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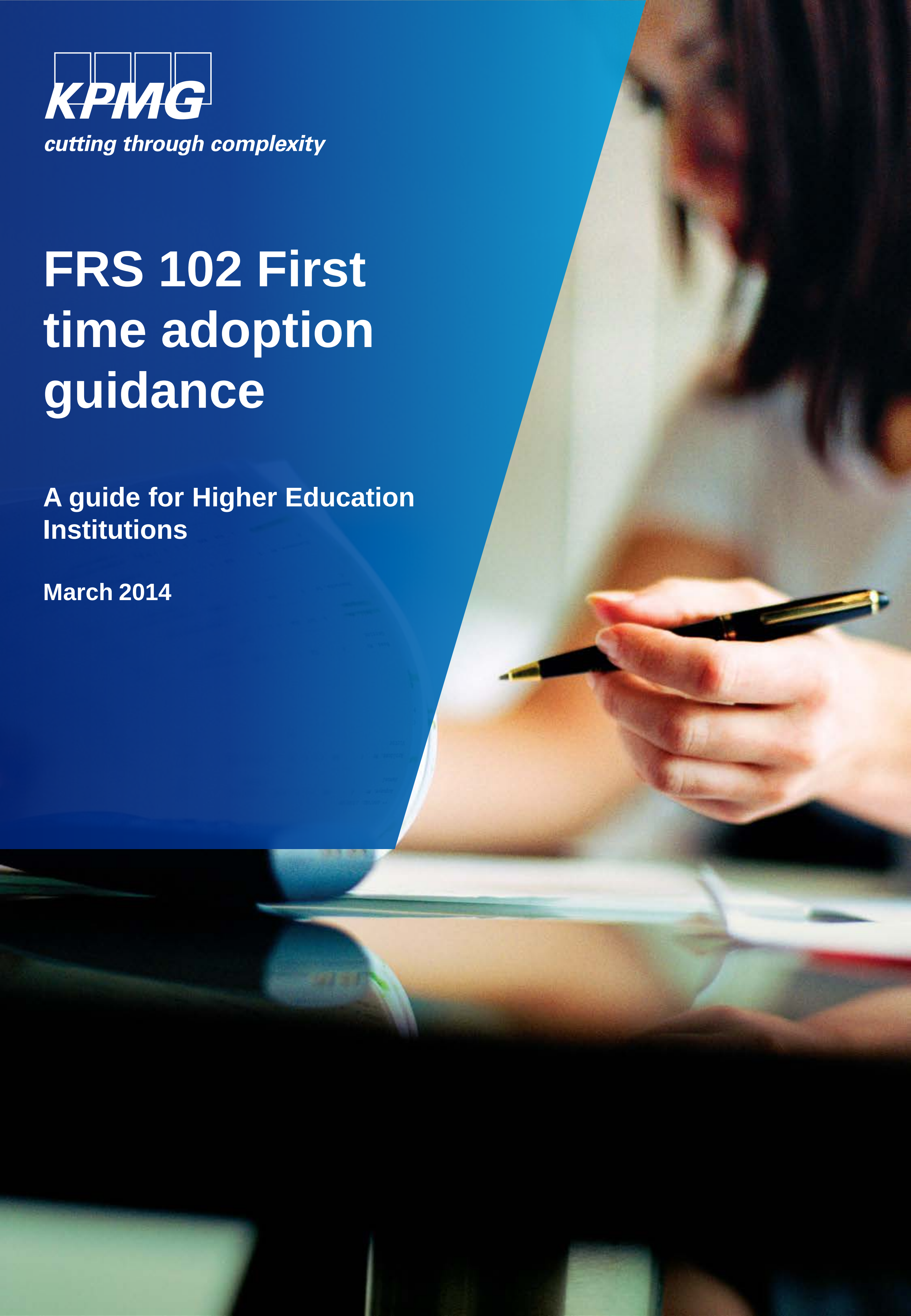
FRS 102 First time adoption guidance

A guide for Higher Education Institutions

March 2014



Introduction and Purpose

FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* represents the most significant change to UK GAAP in a generation. In one standard FRS 102 replaces almost all extant FRSs, SSAPs and UITF Abstracts with a single standard based on the IFRS for small and medium entities. While still preparing financial statements under the previous GAAP, entities will need to gather information and take appropriate action so that they are able to meet the requirements of FRS 102 and the new FE & HE SoRP on first-time adoption.

