

# Financial Reporting Update

KPMG LLP (UK)

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## WEEE Regulations

Further to our article in the July/August 2006 *Update*, final regulations to implement the EU directive on Waste Electrical and Electronic Equipment (WEEE) were laid before parliament on 12 December 2006 and passed into law on 2 January 2007. KPMG in the UK considers that the legislation was substantively enacted by 31 December 2006 and therefore that entities should consider its impact when preparing their December 2006 financial statements.

The impact of the regulations may be summarised as follows:

Producers of electrical or electronic equipment (EEE) are responsible for the costs of recycling WEEE from private households deposited at designated collection facilities from 1 July 2007. The obligations of a producer are based on its share of the market from 1 July 2007 and no liabilities arise until sales are made in this period. Accordingly, no provisions in respect of household WEEE are required at 31 December 2006.

However, in respect of WEEE arising after 1 July 2007 from users other than private households (Commercial WEEE), a producer is responsible for the recycling cost where:

- the equipment originally was sold by that producer on or after 13 August 2005; or
- the equipment originally was sold before 13 August 2005 but where, after that date, that producer supplies new EEE to replace the pre 13 August 2005 equipment.

Therefore such producers are 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; however, users and producers of Commercial WEEE may conclude agreements to transfer their obligations under the regulations to a different party.

The legislation is available at  
[www.opsi.gov.uk/si/si2006/  
uksi\\_20063315\\_en.pdf](http://www.opsi.gov.uk/si/si2006/uksi_20063315_en.pdf)

Accordingly, commercial users (i.e., many businesses) are likely to have decommissioning liabilities that require recognition at 31 December 2006. In many cases, such liabilities should be capitalised as part of the cost of the fixed asset.



## **IFRS implementation**

The Financial Review Reporting Panel (FRRP) has issued its first report outlining the preliminary findings of its review of IFRS implementation by UK listed companies. Its review continues but it has identified a number of issues which it believes should be drawn to the attention of companies planning the preparation of their second IFRS annual accounts.

In keeping with the FRRP's activity report to 31 March 2006 issued in October 2006 (and discussed in the September/October *Update*), the FRRP reports a good level of compliance with IFRS and recognises the significant amount of work by UK companies that has gone into the accounts production process. The FRRP identified several key areas for improvement: accounting policies; disclosure of judgements and estimates; disclosure of reasons for goodwill; intangible assets; impairment testing; related party disclosures; new standards and interpretations; and presentation, each of which is discussed in more detail below.

Accounting policy descriptions were found to be a little too generic with companies opting to use wording from the standards, rather than adapting the wording to describe more accurately the issues relevant to the company's individual circumstances. Also UK GAAP terminology was still found, despite this issue being highlighted in their report on interims. For example, revenue recognition policies may need to include a description of the methods applied to determining a transaction's stage of completion. In addition, the FRRP found that some stated accounting policies were irrelevant since there were no accounting transactions falling within their scope, e.g., the inclusion of a policy in respect of hedging when this was not applied in practice. In its report, the FRRP encourages companies to disclose only those accounting policies applied in practice, with information provided being specific to their particular circumstances.

IAS 1 *Presentation of Financial Statements* requires disclosure of the key sources of estimation uncertainty and key assumptions concerning future events that have a significant risk of causing material adjustment in the carrying amounts of assets or liabilities in the subsequent year. It also requires disclosure of the judgements made by management in applying the accounting policies that have the most significant impact on the amounts recognised in the accounts.

The FRRP found that practice varied with some companies providing detailed disclosures of their key judgements and estimation uncertainties, whereas others provided only disclosures similar to those required by IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Others provided 'bland' disclosures that bore no relation to the company's particular circumstances; they should always cover specific information relevant to understanding, in particular, a company's key sources of estimation uncertainty.

The FRRP also reminds preparers that where goodwill is recognised on an acquisition, IFRS 3 requires an explanation of why that goodwill arises and an explanation of any intangible assets that were not recognised, including why their value could not be measured reliably. In addition, IAS 36 *Impairment of Assets* requires goodwill and those intangible assets with indefinite lives to be tested for impairment annually. In particular, paragraph 134 of IAS 36 requires disclosures regarding the method and assumptions used to determine recoverable amount for a cash-generating unit that contains goodwill or indefinite-lived intangibles, whether or not an impairment has been charged. In some cases, the FRRP found that these disclosures were omitted.

IAS 24 *Related Party Disclosures* includes key management within the definition of a related party and requires certain disclosures in respect of transactions with those related parties, including remuneration. The Companies Act 1985 continues to require disclosure of directors' remuneration but the remuneration of key management personnel was sometimes overlooked as a related party transaction under IAS 24. In other cases companies stated that their only key management were their directors: the FRRP specifically states that where narrative reports elsewhere in the annual accounts refer to management personnel by name, companies should consider whether their remuneration and other details should be included within the IAS 24 disclosures.

The FRRP also noted that some companies had failed to comply with the requirement under IAS 8 *Accounting Policies* to disclose details of the impact of new standards and interpretations that were issued but not yet effective (for UK preparers, 'issued' means endorsed for use in Europe). Where the impact is not known or reasonably estimable, this fact should be stated.

