactions required to transition from one accounting framework to another do you consider that your current financial reporting resources within the finance function are adequate to ensure a smooth transition?



CFO Survey Q3 – Areas of Concern

3. Do you think that the choice of framework has the potential to adversely impact on the business:



Transition phases

Phase 1 – **Planning & scoping**

Phase 2 – **Assessment & GAAP analysis**

Phase 3 – **Embed in monthly procedures**

Phase 4 – **Drafting financial statements**

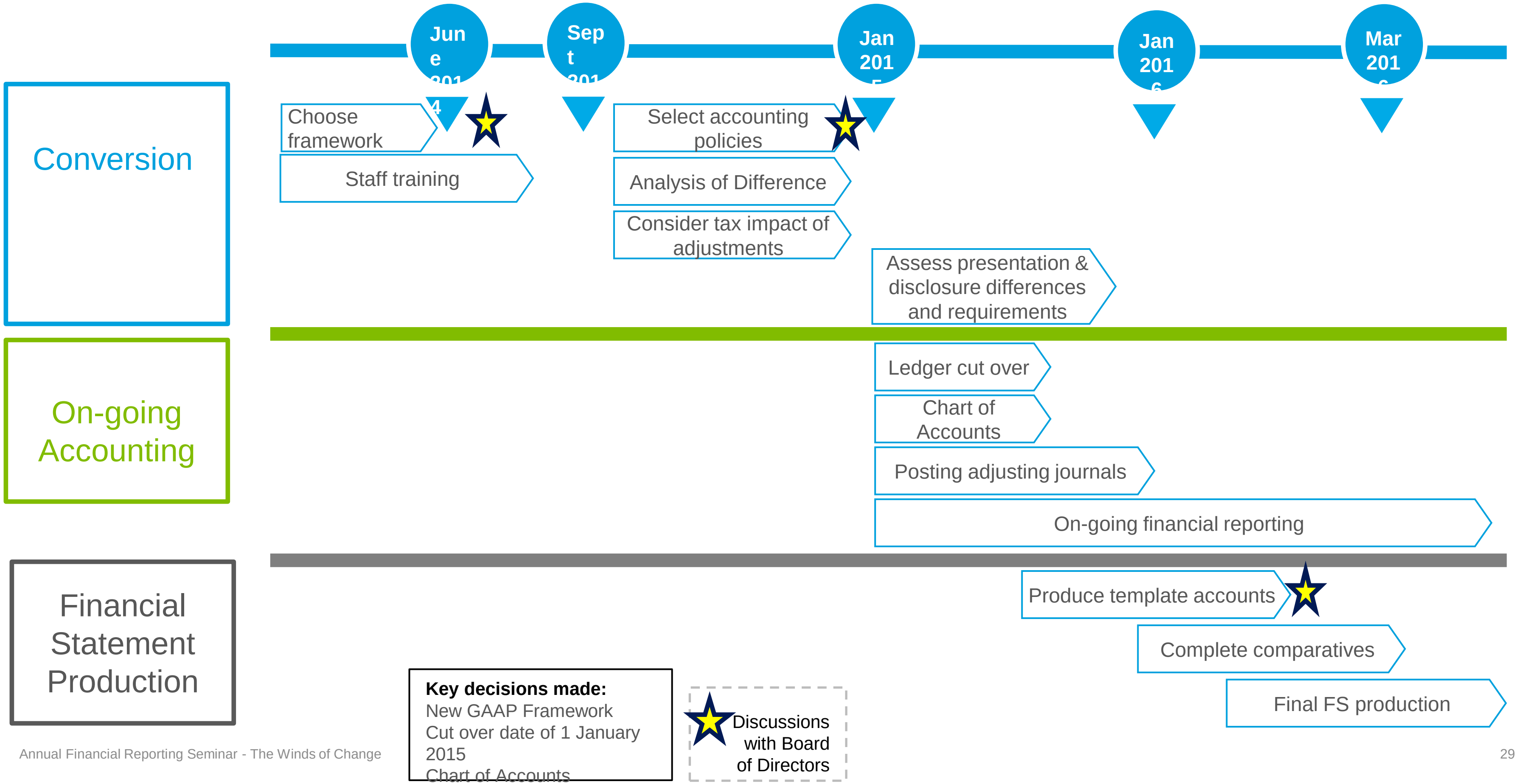
Phase 5 – **Sustain**

Analyse the implications of new GAAP adoption, identify potential opportunities, and develop an approach to phased adoption where it makes sense.