The purpose of this guide is to help those Higher Education Institutions (HEIs) adopting FRS 102 to prioritise what needs to be done in the time leading up to the preparation of the first set of FRS financial statements. The guide is set out in 2 sections:

- Planning an FRS 102 conversion project (pages 2 to 7)

- First Time adoption – transition considerations (pages 8 to 14)

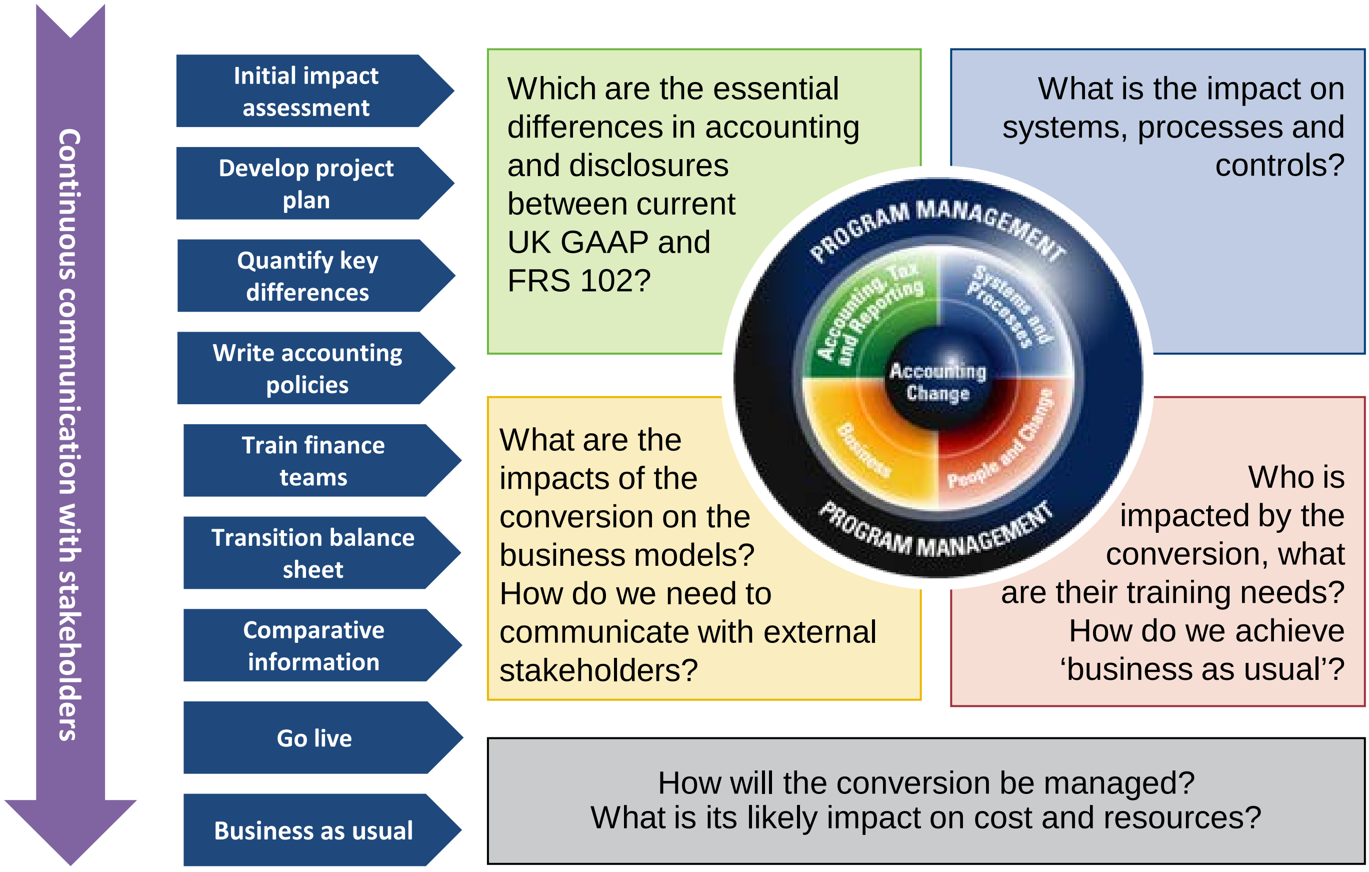
Planning a Conversion Project - Overview

Institutions adopting FRS 102 should treat a conversion project as they would any other significant project. This means that it should have appropriate project documentation, reporting and governance arrangements in place. The extent to which a project team, a detailed action plan and a communication plan is needed will depend on individual circumstances and the impact FRS 102 will have on the institution.

A logical first step is to understand the impact FRS 102 will have on the institution during an "assess" phase. This is commonly completed through undertaking a detailed gap analysis of the requirements of FRS 102. Gaps identified should give rise to an action plan which covers:

- Accounting and reporting requirements;
- Systems and processes;
- Business; and
- People and change.

