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FRS 102

The 5 Most Common Mistakes Applying FRS 102

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FRS 102

Accounting for preference shares – All too often incorrectly accounted for

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Extracts from Section 22 Detailed Guide

Section 22-Liabilities and Equity – Extracts

22.2.2.1 Definition of financial liability

As per section 22.3 of FRS 102 a financial liability is any liability that is:

(a) a contractual obligation:

(i) to deliver cash or another financial asset to another entity; or

(ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the entity; OR

(b) a contract that will or may be settled in the entity's own equity instruments and:

(i) under which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; OR

(ii) which will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose, the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

As can be seen from the definition of a financial liability in Section 22.3 of FRS 102 above, the key question when assessing whether an item is classed as debt or equity is if:

- Ignoring share settlement, the issuer does not have an unconditional right to avoid delivering cash or another financial asset to settle a contractual obligation, the obligation meets the definition of a liability with the exception of a puttable instrument and an obligation on liquidation that meet the criteria in Section 22.4 of FRS 102 for further details. where classified as debt See liability under section 22.

22.2.2.2 Definition of equity

Equity is defined in section 22.3 of FRS 102 in short as being what remains after all debt is paid/all liabilities are taken into consideration. In essence it is the share capital which does not meet the definition of liability plus accumulated profits /less accumulated losses and any other contributions from shareholders

22.2.3 Accounting treatment of instruments classified as debt

Shares which are deemed to be debt are usually accounted for in line with Section 11 i.e. at amortised cost or where there is a derivative element or it does not meet the definition of basic as stated in section 11.9 of FRS 102 under Section 12 at fair value. In nearly all cases they will be valued at amortised cost however certain state funded organisations do require preference shares to be issued to them where the liability component is considered complex and therefore accounted for under Section 12.

22.2.3.1 Instruments made up of debt and equity – compound financial instruments or an instrument classified as liability and at non-market rates.

Where some of an instrument is made up of debt and some is made up of equity, then the debt element will be accounted for in accordance with section 11 or 12 as stated at 22.2.3 and the equity element accounted for in line with section 22 as detailed at 11.8.2. Where this situation arises, the instrument is known as a compound financial instrument. See an example of the accounting for same at 22.2.6.9 and 22.7.2.6

Where a loan note or shares are subscribed for and a below market rate is charged and these are classified as a liability under section 22, and it meets the definition of a basic financial instrument in section 11 of FRS 102 at 11.5.2, then in line with section 11 rules there is a requirement to present value the cash flow of a market rate of interest. Where the difference between the present value amount and the actual amount subscribed is recognised depends on the facts and circumstances. If the subscriber is an existing shareholder, then the difference should be recognised in equity. Alternatively, if the subscriber is a new investor then it should be recognized in the profit and loss account. See an example at 22.2.6.9 If the

debt element does not meet the definition of basic in section 11 and instead it is complex and must be accounted for at fair value under the rules of section 12 (if permitted under IFRS) then the difference would have to go to the profit and loss, it would not be recognised in equity. See section 12 for further details.

22.2.4 Mandatory requirements to pay dividends even if no distributable reserves when classified as a liability

NOTE: IN RELATION TO THE MANDATORY REQUIREMENT TO PAY DIVIDEND, IT IS IRRELEVANT WHETHER THE COMPANY HAS DISTRIBUTABLE RESERVES TO PAY THE DIVIDEND. The dividend should still be accrued in the financial statements. Also, in relation to the requirement to repurchase the shares, the fact that the entity has no distributable reserves is not taken into account. Just because there is not distributable reserves or there is insufficient cash, does not prevent the dividend from being accrued. Obviously, the dividend cannot be paid to the holder until the company has distributable reserves however as it is contractually payable, the instance distributable reserves arise then they must be paid.

Where a financial instrument is classified as debt, the dividend/interest accrued or paid on the loan notes preference shares/loan notes are classified as an interest cost in the financial statements. The preference dividend which is mandatory where not paid should be accrued as the entity is contractually obliged to pay this in the future.