As a final point, the FRRP comments on the presentation of the primary statements, in particular the income statement, and the narrative reports. It found that some companies provided additional line items in their income statements, similar to those found under UK GAAP such as amortisation or impairment charges. Although IAS 1 allows additional line items, the FRRP states that in its view, these should be included only when they are necessary to explain elements of financial performance. The report also reminds companies that non-GAAP performance measures should be defined and reconciled to GAAP measures and should not be given undue prominence. This latter point may be advance warning of its area of focus when the Enhanced Business Review falls within its scope in years beginning on or after 1 April 2006.

The FRRP's preliminary report is available on the Web at [www.frc.org.uk/frfp/press/pub1206.html](http://www.frc.org.uk/frfp/press/pub1206.html)



## UITF IS 81

The Urgent Issues Task Force (UITF) has issued Information Sheet 81 which recommends to the Accounting Standards Board (ASB) an amendment to FRS 3 *Reporting Financial Performance*. If implemented, it will be applicable to UK entities within the scope of FRS 26 *Financial Instruments: Recognition and Measurement*.

Currently, FRS 3 specifies the treatment of gains and losses both on disposal and revaluation for all assets and liabilities. It includes a dispensation from certain of its requirements for insurance businesses and requires that realised and unrealised gains and losses on investments held as part of their investment portfolios are included as part of the investment return in the profit and loss account.

FRS 26, which is applicable to listed companies or those companies preparing their accounts in accordance with the fair value accounting rules (as set out in the Companies Act 1985), specifies the treatment of gains and losses on the disposal and revaluation of financial instruments. A conflict may therefore arise between FRS 3 and FRS 26 for insurance entities applying FRS 26. For example, FRS 26 would require that unrealised gains and losses on an insurance company's financial asset that is classified as available for sale (AFS) are recognised in the statement of total recognised gains and losses. On subsequent sale or realisation of the AFS asset, the gains or losses would be recycled through the profit and loss account. As stated above, however, FRS 3 would require that such unrealised gains and losses on investments are included as part of the investment return in the profit and loss account.

Accordingly, the UITF has recommended that the ASB makes a limited amendment to FRS 3 to clarify that certain paragraphs of the standard do not apply to the financial instruments of entities within the scope of FRS 26. Therefore, any unrealised gains and losses on insurance entities' financial assets classified as AFS are recognised in the statement of total recognised gains and losses in accordance with FRS 26.

The UITF's Information Sheet is available on the Web at

[www.frc.org.uk/asb/uitf/pub1223.html](http://www.frc.org.uk/asb/uitf/pub1223.html)



## Heritage assets

The ASB has issued FRED 40 *Accounting for Heritage Assets*. The FRED was developed from the Discussion Paper *Heritage Assets: Can Accounting Do Better?*, issued in January 2006. Comments on the exposure draft are requested by 20 April 2007.

The proposals in the FRED require entities, wherever practical, to report collections of heritage assets at valuation in their annual accounts. Heritage assets are defined as assets which have historic, artistic, scientific, technological, geophysical or environmental qualities that are held and maintained principally for their contribution to knowledge and culture. Where it was not practicable to obtain valuations which provide relevant information sufficient to assist in an assessment of the value of the collection at the balance sheet date, the collection would not be recorded on the balance sheet. This assessment would be made on a collection by collection basis, rather than for the entity's assets overall. Enhanced disclosures are proposed, however, regardless of whether the collection is recorded on the balance sheet.

The proposals are intended to address criticisms of current financial reporting of heritage assets, which involves many entities adopting an approach under which assets purchased in 2001 and subsequently are recorded in the balance sheet at cost. Assets acquired prior to that date are not recorded; the assets recorded in the balance sheet therefore bear no resemblance to the value of the entire collection. Many of the entities that hold heritage assets are charities and it is expected that proposals to amend the Statement of Recommended Practice (SORP) Accounting and Reporting by Charities, will be published in due course.

The ASB's exposure draft is available on the Web at

[www.frc.org.uk/asb/press/pub1215.html](http://www.frc.org.uk/asb/press/pub1215.html)



## IFRS newsletters

KPMG IFRG Limited has published the following since the November/December 2006 *Update*, which are available on our Web site at [www.kpmg.co.uk](http://www.kpmg.co.uk):

- *IFRS in Brief*, December 2006 – a summary of the November 2006 meeting of the IASB
- *IFRS Briefing Sheet*, Issue 58 – IFRS 8 Operating Segments
- *IFRS Briefing Sheet*, Issue 59 – IFRIC 12 Service Concession Arrangements
- *IFRS Briefing Sheet*, Issue 60 – Discussion Paper: Fair Value Measurements

If you would like further information on any of the matters discussed in this *Update*, please talk to your usual contact at KPMG LLP (UK) or call any of our offices. Earlier *Updates* are available on our Web site, at [www.kpmg.co.uk](http://www.kpmg.co.uk).

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