The simple diagram below sets out the high level considerations of a conversion plan.

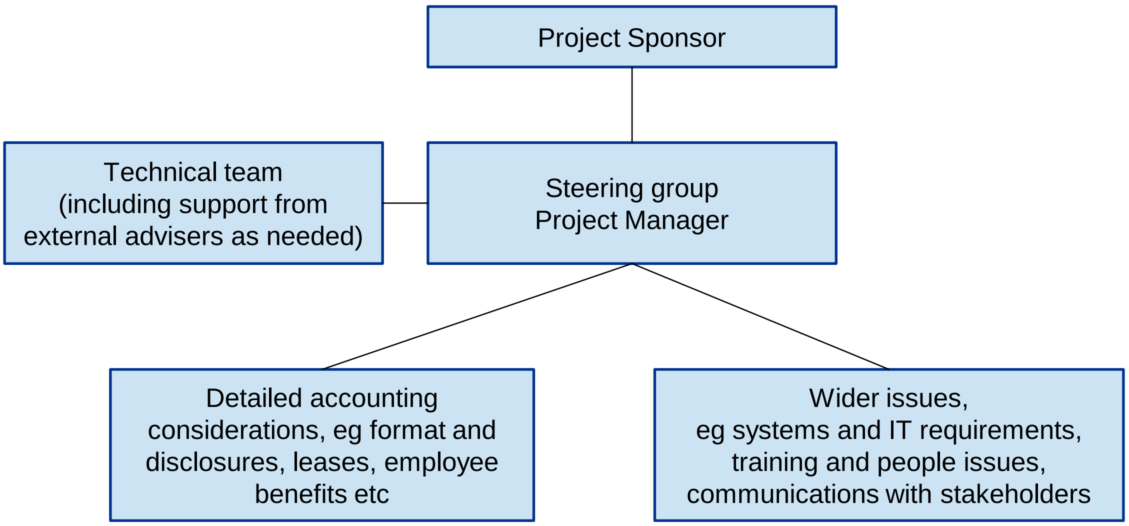


Planning a Conversion Project- Project Structure

Project team structure

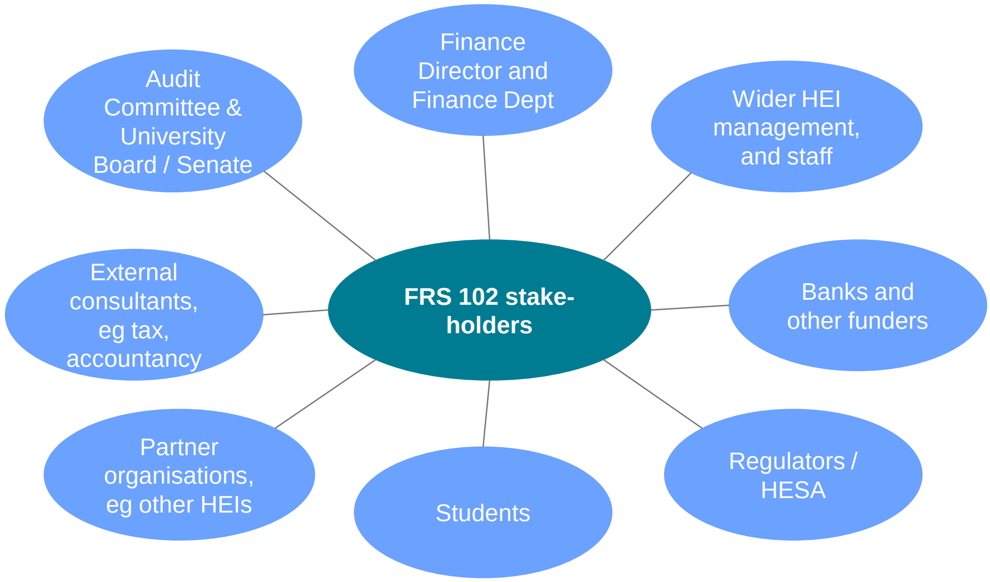
As with any major new development, the conversion to FRS 102 will benefit from the application of a well-defined project structure and the application of proper project management procedures. These procedures should include clearly defined roles, effective lines of communication, and robust input and support from the project sponsor and the institution's senior management.

An example project team structure is shown below.



Stakeholder considerations

In addition to the Finance Department, there are many other potential stakeholders in the FRS 102 conversion project. The map below illustrates the possible stakeholders that might exist in an Institution.