Develop a detailed approach to adoption and execute implementation.

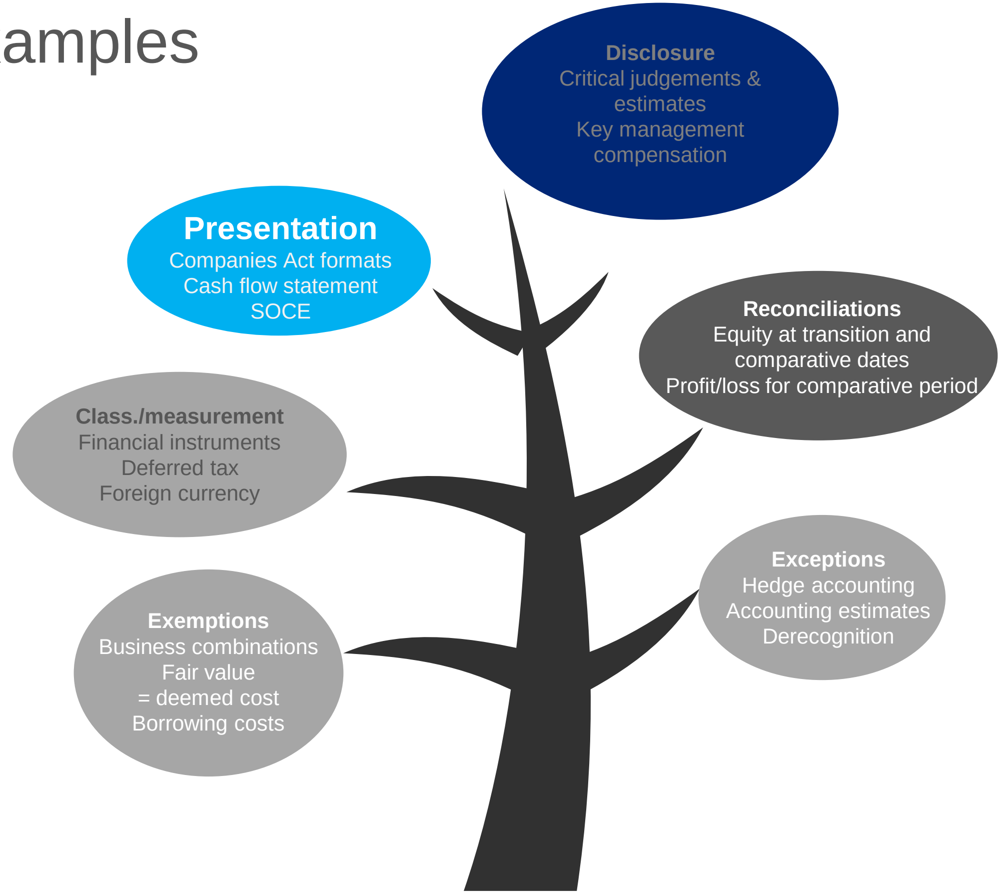
Complete and sustain "business as usual" reporting.

New GAAP Implementation - Project plan



Key areas of focus

Some examples



Some Key Questions for Directors

? Which accounting framework is most suitable to company's circumstances?

? Can the current accounting systems support a revised chart of accounts?

? Might this be the time to simplify group structures?

? Will a different GAAP impact on the ability of group companies to pay dividends up through the group?

