

Financial Reporting 2007 UK GAAP Checklist

KPMG LLP (UK)

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Revised disclosure of auditor remuneration

Issued August 2005

Effective for periods starting on/after 1 October 2005

The Companies Act 1985 (Disclosure of Auditor Remuneration) Regulations 2005 (SI 2005/2417) supersedes existing requirements for disclosure of audit and non-audit fees. In October 2006 ICAEW issued TECH 6/06 which provided guidance on their application. In July 2007 a revised version of TECH 6/06 was issued which reflects changes made in the light of practical experience of working with the new disclosure requirements.

Main effects

- Audit fees to be disclosed (computation of group audit fee different from previous requirements).
- Fees for non-audit services provided to company, its subsidiaries and any related pension schemes by company auditor and its associates (as defined) to be disclosed, analysed by detailed categories.
- Some exemptions available for certain small or medium sized companies and in parent/subsidiary individual accounts where disclosures are given on a group basis.

Mandatory years starting January 2005/6 (and related requirements)

FRS 20: Share-based payment

Issued April 2004

Mandatory for periods starting on/after 1 January 2005 (listed entities) or 1 January 2006 (all other entities)

Early adoption encouraged

FRS 20 is identical to IFRS 2 and supersedes Abstract 17. It requires companies to recognise an expense in respect of their employee share option plans, share purchase plans and share-based payments.

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Main effects

- An expense is recognised for all share-based payments based on the fair value of the instrument.
- Market based performance conditions taken into account in measuring fair value of instrument granted (no subsequent adjustments made for equity-settled).
- Service conditions and non-market based performance conditions cause subsequent adjustments to the number of shares/options in respect of which fair value is charged to the P&L account.
- Applies to both equity-settled and cash-settled share-based payment arrangements, whether with employees or third party providers of goods and services.
- Applies to all share option and share purchase schemes, including Save As You Earn (SAYE) schemes.

Abstract 41: (IFRIC 8) Scope of FRS 20 (IFRS 2) Share-based payment

Issued April 2006

Mandatory for periods starting on/after 1 May 2006

Early adoption encouraged

Main effects

- Where an entity cannot identify specifically some or all of the goods or services received as consideration for its equity instruments, or it appears that unidentifiable goods or services have been received as consideration (if any), i.e., where fair value of consideration is less than fair value of equity instruments granted or liability incurred, FRS 20 applies to such transactions.
- Identifiable goods or services received as consideration measured in accordance with FRS 20. Any unidentifiable goods or services measured as difference between fair value of share based payment and fair value of any identifiable goods or services received.
- Unidentifiable goods or services received shall be measured at grant date. However, for cash settled transactions, liability remeasured at each reporting date until settled.

Abstract 44: (IFRIC 11) FRS 20 (IFRS 2) – Group and Treasury Share Transactions

Issued February 2007

Applicable for years starting on/after 1 March 2007

Early adoption encouraged

Abstract 44 provides guidance on whether share-based payment arrangements, in which employees of a subsidiary are provided with equity instruments of the parent, should be accounted for as cash-settled or equity-settled in the subsidiary's

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accounts. Abstract 44 is limited to classification and does not change the existing requirement of FRS 20 for the subsidiary to recognise a share-based payment.

Main effects

- Arrangements granted by the parent that are accounted for as equity-settled in the group accounts should also be accounted for as equity-settled in the subsidiary's individual accounts
- Arrangements granted by the subsidiary (over its parent's shares) should be accounted for as cash-settled in the subsidiary's individual accounts.
- Share-based payment arrangements in which an entity receives goods or services as consideration for its own equity instruments should be accounted for as equity-settled share-based payment transactions, regardless of how the equity instruments needed are obtained.

FRS 26: Financial instruments: Measurement

Issued December 2004; amendments issued October 2005 and April 2006

Mandatory for periods starting on/after 1 January 2005 (listed companies)

or 1 January 2006 (all other entities within its scope)

Transition/initial recognition amendment effective immediately FRS 26 adopted

Other amendments mandatory for periods starting on/after 1 January 2006/7

Early adoption in years starting before 1 January 2005 not permitted

FRS 26 introduces to UK GAAP the measurement and hedge accounting rules of IAS 39 and, following amendment (see below), its recognition and derecognition requirements. It applies from 2005 to listed companies (those with securities traded on an EU regulated market) that are not preparing their individual accounts in accordance with IFRS. Entities choosing to apply the fair value accounting rules for financial instruments permitted under company law from 2005 will have to adopt FRS 26 from 2006 and can choose to adopt it in 2005.