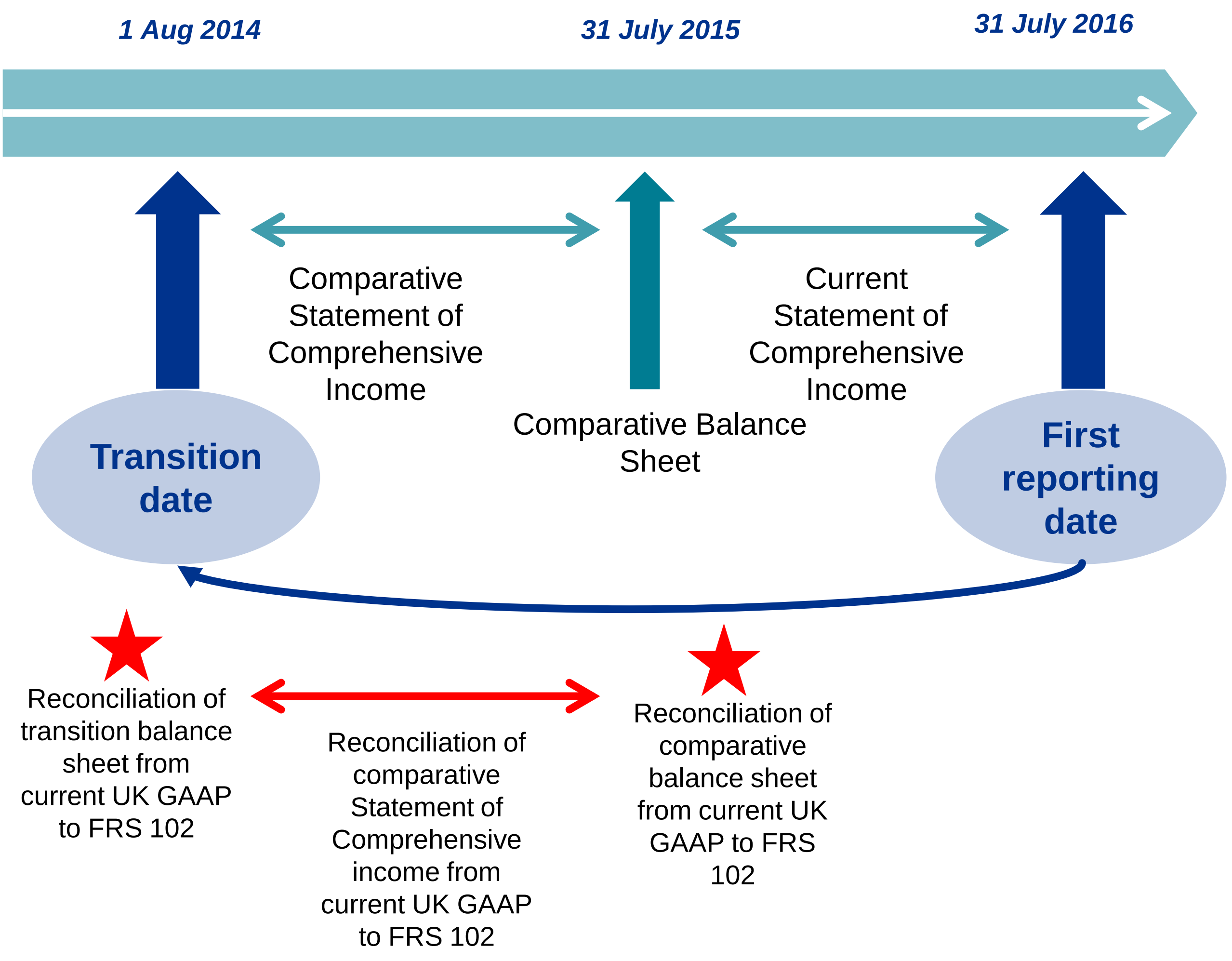
The project team will want to identify the expectations for each stakeholder, how these will be met, and the strategy and frequency of communication required for each.

Planning a Conversion Project - Adoption Timeline

FRS 102 is effective for accounting periods beginning on or after 1 January 2015. The date of transition is the beginning of the earliest period for which an entity presents full comparative information under FRS 102 in its first financial statements that comply with that standard.

For an HEI, with a year-end of 31 July, the Institution's first FRS 102 financial statements are to be prepared as at 31 July 2016. Given the requirement to present at least one year's comparatives, the date of transition would be 1 August 2014.

FRS 102 adoption timeline



First time adoption requirements:

The first set of full FRS 102 based financial statements are required to include certain disclosures about the changes from current UK GAAP to FRS 102. See pages 8 - 14 for more details about first time adoption and transition.

Conversion process – conversion timetable

The timetable below identifies steps that institutions may want to undertake as part of their conversion process. It has assumed a project commencing on 1 August, although earlier project commencement is ideal.