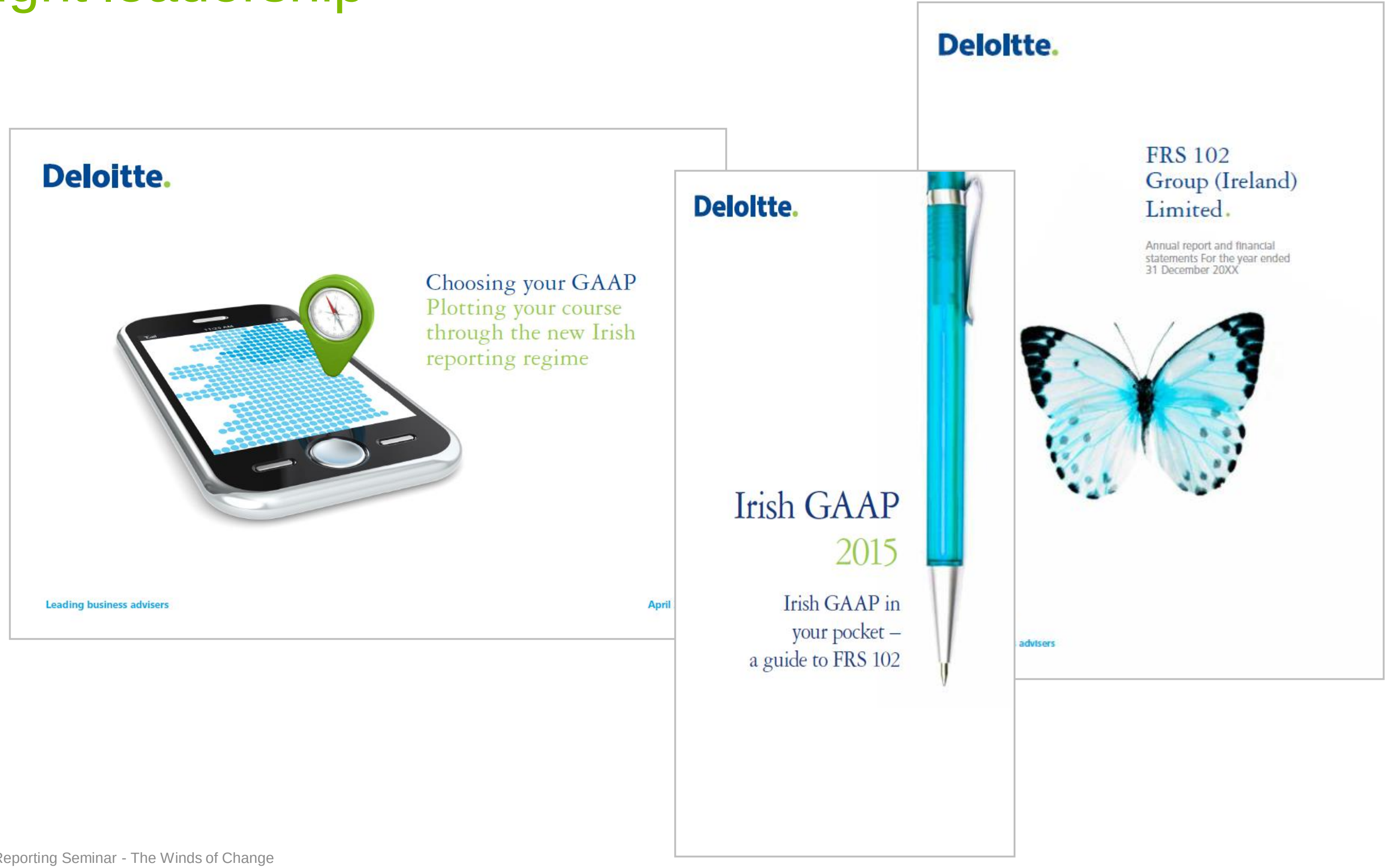
? Does the company have sufficient skills in-house to manage conversion?

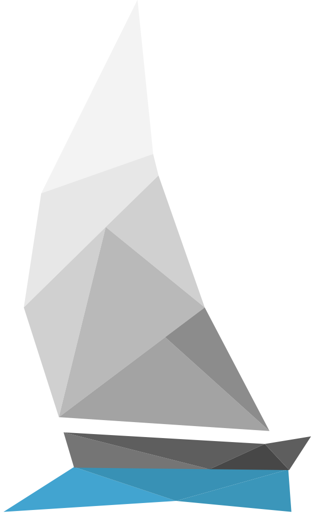
? What are the likely impacts on the company's tax cash costs?

? Will derivatives and hedge accounting require additional focus?

? Will changes affect key metrics e.g. loan covenants, earn outs and remuneration schemes?

Thought leadership





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