

Need to know

FRC consults on changes to accounting standards as a result of implementation of the EU Accounting Directive



In a nutshell

- The FRC has published three financial reporting exposure drafts (FREDs) proposing changes to the existing UK financial reporting framework resulting from the UK implementation of the EU Accounting Directive.
- FRED 58 introduces a separate, simplified standard for micro-entities.
- FREDs 59 and 60 amend FRSs 100, 101 and 102 to introduce a new regime for small companies and make other consequential amendments to the standards resulting from the changes to UK company law. The FRSSE will be withdrawn once these amendments are approved.
- The proposed new standard and amendments, once finalised, will be effective for accounting periods beginning on or after 1 January 2016 with earlier application permitted subject to some restrictions.
- The FRC is requesting comments on the FREDs by 30 April 2015.

Background

In September 2014 the FRC consulted on the future of accounting standards for micro-entities, small entities and other amendments to accounting standards necessary as result of the UK implementation of the EU Accounting Directive. This followed a consultation issued by the Department for Business, Innovation and Skills (BIS) on the implementation of the Directive, which sought to consolidate existing legislation on financial reporting and reduce the regulatory burden on smaller companies. Deloitte's *Need to know*, issued in September 2014, provides further background on this consultation process.

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The following FREDs have now been issued by the FRC for public comment:

- FRED 58 – Draft FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*;
- FRED 59 – Draft amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland – Small entities and other minor amendments*; and
- FRED 60 – Draft amendments to FRS 100 *Application of Financial Reporting Requirements and FRS 101 Reduced Disclosure Framework*.

The FREDs take into account the feedback from the previous consultation and are consistent with the requirements outlined in the draft *Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015*, which implement the Accounting Directive in the UK. These Regulations have been laid before Parliament and are expected to be debated and approved in due course, coming into force on 6 April 2015.

When would the revised requirements apply?

Once finalised, the new standard proposed by FRED 58 would apply to entities that are eligible to apply the micro-entity regime in law for accounting periods beginning on or after 1 January 2016, with earlier application permitted.

The amendments set out in FRED 59 and 60, if finalised, would be effective for accounting periods beginning on or after 1 January 2016, with early adoption permitted for periods beginning on or after 1 January 2015 to be consistent with changes in relevant legislation.

Observation

Early adoption may be attractive to some companies to avoid having to make changes in two consecutive years. In particular, some companies may be able to benefit from the increased thresholds for the small companies regime in 2015. They would also be able to avoid having to apply the existing FRS 102 for one year and instead move directly to the new regime for small companies within the revised FRS 102.

What are the changes proposed in these exposure drafts?

FRED 58 – a new standard for micro entities

Draft FRS 105 is a single financial reporting standard that will apply to entities that qualify as micro-entities as defined by the Companies Act 2006 (the Act) and choose to apply the micro-entities regime. The regime was originally introduced into UK company law in November 2013 following new EU legislation. At that time, the FRC amended the *Financial Reporting Standard for Smaller Entities* (FRSSE), enabling eligible micro-entities to state compliance with accounting standards. However, this was always seen as a temporary solution.

The draft FRS includes the presentation and disclosure requirements of the regime as set out in law. The recognition and measurement requirements are based on FRS 102 but with significant simplifications. The key amendments from FRS 102 are:

- to remove recognition and measurement options that are not available to micro-entities by law e.g. revaluations of property plant and equipment, intangible assets, and fair value accounting for investment property and financial instruments;
- to remove all disclosure requirements other than those required by law; and
- to exempt micro-entities from having to account for some complex transactions such as equity settled share based payments, defined benefit pension schemes and deferred tax, and to simplify requirements for some complex transactions where an alternative accounting treatment is available and would provide relevant and reliable information to users of the financial statements.

If transactions are not addressed by the draft FRS, a micro-entity is not required to refer to FRS 102 in selecting its accounting policies. A micro-entity may provide voluntary disclosures beyond those required by the draft FRS.

FRED 59 – revised accounting requirements for small entities

This FRED sets out the revised presentation and disclosure requirements for financial reporting by small entities in a new section of FRS 102, Section 1A *Small Entities*. Taken together with the recognition and measurement requirements of the rest of the standard, this will replace the existing FRSSE. The information to be presented and disclosed in the financial statements of a small entity is consistent with the new small companies regime within company law. From the effective date of these amendments, the FRSSE will be withdrawn.

The amendments are consistent with the draft *Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015*. The draft Regulations, once finalised, will increase the headroom on the qualifying requirements for small companies. The changes are summarised in the table below.

	Old Criteria	New Criteria
Total assets	<£3.26m	<£5.1m
Turnover	<£6.5m	<£10.2m
Number of employees	<50	<50

A company is small for accounting purposes if it meets two of the new criteria although other eligibility criteria must also be considered. These have been relaxed so that companies in the same group as an unlisted PLC are no longer ineligible although PLCs themselves continue to be ineligible. BIS is consulting separately on whether the increased thresholds will apply for the purposes of exemption from audit. The thresholds relating to micro-entities remain unchanged by these draft regulations.

The FRED also proposes a small number of other amendments necessary to maintain consistency between FRS 102 and company law.

Observation

The recognition and measurement requirements of FRS 102, particularly on financial instruments and share-based payments, will be challenging for many small companies. Those that qualify as micro entities may wish to consider adopting the much simplified regime in FRS 105. For entities that are not small, most of the changes proposed by FRED 59 are minor and technical.

FRED 60

This FRED proposes amendments to FRS 100 to reflect the revised framework of accounting standards, including the proposed replacement of the FRSE with a new section in FRS 102 and the proposed introduction of micro-entity accounting standard, draft FRS 105.

The FRED also proposes minor amendments to FRS 101 to maintain consistency between FRS 101 and company law.

Observation

The proposal to make use of new flexibility in company law to permit the use of formats based on IAS 1 for the balance sheet and income statement of companies using FRS 101 and hence IFRS-based accounting policies is particularly welcome. More surprisingly, the FRC is proposing also to extend this flexibility to financial statements prepared under FRS 102.

Further information

If you have any questions about the subjects raised in this publication, please speak to your usual Deloitte contact. More information on the proposed changes to the existing UK financial reporting framework, as well as other UK accounting, reporting and corporate governance news and publications, can be found at www.ukaccountingplus.co.uk

The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015 laid before Parliament can be accessed at: www.legislation.gov.uk/ukdsi/2015/978011127896

The FREDs published by the FRC can be found at: www.frc.org.uk

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