Managing the Change: FRS 102 Conversion Timeline for Higher Education Institutions

In advance of 31 July 2014	Quarter 1 or earlier 1/8/2014 – 31/10/2014	Quarter 2 1/11/2014 – 31/1/2015	Quarter 3 1/2/2015 – 30/4/2015	Quarter 4 1/5/2015 – 31/7/2015
	Prepare 2013/14 financial statements under UK GAAP			
Assess and make preliminary accounting policy choices		Confirm preliminary accounting policy choices	Restate FRS 102 conversion date balance sheet 31/7/2014	
Analyse detailed differences between existing policies and FRS 102 and FE HE SORP	Analyse necessary changes to accounting disclosures	Consider key presentation issues	Investigate accounting issues within 'group' (if applicable)	
		Mock-up the most recent financial statements under FRS 102	Revise accounting manual	
Assess changes to systems and processes needed to capture and report additional data.	Assess changes to systems and processes needed to capture and report additional data.		Assess changes to systems and processes needed to capture and report additional data	
Complete FRS 102 initial training.	Consider need for manual workarounds especially during the transition phase.		Decide on level of accounting overlay versus embedded accounting changes.	Conduct user training for new systems and processes.
	Define, plan and approve systems changes.	Plan user training for new systems and processes		Develop systems and process changes. Test and implement.
			Consider impact of FRS 102 on Key Performance Indicators	
		Integrate FRS 102 into management information processes	Prepare 2015/16 budgets on FRS 102 basis.	
			Review potential impact on contracts and other legal documents	Revise legal documentation where necessary.
Conduct FRS 102 training.		Determine training plan. Brief audit committee on accounting differences	Conduct FRS 102 further training.	
Brief audit and finance committee on conversion plan.	Determine necessary input from stakeholders including external auditors	Brief subsidiaries and identify key representatives.	Update audit and finance committee on conversion plan.	
Update senior and sponsoring management.		Tackle and resolve issue as appropriate.		
Prepare detailed project plan, setting out milestones and activities.		Update senior and sponsoring management.		
Mobilise project team and appoint project manager	Prepare detailed project plan, setting out milestones and activities.	Ensure project is progressing on time and to quality required.		
	Approve project budget.	Manage interdependence across project activities.		

Transition date

Final annual reporting date under existing accounting policies

- Reporting milestones
- Accounting and reporting
- Systems and processes
- Business impact
- People and communication
- Project management

Quarter 5 1/8/2015 – 31/10/2015	Quarter 6 1/11/2015 – 31/1/2016	Quarter 7 1/2/2016 – 30/4/2016	Quarter 8 1/5/2016 – 31/7/2016		Quarter 9 1/8/2016 – 31/10/2016
Prepare 2014/15 financial statements under current UK GAAP				First annual reporting date under FRS 102	Prepare 2015/16 accounts under FRS 102, including full comparatives for 2014/15
	Reconcile opening and closing reserves for 2014/15 under existing policies to FRS 102				
Develop FRS 102 accounts in parallel	Restate 2014/15 annual accounts under FRS 102.				
Transition to FRS 102 compliant accounting systems.					
Perform new FRS 102 processes on an ongoing basis					
Conduct post implementation review					
		Prepare 2016/17 budgets on FRS 102 basis.			
	Update audit and finance committee on restatement of 2014/15 numbers				
Tackle and resolve issue as appropriate					
Update senior and sponsoring management.					
Ensure project is progressing on time and to quality required.					
Manage interdependence across project activities.					

Planning a Conversion Project – Key considerations

Below are a number of considerations that institutions should include within the conversion plans.

Accounting, tax & reporting

- Accounting differences
- Reporting differences
- Tax differences
- Effect on statutory reporting
- Effect on regulatory reporting
- Resource allocation and other management tools.

Systems & processes

- General ledger and sub-ledgers
- Data collection
- Impact on ERP system
- Reporting package and consolidation
- Research ledges
- Contract registers

Business

- Contracts & agreements
- Management compensation
- Communication to financial markets
- Customer & supplier relationships
- Budget & management reporting
- Covenants
- Significant projects such as accommodation arrangements

People & change

- Skills of individuals
- Training strategy
- Change to roles & responsibilities
- Additional workload during conversion
- Project interdependencies
- Senior management team engagement

First Time Adoption – transition considerations

Planning for transition

For an HEI adopting FRS 102 for the first time in 2015, its first set of FRS 102 financial statements might seem to be a long way off but, as can be seen from the timeline overleaf, it is the balance sheet as at 31 July 2014 that will form the basis for the opening figures in the FRS 102 financial statements as at 1 August 2014. The FRS 102 balance sheet may include assets and liabilities not previously recognised, and previously recognised balances may be measured according to different requirements.