22.2.5 Treatment of dividend on instruments classified as equity

Where the instrument is classified as equity the dividend paid is posted to equity/profit and loss reserves. A dividend declared on an equity share cannot be accrued unless it has been approved by the members in an AGM prior to the year end. If it has not it should not be accrued. Note if a coupon rate is on a share but it is at the discretion of the issuer as to whether to pay it or not, then these shares would be classified as equity. See example at 22.2.6.6.

22.2.6 Examples illustrating whether an instrument meets the definition of debt or equity

Note in any of the examples below, we use preference shares however the shares could be called whatever they like i.e. 'A' ordinary shares, bonds etc., it is the rights attaching to the instrument that matter. The examples below detail the majority of alternatives that entities may come across in practice and explains the points in the standard above.

22.2.6.1 Redeemable preference shares at option of the holder with mandatory coupon

Example 1: Redeemable preference shares at option of the holder with mandatory coupon

Company A issued 200,000 10% preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- 10% dividend must be paid annually in arrears i.e. CU20,000 mandatory
- The preference shares are redeemable at their par value at the option of the holder at some time in the future.

Given that Company A has a contractual obligation to pay a dividend yearly and is contractually obliged to redeem the shares, these shares would be classified as debt in Company A's financial statements. The journals required on issue would be to:

	CU	**CU**
Dr Bank	200,000	
Cr Preference Shares Liability		200,000

The journal required at the end of each year for the dividend payable is:

	CU	**CU**
Dr Interest Expenses with Preference Dividend	20,000	
Cr Bank/Preference Dividend Accrual		20,000

22.2.6.2 Non-redeemable preference shares with mandatory coupon at market rate

Example 2: Non-redeemable preference shares with mandatory coupon at market rate

Company A issued 200,000 10% preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- 10% dividend must be paid annually in arrears i.e. CU20,000 mandatory
- The preference shares are non-redeemeable or redeemable at the option of the issuer (i.e. Company A) at any time

Given that Company A has a contractual obligation to pay/accrue a dividend yearly, these shares would be classified as debt in Company A's financial statements as the stream of cash flow is into perpetuity. The journals required in this case are the same as example 1 at 22.2.6.1.

22.2.6.3 Non-redeemable preference shares with mandatory coupon at non-market rate or at market rate with option of entity to pay additional dividends

Example 3: Non-redeemable preference shares with mandatory coupon at non-market rate or at market rate with option of entity to pay

Company A issued 200,000 10% preference shares of CU1 each in return for CU200,000. The market coupon rate on such shares should be 12%. The rights attaching to the shares are such that:

- 10% dividend must be paid year on year i.e. CU20,000 mandatory
- The preference shares are non-redeemeable or redeemable at the option of the issuer (i.e. Company A) at any time

In this particular circumstance, there is both a liability and equity component to these shares. This is in effect a compound financial instrument. The liability element being the mandatory present value of the dividend payable into perpetuity and equity element being the residual. Therefore a certain element of the proceeds will be shown in equity and liabilities. See section on compound financial instruments below (example 17) at 22.11.2.6 and example 9 at 22.2.6.9.

Note if the above example was at market rate but it also contained rights which stated that additional dividends on top of the coupon rate may be paid at the discretion of the board, it would also be a compound instrument and the market rate for an instrument with the additional option would have to be applied so as to ascertain the liability and equity component. The difference here between 22.2.6.2 and the example here is that the coupon rate was not at a market rate here.

22.2.6.4 Shares/loan notes redeemable at the option of the holder

Example 4: Shares/loan notes redeemable at the option of the holder (i.e. a type of share/loan note which meets the definition of debt)

'Ordinary shares' that can be converted into debt (i.e. a type of share /loan note which meets the definition of debt), based on fair value of the shares at the date of conversion at the option of the holder

Here this is accounted for as a financial liability on the basis that once converted which is at the option of the holder, there is a contractual obligation to redeem for cash, hence the issuer cannot avoid paying in cash (meets definition of a liability in section 22.3 of FRS 102).