The October 2005 amendments were to maintain alignment with IAS 39 following IASB amendments and, except for the transition/initial recognition amendment, are all mandatory from 1 January 2006.

Additionally, the ASB issued an amendment in April 2006 implementing the recognition and derecognition rules of IAS 39 into FRS 26. This amendment is mandatory for accounting periods starting on/after 1 January 2007 for entities within the scope of FRS 26, with earlier adoption encouraged. Transitional relief is available.

Main effects

- All derivatives recognised on balance sheet at fair value.
- Embedded derivatives must be identified; often accounted for separately from host contract unless 'closely related'.
- Certain types of other financial instrument must be held at fair value.

- Also, under unamended FRS 26 *any* financial asset or liability may be designated irrevocably on initial recognition as being measured at fair value, with period movements to P&L account (the fair value option). The amended (10/05) fair value option restricts the designation of financial assets and financial liabilities as at fair value through profit or loss to certain prescribed circumstances.
- Strict criteria to be met and formal documentation required to apply hedge accounting.
- Amendment (10/05) permits a forecast intra-group transaction to be the hedged item in a cash flow hedge in certain circumstances.
- Derecognition continues to be dealt with under FRS 5, until the amendment (4/06) to FRS 26 is adopted when the recognition/derecognition of financial assets and liabilities falls within the scope of FRS 26 (FRS 5 still applies to the recognition/derecognition of non-financial assets and liabilities).
- Amendment (10/05) defines financial guarantee contracts and credit insurance to be financial instruments within scope of FRS 26. However, permits choice of applying either FRS 26 or insurance accounting under certain conditions.
- Amendment (10/05) introduces a scope exclusion for certain loan commitments, however intra-group loan commitments are not excluded from the requirements to be recognised initially at fair value.
- Detailed transitional arrangements, with relief from full restatement of comparatives if adopted by certain date.
- Amendment (10/05) permits a relief from full retrospective application of rules for initial recognition of financial assets and financial liabilities and transitional arrangements.

Abstract 42: (IFRIC 9) Reassessment of embedded derivatives

Issued April 2006

Mandatory for periods starting on/after June 2006

Early adoption encouraged

Main effects

- Assess whether embedded derivative is required to be separated from host contract and accounted for as a derivative when entity first becomes a party to contract.
- Subsequent reassessment prohibited unless change in the terms of the contract that significantly modifies cash flows. Modification to cash flows may be considered significant where expected future cash flows associated with embedded derivative, host contract or both have changed and where change is significant relative to previously expected cash flows on the contract.

Mandatory for entities applying FRS 26

FRS 23: The effects of changes in foreign exchange rates

Issued December 2004; amendment issued December 2005

Mandatory for entities applying FRS 26; other entities may not apply FRS 23

Amendment effective immediately FRS 23 adopted

FRS 23 is largely identical to IAS 21. Must be adopted by entities applying FRS 26, for whom it supersedes SSAP 20. For other entities, SSAP 20 continues to apply.

Main effects

- Functional currency of certain subsidiaries in their *individual* accounts treated as being same as that of parent. Accordingly, temporal method of translating the results of overseas entities no longer necessary and standard acknowledges only net investment method.
- When applying the net investment method, P&L account must be translated at transaction-date rate (an average rate will often suit); closing rate prohibited.
- Acquisition fair value adjustments and goodwill must be treated as currency items and translated at closing rate.
- No reference to hedge accounting; the FRS 26 requirements apply (broadly, net investment hedge accounting now possible only in group accounts).
- Free choice of presentation currency. Functional currency remains question of fact.
- Under SSAP 20, contracted exchange rates sometimes used to translate a transaction. FRS 23 requires transaction to be recorded initially at spot rate; any related monetary items subsequently retranslated at balance sheet date rate.
- Cumulative exchange differences on translation of an overseas entity recycled through P&L account on its disposal. Transitional relief to "start the clock" on these differences at effective date of standard.
- Amendment permits exchange differences arising on loans denominated in any currency forming part of net investment in foreign operation to pass through equity. Amendment also clarifies that loan between foreign operation and any part of the group can form part of net investment in foreign operation.

FRS 24: Financial reporting in hyperinflationary economies

Issued December 2004

Mandatory for entities applying FRS 26; other entities may not apply FRS 24

Largely identical to IAS 29. If adopted, supersedes UITF Abstract 9.

Main effects

- Applies to individual accounts of entities that have a hyperinflationary functional currency as well as to group accounts consolidating such entities.
- Requires adjustment for *all* inflation from date non-monetary assets acquired – i.e., not just during the period of hyperinflation.
- More prescriptive than UITF 9 in its methodology.
- Fully retrospective.