In preparing its 2013/14 financial statements the entity should consider not only the information required for its year-end balance sheet under its current GAAP but also the additional information required to restate the same items under FRS 102. Furthermore, transactions and contracts entered into in 2014/15 although initially accounted for under current GAAP, will need to be restated for the comparative information to be presented under FRS 102. This is particularly important as the exemptions available on transition are not available for transactions entered into after the transition date.

Preparing the transition balance sheet

The general requirement is that FRS 102 be applied retrospectively and therefore the transition balance sheet must be prepared in accordance with the requirements of FRS 102, with some limited exceptions. HEIs will therefore need to restate their 31 July 2014 balance sheets so that they can prepare a FRS 102 transition balance sheet as at 1 August 2014. Paragraph 35.7 of FRS 102 requires that the transition balance sheet must:

- recognise all assets and liabilities whose recognition is required by FRS 102;
- not recognise items as assets or liabilities if FRS 102 does not permit such recognition;
- reclassify items that are recognised in accordance with previous GAAP as one type of asset, liability, or component of equity, but are a different type of asset, liability or component of equity under FRS 102; and
- apply FRS 102 in measuring all recognised assets and liabilities.

Adjustments on transition are usually recognised in retained surplus (or deficit), or where appropriate another category within capital and reserves at the date of transition.

There are, however, certain exceptions to this requirement where retrospective change is not permitted, as set down in paragraph 35.9 of FRS 102.

(i) de-recognition – financial assets and financial liabilities derecognised in accordance with current FRS should not be recognised on transition.

(ii) hedge accounting – hedge accounting prior to the transition date shall not be changed for hedging relationships that no longer exist on the date of transition.

(iii) accounting estimates (for example a change in depreciable amount or useful economic life would be accounted for prospectively from the date of transition in calculating depreciation charges).

(iv) discontinued operations (for example if an operation would have been described as discontinued in accordance with FRS 3 prior to adoption of FRS 102, but would not meet the definition of a discontinued operation in FRS 102, it should not be restated in the comparatives on first time adoption).

(v) non-controlling interests.

The transition balance sheet does not need to be presented in the first set of FRS 102 financial statements, however it is required for reconciliation disclosures.

Additional disclosures required upon first-time adoption

Additional disclosures required for first time adoption

FRS 102 requires various additional information upon first time adoption. Paragraph 35.12 requires the following:

FRS 102

35.12 An entity shall explain how the transition from its previous financial reporting framework to this FRS affected its reported financial position and financial performance.

This requirement is exemplified in paragraphs 35.13 and 35.14 which state:

35.13 To comply with paragraph 35.12, an entity's first financial statements prepared using this FRS shall include:

(a) A description of the nature of each change in accounting policy.

(b) Reconciliations of its equity [reserves] determined in accordance with its previous financial reporting framework to its equity [reserves] determined in accordance with this FRS for both of the following dates:

(i) the date of transition to this FRS; and

(ii) the end of the latest period presented in the entity's most recent annual financial statements determined in accordance with its previous financial reporting framework.

(c) A reconciliation of the profit or loss [surplus or deficit] determined in accordance with its previous financial reporting framework for the latest period in the entity's most recent annual financial statements to its profit or loss [surplus or deficit] determined in accordance with this FRS for the same period.

35.14 If an entity becomes aware of errors made under its previous financial reporting framework, the reconciliations required by paragraphs 35.13(b) and (c) shall, to the extent practicable, distinguish the correction of those errors from changes in accounting policies.

The BUFDG FRG pro-forma financial statements will set out some example disclosures required on first time adoption.

First Time Adoption – Transition considerations. Exemptions for first time adoption

Paragraph 35.10 of FRS 102 allows certain exemptions on first time adoption. These exemptions are potentially useful, and HEIs may want to apply them. The table below sets out the exemptions and their applicability to the HE sector.