22.2.6.5 Non-redeemable preference shares with discretionary dividend

Example 5: Non-redeemable preference shares with discretionary dividend

Company A issued 200,000 preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- Dividend is payable at the discretion of the company

- The preference shares are non-redeemable

Given that company A has no contractual obligation to redeem or pay dividends, this should be classified as equity in the financial statements. The journal required on issue of the shares are:

	CU	**CU**
Dr Bank	200,000	
Cr Equity –Preference Share Capital		200,000

Where a discretionary dividend is paid on these equity shares the journal required is to:

	CU	**CU**
Dr Equity-Profit and Loss Reserves	XXX	
Cr Bank		XXX

If the dividend was approved by the members prior to the year end, then the dividend can be accrued.

22.2.6.6 Redeemable preference shares at option of issuer with discretionary dividend

Example 6: Redeemable preference shares at option of issuer with discretionary dividend

Company A issued 200,000 preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- Dividend are payable at the discretion of the company

- The preference shares are redeemable at the issuers option at some future date

Given that Company A has no contractual obligation to pay cash, (does not meet the definition of financial liability in section 22.3 of FRS 102) this should be classified as equity in the financial statements. The treatment of any discretionary dividends are posted to equity as in example 5 at 22.2.6.5 above. Note even if there was a coupon attached to these preference shares that was only payable at the option of the Company, they would still be classed as equity. Whether the company has a history of paying dividends in the past is irrelevant, it would still be classed as equity as it does not have a contractual obligation to make the dividend payment.

22.2.6.7 Redeemable preference shares at option of issuer with mandatory dividend

Example 7: Redeemable preference shares at option of issuer with mandatory dividend

Company A issued 200,000 10% preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- 10% dividend must be paid annually in arrears i.e. CU20,000 mandatory

- The preference shares are redeemable at the issuers option at some future date

Here assuming the coupon rate of 10%, is the market rate on issue, as Company A has a contractual obligation to pay/accrue a dividend annually, this would be classified as a financial liability. See example 3 at 22.2.6.3 for how this would be accounted for if the rate was a non-market rate.

22.2.6.8 Mandatory redeemable preference shares/loan note at fixed amount at a fixed or future date with mandatory dividend

Example 8: Mandatory redeemable preference shares/loan note at fixed amount at a fixed or future date with mandatory dividend

Company A issued 200,000 10% preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- 10% dividend must be paid annually in arrears i.e. CU20,000 mandatory
- The preference shares are redeemable at a fixed or future date

Given that Company A has a contractual obligation to pay/accrue a dividend yearly and that the must be redeemed in the future, these shares would be classified as debt (section 22.3 of FRS 102) in Company A's financial statements. The journals required in this case are the same as example 1 at 22.2.6.1.

22.2.6.9 Mandatory redeemable preference shares/loan note at fixed amount at a fixed or future date with dividend payable at the discretion of the issuer

Example 9: Mandatory redeemable preference shares/loan note at fixed amount at a fixed or future date with dividend payable at the discretion of the issuer

Company A issued 200,000 preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- Dividend is payable at the discretion of the company
- The preference shares are mandatory redeemable at a fixed or future date

Here this is in fact a compound instrument as it contains both an equity and liability component. The liability component is the present value of the redemption amount and equity component is equal to the proceeds less liability component. Any dividends paid are taken to relate to the equity component. The present value rate that should be used is the rate that would be charged by a bank for period up to the mandatory redemption date on a similar instrument.

For example assume in the above example, it is mandatory redeemable at the end of year 5 and the market rate of interest for a similar loan would be 8%. Then the present value of CU200,000 is CU136,117 (CU200,000/((1.08^5)). Therefore the amount to be recognised as a liability is CU136,117 and the amount to be recognised in equity is CU63,883. The journal required on intial recognition is:

	CU	**CU**
Dr Bank	200,000	
Cr Preference Share Liability		136,117
Cr Equity		63,883

22.2.6.9.1 Treatment of difference between present value ad actual amount subscribed for

NOTE when assessing where the difference between the liability component and the amount given to subscribe for the shares, one needs to assess who the shares are being issued to. If the shares are being issued to an existing shareholder, then the difference will be recognised in equity as in this example - if the shares/loan rate is issued to a new investor then the difference (i.e. CU 63,883 in his example) should be recognised as a gain in the profit and loss account.