FRS 25: Financial instruments: disclosure and presentation – disclosure aspects

Issued December 2004

Disclosure requirements of paragraphs 51 to 95 mandatory for entities applying FRS 26; adoption by other entities encouraged

FRS 25 introduced IAS 32 into UK GAAP; the presentation requirements became mandatory for all entities for periods starting on or after January 2005. Entities not adopting FRS 26 (see above) are exempt from the disclosure requirements of FRS 25 and will continue to follow FRS 13 where applicable. The disclosure requirements of FRS 25 will be replaced by FRS 29 (see below) for years starting 1 January 2007. Exemption from disclosure requirements is available for the individual accounts of certain parents and 90 percent subsidiaries, where consolidated accounts complying in full are available.

The main effect is that FRS 25 has more extensive disclosure requirements than FRS 13 in some respects.

Mandatory years *ending* December 2006 (and related requirements)

WEEE Directive

Substantively enacted December 2006 and passed into law January 2007

Mandatory for years ending December 2006

Final regulations to implement the EU directive on Waste Electrical and Electronic Equipment (WEEE) laid before parliament (and therefore substantively enacted) on 12 December 2006 and passed into law on 2 January 2007.

Main effects

- Producers of electrical or electronic equipment (EEE) responsible for the costs of recycling WEEE from private households deposited at designated collection facilities from 1 July 2007.
- Obligations of a producer based on its share of the market from 1 July 2007. No liabilities arise until sales are made in this period.
- No provisions in respect of household WEEE required at 31 December 2006.
- A producer is responsible for recycling cost of WEEE arising after 1 July 2007 from users other than private households (Commercial WEEE), where:
 - equipment originally sold by that producer on or after 13 August 2005; or
 - equipment originally sold before 13 August 2005 but after that date, producer supplies new EEE to replace the pre 13 August 2005 equipment.
- Such producers likely to have liabilities in respect of Commercial WEEE that require recognition at 31 December 2006.
- For other Commercial WEEE the final user is responsible for the costs of its disposal.
- Users and producers of Commercial WEEE may conclude agreements to transfer their obligations under the regulations to a different party.

Abstract 45: (IFRIC 6) Liabilities arising from Participation in a Specific Market – Waste Electrical and Electronic Equipment

Issued 13 February 2007

Mandatory for years ending on/after 22 June 2007

Early adoption encouraged

Abstract 45 provides guidance on accounting for liabilities for waste management costs under the WEEE Directive. The Abstract confirms that the obligating event giving rise to a liability for waste management costs is participation in the market during a measurement period (and not as products are manufactured or sold).



Mandatory for directors' reports approved from 6 April 2007

Disclosure of directors' interests in shares – changes

Effective for directors' reports approved on/after 6 April 2007

Applicable to all UK companies

Section 325 of the Companies Act 1985 required a company to maintain a register of notified interests in shares. Schedule 7 of the Act required disclosure of notified interests in the directors' report. For listed companies, disclosure required also by Listing Rule 9.8.6 R (1).

Main effects:

- Companies Act requirements were repealed with effect from 6 April 2007.
- Listing Rule 9.8.6 R (1) has been amended to require the annual financial report of a company subject to the listing rules of the London Stock Exchange to include a statement as at the end of the financial year setting out the directors' interests that are notifiable transactions under DTR 3.1.2R.



Mandatory years starting 20 May 2006

Takeovers Directive

Issued April 2004 for implementation into EU member states' law by 20 May 2006
Mandatory for periods starting on/after 20 May 2006

The requirements of the Takeovers Directive were introduced into UK law by SI 2006/1183 *The Takeovers Directive (Interim Implementation) Regulations 2006*. These requirements were initially incorporated in the Companies Act on 6 April 2007 by inserting a new Part 7 into Schedule 7 (matters to be dealt with in directors' report).

Main effects

- Applies in directors' reports of companies with securities traded on a regulated market
- Additional disclosure requirements to be made in directors' reports concerning company's share capital, directors and employees – e.g., disclosure of how control rights over shares issued under an employee share scheme are exercisable where those rights are not exercised directly by the employee; disclosure of agreements between company and its directors or employees providing for compensation for loss of office or employment that occurs because of a takeover bid.