Ref	Exemption in para 35.10 of FRS 102	Comments
a	**Business combinations, including group reconstructions** A first-time adopter may elect not to apply Section 19 of FRS 102 Business Combinations and Goodwill to business combinations that were effected before the date of transition to FRS 102. However, if a first-time adopter restates any business combination to comply with Section 19, it shall restate all later business combinations. If a first time adopter does not apply Section 19 retrospectively, the first-time adopter shall recognise and measure all its assets and liabilities acquired or assumed in a past business combination at the date of transition to FRS 102 in accordance with paras 35.7 to 35.9 or if applicable, with paras 35.10(b) to (r) except for: (i) intangible assets other than goodwill - intangible assets subsumed within goodwill shall not be separately recognised; and (ii) goodwill - no adjustment shall be made to the carrying value of goodwill.	See paras 35.7 to 35.9 of FRS 102 for recognition and measurement requirements if section 19 is not adopted, with exceptions for goodwill. Generally there are very few business combinations in the sector. Where they do exist it is considered highly likely that HEIs will apply this exemption and therefore not re-analyse past business combinations.
b	**Share-based payment transactions** A first-time adopter is not required to apply Section 26 Share-based Payment to equity instruments that were granted before the date of transition to FRS 102, or to liabilities arising from share-based payment transactions that were settled before the date of transition to FRS 102. Except that a first-time adopter previously applying FRS 20 (IFRS 2) Share-based Payment or IFRS 2 Share-based Payment shall, in relation to equity instruments that were granted before the date of transition to this FRS, apply either FRS 20 / IFRS 2 (as applicable) or Section 26 of FRS 102 at the date of transition.	Unlikely to be applicable to HEIs.
c	**Fair value as deemed cost** A first-time adopter may elect to measure an: (i) item of property, plant and equipment; (ii) investment property; or (iii) intangible asset which meets the recognition criteria and the criteria for revaluation in Section 18 Intangible Assets other than Goodwill on the date of transition to FRS 102 at its fair value and use that fair value as its deemed cost at that date.	Simplifies the accounting for assets where information on the original cost is not easily available. Note that HEIs will need to carefully consider the impact of which valuation model (cost or valuation) they apply to their fixed assets, and to apply this model consistently to all items in the same class. The cost model is simpler but the impact on the balance sheet value of the HEI needs to be carefully considered. If the valuation model is adopted then valuations must take place with "sufficient regularity". This is a major accounting policy decision on first-time adoption.

First Time Adoption – Transition considerations. Exemptions for first time adoption

Ref	Exemption	Comments
d	**Revaluation as deemed cost** A first-time adopter may elect to use a previous GAAP revaluation of an: (i) item of property, plant and equipment; (ii) investment property; or (iii) intangible asset which meets the recognition criteria and the criteria for revaluation in Section 18 Intangible Assets other than Goodwill at, or before, the date of transition to FRS 102 as its deemed cost at the revaluation date.	As c.
e	Not used by FRS 102	
f	**Individual and separate financial statements** When an entity prepares individual or separate financial statements, paragraphs 9.26, 14.4 and 15.9 require the entity to account for its investments in subsidiaries, associates, and jointly controlled entities either at cost less impairment or at fair value. If a first-time adopter measures such an investment at cost, it shall measure that investment at one of the following amounts in its individual or separate opening statement of financial position, as appropriate, prepared in accordance with FRS 102: (i) cost determined in accordance with Section 9 Consolidated and Separate Financial Statements, Section 14 Investments in Associates or Section 15 Investments in Joint Ventures; or (ii) deemed cost, which shall be the carrying amount at the date of transition as determined under the entity's previous GAAP.	Institutions generally already hold investments in subsidiaries, associates and joint ventures at cost. Acquiring a fair value for such investments can be difficult. It is anticipated that this exemption will rarely, if ever be required by the sector.
g	**Compound financial instruments** Paragraph 22.13 requires an entity to split a compound financial instrument into its liability and equity components at the date of issue. A first-time adopter need not separate those two components if the liability component is not outstanding at the date of transition to FRS 102.	Unlikely to be relevant to HEIs.
h	Not used by FRS 102	
i	**Service concession arrangements – accounting by operators** A first-time adopter is not required to apply paragraphs 34.12E to 34.16A to service concession arrangements that were entered into before the date of transition to FRS 102. Such service concession arrangements shall continue to be accounted for using the same accounting policies being applied at the date of transition to FRS 102.	This exemption obviates the need for operators to reconsider the accounting for such arrangements. However this exemption is **NOT** available to grantors (Universities) and therefore the service concession requirements must be applied fully retrospectively. More generally FRS 102 is likely to require more service concession arrangements to come on to the balance sheets of grantors.

