

The proposed **changes to UK GAAP** would affect many **listed groups**, and introduce new options for **subsidiaries**

What is happening?

The Accounting Standards Board has proposed replacing existing UK GAAP with a new differential reporting framework based on public accountability. Under the proposals, all companies considered publicly accountable will be required to apply EU-adopted IFRS. The definition includes companies with either debt or equity instruments listed on any exchange, anywhere.

Companies which are not publicly accountable will apply the Financial Reporting Standard for Medium-sized Entities (FRSME), which is proposed as a new UK standard based closely on the IFRS for SMEs. Alternatively, they could opt to apply EU-adopted IFRS.

This factsheet focuses on the likely impact for listed groups, and on the choices which may be available to their subsidiaries.

When will these changes happen?

The new framework is currently planned to be effective for accounting periods beginning 1 July 2013. However, it is likely to be available for early adoption when the final standard is released. The aim is that the standard will be published by the end of 2011. The introduction of the new framework may bring advantages for listed groups, and therefore early adoption could be an issue for serious consideration.

What would the impact be on the group accounts?

Where the group is listed, it would be publicly accountable and therefore the group accounts would need to be prepared in accordance with EU-adopted IFRS. As the group accounts of companies listed on the London Stock Exchange or AIM are already required to be prepared under EU-adopted IFRS, this will not represent a change.

What about parent company individual accounts?

Currently, many parent company individual accounts continue to be prepared under UK GAAP, although those listed on the London Stock Exchange are required to adopt **FRS 26 Financial Instruments: Recognition and Measurement** and the associated IFRS-converged standards.

Under the proposals, a listed parent will be publicly accountable and it will be required to apply EU-adopted IFRS in its individual accounts.

Highlights

The proposed new UK GAAP framework will have a number of impacts on listed groups:

- the parent company will have to use EU-adopted IFRS
- subsidiaries may have a choice between FRSME and EU-adopted IFRS, and could benefit from disclosure exemptions
- numerous factors will influence the choices to be made.

What about my subsidiaries?

Most subsidiaries of listed parents will have a choice between applying the FRSME or electing to apply EU-adopted IFRS in their individual accounts. However, a subsidiary which is publicly accountable in its own right will be required to apply EU-adopted IFRS. This could be the case where the subsidiary itself has listed debt or equity instruments, or where the definition of public accountability is met because the subsidiary holds assets in a fiduciary capacity or takes deposits for a broad group of outsiders as one of its primary businesses.

Subsidiaries which are not publicly accountable and meet certain other conditions are 'qualifying subsidiaries'. These are eligible for exemptions from a number of disclosure requirements under both the FRSME and EU-adopted IFRS.

Conditions for qualifying subsidiaries

To be eligible to take disclosure exemptions, the conditions to be a qualifying subsidiary must be met. These are:

- the subsidiary individually is not publicly accountable;
- the subsidiary is included in consolidated accounts which are publicly available; and
- there is no objection from any shareholder.

This definition of a qualifying subsidiary means that the disclosure exemptions would be available to most subsidiaries of listed groups. There would be no requirement for a particular percentage ownership, such as the current cash flow statement exemption which is restricted to 90% subsidiaries.

Also, although the subsidiary must be included in consolidated accounts which are publicly available, there is no requirement for these accounts to be prepared under a particular GAAP. This would mean that UK subsidiaries of foreign parents could be eligible, even when the group accounts are not prepared under IFRS or an equivalent GAAP.

What are the disclosure exemptions for qualifying subsidiaries?

A qualifying subsidiary may take disclosure exemptions from the FRSME. These exemptions cover cash flow statements, financial instruments, group share-based payment schemes and pension schemes.

Alternatively, a qualifying subsidiary could elect to apply EU-adopted IFRS and the reduced disclosure framework. The disclosure exemptions are more extensive for subsidiaries taking this option, but this is a reflection of the increased number of disclosure requirements in EU-adopted IFRS.

The main areas of disclosure exemptions are:

- cash flow statements
- financial instruments
- group share-based payment schemes
- defined benefit pension schemes
- impairment of assets
- discontinued operations
- comparative reconciliations

Some of these exemptions are dependent on 'equivalent' disclosures being made in the consolidated financial statements. However, these equivalent disclosures only have to meet the basic disclosure requirements of IFRS, not necessarily each and every one.

What are the factors to consider?

For many subsidiaries of listed groups, the option of EU-adopted IFRS with reduced disclosures should be given serious consideration as an alternative to the FRSME. However, there are a number of important factors to consider.

Consolidation process

Currently, where the group accounts are prepared under EU-adopted IFRS and the individual accounts under UK GAAP, the consolidation process is likely to involve calculating a number of adjustments to reconcile the two GAAPs.

If the subsidiary accounts are prepared under the FRSME and the group accounts under EU-adopted IFRS, there are still likely to be adjustments as some of the accounting treatments differ. The use of EU-adopted IFRS would remove such adjustments, and streamline the process.

Preparation of individual financial statements

Despite the disclosure exemptions, individual financial statements prepared under EU-adopted IFRS will be considerably longer than those prepared under the FRSME. However, the preparation of the numbers themselves is unlikely to involve much additional work as IFRS-compliant figures will be required for group reporting.

Maintaining financial reporting knowledge

Preparing accounts under two different accounting frameworks also has costs associated with maintaining and updating the required knowledge. Differences between the two GAAPs can occasionally lead to confusion and errors occurring. If all financial statements in the group use the recognition and measurement requirements of EU-adopted IFRS, those involved in the financial reporting process will only need to maintain their knowledge of one set of standards.

Restricted accounting treatment options in FRSME

In simplifying the requirements for the FRSME, a number of accounting treatment options which exist in EU-adopted IFRS have been removed, such as the option to revalue property, plant and equipment. Other treatments are contradictory between the FRSME and EU-adopted IFRS, for example qualifying development costs must be expensed as incurred under the FRSME and capitalised under EU-adopted IFRS.

Therefore, where these treatments would have a significant impact on the amounts reported in the individual financial statements, it may be beneficial to apply EU-adopted IFRS to the subsidiary accounts.

Tax

The differences between treatments under EU-adopted IFRS and the FRSME may lead to differences in the tax treatment of some transactions. Until HMR&C have developed appropriate tax legislation, it is not possible to determine specific issues. However, differences such as the treatment of development costs may lead to a better tax outcome under one framework than the other.

Distributable profits

As for tax, differences in accounting requirements could lead to differences in the distributable profits recognised under either the FRSME or EU-adopted IFRS, and therefore the amount available to be paid as dividends. These will be very specific to each company, and will need to be investigated carefully when making a decision on which framework to adopt.

Any questions?

This factsheet can serve only to introduce the main issues raised by the ASB's proposals for listed groups. Factsheets are also available on the ASB's proposals and on the differences between current UK GAAP and the FRSME. If you need further details or advice on the potential impact on your company's financial statements, please contact the partner, director or manager at Grant Thornton who normally advises you on accounting matters. Alternatively, email your queries to us at FRSME@uk.gt.com with your contact details and we will put you in touch with a specialist in our office nearest to you.