Mandatory years starting November 2006

Revised Combined Code

Issued July 2006
Mandatory for periods starting on/after 1 November 2006

Main effects

The updated version of the Combined Code on Corporate Governance contains the following amendments:

- B.2.1. – enable the company chairman to sit on (but not chair) the remuneration committee if considered independent on appointment.
- D.2.1. – provide shareholders voting by proxy with option of withholding their vote on a resolution.
- D.2.2 – encourage companies to disclose details of proxies lodged on resolutions where votes taken on a show of hands.
- A.4.1, B.2.1, C.3.3 – enable companies to meet requirement of making terms of reference of board committees available by placing them on their Web sites.



Mandatory years starting January 2007

Updated Financial Reporting Standard for Smaller Entities

Updated version of FRSSE issued January 2007

Effective for periods starting on/after 1 January 2007

Early adoption permitted

Supersedes and updates FRSSE (January 2005). Revised version includes a major simplification in the application of FRS 20 *Share-based payment*. It requires a disclosure-only approach for equity-settled arrangements in small companies applying the FRSSE.

Main effects

- For equity-settled share-based payment arrangements the FRSSE requires only disclosure of the principal terms and conditions of such arrangements existing in the period.
- Accounting for cash-settled share-based payments remains the same as that required by FRS 20.
- Principal terms and conditions of cash-settled share-based payments are disclosed.

Amendment to FRS 3: Reporting Financial Performance

Issued 6 July 2007

Effective for periods starting on/after 1 January 2007

Early adoption permitted

Clarifies the application of FRS 3 to entities within the scope of FRS 26 (IAS 39) *Financial Instruments: Recognition and Measurement*. Aligns the requirements of FRS 3 to FRS 26 with respect to the presentation of gains and losses on certain financial instruments and to FRS 23 (IAS 21) *The Effects of Changes in Foreign Exchange Rates* with respect to the recycling of foreign exchange differences from equity to the profit and loss account.

Main effects

- Under FRS 26, gains and losses on the re-measurement of available-for-sale financial assets are required to be recognised in equity and recycled to the profit and loss account on de-recognition.
- Under FRS 23, the cumulative amount of exchange differences recognised through the statement of total recognised gains and losses in relation to a foreign operation is required to be recognised in the profit and loss account when the gain or loss on disposal is recognised.
- The amendment's principal change is to provide an exemption from certain paragraphs of FRS 3 for those entities applying FRS 26 and FRS 23.



Mandatory for entities applying FRS 26

FRS 29: Financial instruments: disclosures

Issued December 2005

Mandatory from 1 January 2007 for entities applying FRS 26; however other entities may apply FRS 29 voluntarily

Certain exemptions apply to subsidiaries and parents in respect of their single entity accounts

Early adoption encouraged

FRS 29 introduces into UK GAAP the requirements of IFRS 7 *Financial Instruments: Disclosures* and the related amendments to IAS 1 *Presentation of Financial Statements*.

FRS 29 supersedes the disclosure requirements of FRS 25 which are otherwise mandatory for entities applying FRS 26. The FRS 25 disclosure requirements replaced the previous UK accounting standard FRS 13 for companies applying FRS 26. However, FRS 29 requires more detailed information to be given in the profit and loss account which may be difficult for some entities to collect in time.

Main effects

- Disclose information on significance of financial instruments for an entity's financial position and performance.
- Disclose qualitative and quantitative information about exposure to risks arising from financial instruments (e.g., credit risk, liquidity risk, market risk) and objectives, policies and processes for monitoring such risks. Quantitative disclosure requirements principally based on the company's own internal risk monitoring information.
- Disclose qualitative and quantitative information about capital management. Disclosures are identical to recent amendments to IAS 1 and include information on policies and processes for managing capital as well as what is regarded as capital.
- Added disclosure requirements in respect of gains and losses for different classes of financial instruments and hedge accounting.



Mandatory for years starting 6 April 2007

Amendment to FRS 17: Retirement Benefits

Issued December 2006

Mandatory for periods starting on/after 6 April 2007

Early adoption encouraged

Non-mandatory best practice disclosure statement also issued

Amendment replaces the current disclosures required by FRS 17 for defined benefit schemes with the disclosures required by IAS 19 *Employee Benefits* (as revised in December 2004). ASB also published a Reporting Statement *Retirement Benefits – Disclosures* which, as a best practice guide, is intended to have persuasive rather than mandatory force. Recommendations aim to assist users to obtain a clear view of the risks and rewards arising from the defined benefit schemes and to identify the funding obligations of the entity with respect to the liabilities of the scheme. Recommendations may be applied by any entity that operates or sponsors a defined benefit scheme, regardless of whether it prepares accounts under UK GAAP or EU-endorsed IFRS.