The CU136,117 is then amortised at the effective interest rate of 8% over the 5-year period as per below

Year	Opening balance	Capital element	Interest for Period 8%	Cash flow	Closing balance
1	136,117	136,117	10,889	-	147,006
2	147,006	147,006	11,760	-	158,766
3	158,766	158,766	12,701	-	171,468
4	171,468	171,468	13,717	-	185,185
5	185,185	185,185	14,815	(200,000)	-

Therefore the journal that would be posted at end of year 1 would be:

	CU	CU
Dr Interest Cost	10,889	
Cr Preference Share Liability		10,889

If a dividend was declared and paid on these shares of CU10,000 during year 1 for example, the following journal would be posted:

	CU	CU
Dr Equity-Profit and Loss Reserves	10,000	
Cr Bank		10,000

22.2.6.9.2 Impact of dividend added to redemption amount if declared, even if not mandatory dividend.

However, where any unpaid dividend is added to the redemption amount and this is included in the share rights, the whole instrument is classed as a liability component i.e. CU200,000 and the dividend accrued increases the liability.

22.2.6.10 Redeemable preference shares at holder's option at some future date with dividend payable at the discretion of the issuer

Example 10: Redeemable preference shares at holder's option at some future date with dividend payable at the discretion of the issuer

Company A issued 200,000 preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- Dividend is payable at the discretion of the company
- The preference shares are redeemable at some future date at the option of the holder

Here this is in fact a compound instrument as it contains both an equity and liability component assuming that it does not meet the definition in section 22.4 of FRS 102 (i.e. a puttable instrument in an entity which has a very limited life in which case it would all be classed as equity). The liability component is the present value of the redemption amount and equity component is equal to the proceeds less liability component. Any dividends paid are taken to relate to the equity component. The present value rate that should be used is the rate that would be charged by a bank for period up to the mandatory redemption date. See example 9 at 22.2.6.9 for further details.

However, where any unpaid dividend is added to the redemption amount and this is included in the share rights, the whole instrument is classed as a liability component i.e. CU200,000.

22.2.6.11 Preference shares with dividends payable at the discretion of the issuer and only redeemable on the liquidation of the company

Example 11: Preference shares with dividends payable at the discretion of the issuer and only redeemable on the liquidation of the company

Company A issued 200,000 preference shares of CU1 each in return for CU200,000. The rights attaching to the shares are such that:

- Dividend is payable at the discretion of the company
- The preference shares are redeemable on the liquidation of the company

Here these shares would be classed as equity as per Section 22.3A(b) of FRS 102 on the basis that every share becomes repayable on a liquidation even ordinary shares.

If in this example, the shares were redeemable on the appointment of a receiver or administrator these would then be classified as a financial liability.

22.2.6.11A Preference shares/bonds convertible with a mandatory coupon redeemable at the option at the holder, into a fixed number of ordinary shares at any time up to maturity (see example 17 at 27.11.2.6)

Example 11A: Preference shares/bonds convertible with a mandatory coupon redeemable at the option at the holder, into a fixed number of ordinary shares at any time up to maturity (see example 17 at 27.11.2.6).

22.2.6.12 Preference shares/loan notes issued which can be redeemed/converted for no set number of shares in the future but based on amount subscribed

Application of Section 22.3(b)(i) of FRS 102

In relation to Section 22.3(b)(i) of FRS 102 it is clear that where a variable number of shares are to be issued from an entity's own equity, these are classified as equity. An example of the application of this section is detailed in the example below:

Example 12: Preference shares issued which can be redeemed/converted for no set number of shares in the future but based on amount subscribed

Company A issued preference shares/loan notes of CU1 each in return for CU200,000. The shares/loan rates are redeemable/convertible after 5 years at the option of the holder into ordinary shares up to the value of CU200,000 at that date. Assume at the end of year five the price per ordinary share is CU10. No coupon applies

In this particular case it is evident that a variable number of shares will be issued to the holder on redemption depending on the value of the company at that date i.e. at the end of year five 10,000 shares will have to be issued (CU200,000/CU10=CU10,000) hence there is variability which dictates that these shares are therefore classed as a financial liability (as the holder is guaranteed to get shares equal to the value of original amount subscribed.