First Time Adoption – Transition considerations. Exemptions for first time adoption

Ref	Exemption	Comments
j	Relates to **extractive activities.**	Unlikely to be applicable to HEIs.
k	**Arrangements containing a lease** A first-time adopter may elect to determine whether an arrangement existing at the date of transition to FRS 102 contains a lease (see paragraph 20.3A) on the basis of facts and circumstances existing at that date, rather than when the arrangement was entered into.	The consideration of leases will be a time-consuming process at many HEIs, with a number of reclassifications from operating leases to finance leases expected. This exemption may help to simplify some of the work required, as the assessment can be completed using information at the transition date.
l	**Decommissioning liabilities included in the cost of property, plant and equipment** Paragraph 17.10(c) states that the cost of an item of property, plant and equipment includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. A first-time adopter may elect to measure this component of the cost of an item of property, plant and equipment at the date of transition to FRS 102, rather than on the date(s) when the obligation initially arose.	This may be relevant to some institutions. The exemption will help with calculating what the balance sheet entries should be at transition by not requiring retrospective application.
m	**Dormant Companies** A company within the Companies Act definition of a dormant company may elect to retain its accounting policies for reported assets, liabilities and equity at the date of transition to FRS 102 until there is any change to those balances or the company undertakes any new transactions.	Note if relevant.
n	**Deferred development costs as a deemed cost** A first-time adopter may elect to measure the carrying amount at the date of transition to FRS 102 for development costs deferred in accordance with SSAP 13 Accounting for research and development as its deemed cost at that date.	Potentially useful simplification, although it is rare that HEIs capitalise development costs.
o	**Borrowing costs** An entity electing to adopt an accounting policy of capitalising borrowing costs as part of the cost of a qualifying asset may elect to treat the date of transition to FRS 102 as the date on which capitalisation commences.	Will be relevant if an HEI intends to commence capitalising interest. This is expected to be rare in the sector, as few HEIs currently capitalise interest.
p	**Lease incentives** A first-time adopter is not required to apply paragraphs 20.15A and 20.25A to lease incentives provided the term of the lease commenced before the date of transition to FRS 102. The first-time adopter shall continue to recognise any residual benefit or cost associated with these lease incentives on the same basis as that applied at the date of transition to FRS 102.	A potentially useful simplification, as it means that HEIs need not consider lease incentives for leases entered into before the transition date. Institutions must consider lease incentives on any lease arrangements entered into after transition (1 August 2014).

First Time Adoption – Transition considerations. Exemptions for first time adoption

Ref	Exemption	Comments
q	**Public benefit entity combinations** A first-time adopter may elect not to apply paragraphs PBE34.75 to PBE34.86 relating to public benefit entity combinations to combinations that were effected before the date of transition to FRS 102. However, if on first-time adoption a public benefit entity restates any entity combination to comply with this section, it shall restate all later entity combinations.	Note if relevant. Generally there are very few business combinations in the sector. Where they do exist it is considered highly likely that HEIs will apply this exemption and therefore not re-analyse past business combinations.
r	**Assets and liabilities of subsidiaries, associates and joint ventures** If a subsidiary becomes a first-time adopter later than its parent, the subsidiary shall in its financial statements measure its assets and liabilities at either: (i) the carrying amounts that would be included in the parent's consolidated financial statements, based on the parent's date of transition to this FRS, if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary; or (ii) the carrying amounts required by the rest of this FRS, based on the subsidiary's date of transition to this FRS. These carrying amounts could differ from those described in (i) when: (a) the exemptions in FRS 102 result in measurements that depend on the date of transition to FRS 102; or (b) the accounting policies used in the subsidiary's financial statements differ from those in the consolidated financial statements. For example, the subsidiary may use as its accounting policy the cost model in Section 17 Property, Plant and Equipment, whereas the group may use the revaluation model. A similar election is available to an associate or joint venture that becomes a first-time adopter later than an entity that has significant influence or joint control over it. However, if an entity becomes a first-time adopter later than its subsidiary (or associate or joint venture) the entity shall, in its consolidated financial statements, measure the assets and liabilities of the subsidiary (or associate or joint venture) at the same carrying amounts as in the financial statements of the subsidiary (or associate or joint venture), after adjusting for consolidation (and equity accounting) adjustments and for the effects of the business combination in which the entity acquired the subsidiary (or transaction in which it acquired the associate or joint venture). Similarly, if a parent becomes a first-time adopter for its separate financial statements earlier or later than for its consolidated financial statements, it shall measure its assets and liabilities at the same amounts in both financial statements, except for consolidation adjustments.	Note if relevant.

First Time Adoption – Transition considerations. Exemptions for first time adoption

Ref	Exemption	Comments
s	**Designation of previously recognised financial instruments** FRS 102 permits a financial instrument (provided it meets certain criteria) to be designated on initial recognition as a financial asset or financial liability at fair value through profit or loss. Despite this an entity is permitted to designate, at the date of transition to FRS 102, any financial asset or financial liability at fair value through profit or loss provided the asset or liability meets the criteria in para 11.14(b) at that date (para 11.14(b) sets out the criteria that allows debt instruments to be designated by the entity as at fair value through profit or loss).	An institution can allocate a financial instrument at fair value through the P&L at transition rather than when the instrument was issued. We expect this to be applied very rarely, if at all in the HE sector.

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