Main effects

- Current bid price to be used as fair value of quoted securities held as plan assets rather than mid-market price.
- As amendment applied retrospectively, bid price valuations required going back three years.
- Separate opening to closing reconciliations for scheme assets and liabilities instead of the single reconciliation of the scheme's net surplus or deficit.
- More extensive disclosure of actuarial assumptions required, e.g., in many cases, of mortality assumptions.
- Reporting Statement notes that directors should assess the significance of the company's exposure to defined benefit schemes in planning their disclosures.
- Recommended disclosures complement the existing FRS 17 (and IAS 19) disclosures. Reporting Statement contains illustrative examples of the disclosures.



Mandatory for years starting 1 October 2007

Impact of Companies Act 2006 on Directors' report – Business review

Effective for periods starting on/after 1 October 2007

The Companies Act 2006 is being phased in over time. CA 2006 section 417, which sets out the requirements for the business review in the directors' report, is effective for financial years beginning on or after 1 October 2007; CA 1985 section 234ZZB, which contains the business review requirements of that Act, is repealed for those financial years. 2006 Act's requirements for quoted companies are more extensive than those of 1985 Act.

Main effects

- Purpose is to inform members and help them assess how the directors have performed their duties to promote the success of the company.
- More forward looking disclosure regarding the trends and factors likely to affect the future development, performance and position of the business.
- Information about environmental matters, employees and social and community issues including policies and the effectiveness of policies in relation to these matters. If this information has not been given, a statement must be made to this effect.
- Information about persons with whom there are contractual or other arrangements which are essential to the business (so-called 'supply chain' disclosures). Subject to limited exemption from disclosure where disclosure would be seriously prejudicial to that person and contrary to the public interest (use of this exemption is expected to be extremely rare in practice).
- General exemption from disclosure of any impending matters/matters in the course of negotiations where disclosure would be seriously prejudicial to the interests of the company (no comparable exemption provided in section CA 1985 234ZZB).



Publications

Recent books and publications from KPMG member firms relevant to financial reporting:

Published by KPMG IFRG Limited:

- *Insights into IFRS* (2007/8 Edition): a practical guide to International Financial Reporting Standards.
- *IFRS: an overview* (August 2007): an executive summary of the key requirements of IFRSs for financial periods beginning on or after 1 January 2007.
- *The Application of IFRS: Disclosures in Practice* (December 2006): an illustration of disclosures made in practice by companies.
- *The Application of IFRS: Choices in Practice* (December 2006): a survey of how companies dealt with explicit options offered by IFRS.
- *IFRS 7 for Corporates* (December 2006): a supplement to the August 2006 *Illustrative Financial Statements*.
- *First Impressions: IFRS 8 Operating Segments* (July 2007): an assessment of the impact of implementation of IFRS 8.
- *First Impressions: IFRIC 12 Service Concession Arrangements* (January 2007): an assessment of the impact of implementation of IFRIC 12.
- *Illustrative financial statements – IFRS* (August 2007) – Annual periods beginning on or after 1 January 2007.
- *Illustrative financial statements: banks – IFRS* (September 2006) – Annual periods beginning on or after 1 January 2006.
- *Disclosure checklist: IFRS* (August 2007) – Annual periods beginning on or after 1 January 2007.
- *IFRS compared to US GAAP (July 2007) – an overview of significant differences between IFRS and US GAAP.*

Published by KPMG LLP (UK):

- *Financial Reporting Supplement Companies Act 2006* (November 2006): summarises the financial reporting and other key aspects of the Companies Act 2006.
- *Financial Reporting Supplement the DTR and IAS 34 in practice* (October 2007): summarises the financial reporting and other key aspects of applying IAS 34.

Recent corporate governance publications from the KPMG-sponsored Audit Committee Institute (ACI) include:

- *Horizon*, Issue 2 (June 2007) – briefing paper for audit committee members and finance directors that monitors the likely forthcoming changes in financial reporting, regulation, company law, tax and pensions and explores their potential effect.
- *Accounting judgements, estimates and restatements – implications for audit committee oversight* (May 2007) – a survey of UK audit committee members on the challenges and issues they face in respect of their financial reporting oversight responsibilities.
- *Perspectives* (September 2007) – report from the European Audit Committee Chairmen’s Forum.
- *Audit Committee Quarterly*, Issue 18 (September 2007).
- *Audit Committee Quarterly*, Issue 17 (June 2007).
- *Remuneration Committee Journal* (February 2007) – technical and regulatory summary for remuneration committee members.



Publications may be requested from your usual contact at KPMG LLP (UK) or via our Web site (www.kpmg.co.uk) using 'Contact us'.

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