NOTE if in the above example the condition stated at inception stated that the preference shares/loan rates could be converted to a set number of shares as opposed to having vairability then this would be accounted for as a compound financial instrument. See example at 22.11.2.6

22.2.6.13 Fixed for fixed arrangement

Example 13: Fixed for fixed arrangement

An example of where this exemption applies is where a company receives CU10,000 from another entity/person in return for the company issuing 300 shares in itself in four years' time (with no other conditions attached (i.e. not mandatory dividend). As the holder will suffer from a loss and benefit from a gain with regard to a fall/uplift in the value of the company, this CU10,000 would be classified as equity on receipt of CU10,000. Another example is where the company issue preference shares/loan notes which are convertible into a fixed number of ordinary shares at a future date.

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What companies can apply the Section 11 exception with regard to discounting of non-market rate loans and what loans does this apply to?

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Extracts from Section 11 Detailed Guide

Section 11: Basic Financial Instruments – the small company exemption & changes in estimates to the amortised cost method - Extracts

11.6.2.4.5 – Financing Arrangement

Where a financing arrangement exists i.e. sales/purchases made at non-standard terms or where loans are provided at non market rates and not repayable on demand then the financing element needs to be separated and posted as a finance income or expense using the effective interest rate method as stated in Section 11.13 of FRS 102.

The standard is silent on how the difference between the transaction price paid or received and the present value of future payments of the future cash flows should be accounted for however example 15 to example 18 below would be indicative of how these can be accounted for.

Where a debt instrument is repayable on demand whether a market rate of interest is charged or not, then the amortised cost is effectively equal to the value of the money received or paid and any transaction costs are expensed as incurred as this represents the present value as it is repayable on demand.
NOTE: where there are no transaction costs and no financing arrangement exists then the amortised cost is the same as the actual amount received or paid, the effective interest rate is the rate stated in the agreement. If Any

11.6.2.4.5.1 Financing arrangement for small entities for loans from directors (who are natural persons) to the entity.

In May 2017 the FRC made an amendment to Section 1 of FRS 102. This inserted a new Section 1.15A into Section 1 of FRS 102. This states where a small entity meets the definition of a small company as stated in Section 280A and 280B of Companies Act 2014 and when there is a loan payable by the entity to a director or close family members which is not repayable on demand and not at market rates (i.e. a financing transaction exists), then under Section.1.15A of FRS 102, the entity has the option to carry this at the amount of the loan received less repayments, plus interest if any of each reporting date (i.e. the entity does not have to follow the rules in Section 11.13 and 11.14 (a) of FRS 102 (the entity does not have to present value the loan or hold at amortised cost). Note the above is a choice, the entity can continue to apply the full rules in Section 11 if it wishes.

If the entity previously applied the rules stated in Section 11.13 and 11.14 (a) of FRS 102 (i.e. present valued the loans at market rates) and decides in the current year to apply the exemption in Section 1.15A of FRS 102 the entity will need to restate the prior year comparatives to reflect the new accounting policy (i.e. retrospective application is required). The disclosure and method to be adopted as a result of the change in accounting policy should be disclosed in accordance with Section 10.12 of FRS 102

Note where a small entity has loans to directors or loans between companies which come within the definition of a financing transaction or loans from other parties who are not directors (and are not close family members) then the rules in Section 11.13 and 11.14(a) of FRS 102 continue to apply as Section 1.15A of FRS 102 only applies in the case of loans from directors or close family members to a company.

11.6.2.4.6 Steps in determining the effective interest rate

Example 13: loan at market rates with transaction costs (application of Section 11.12 to 11.20 of FRS 102)

Company A obtains a loan from the bank for CU100,000 on 1 January 2015. Arrangement fees of CU10,000 was charged by the bank. The loan carries a market rate of interest of 5% per annum which is charged annually. It is repayable after 5 years. Entity A would calculate the amortised cost and effective interest rate in the following way:

Step 1: Assess whether the instrument meets the definition of a basic instrument and the category it falls into

As this loan meets the definition of a debt instrument where there is no unusual interest rates, then this meets the definition of a basic debt instrument.

Step 2: Determine the method in which the debt instrument should be measured (does section 11.14 (b) apply)

As using the amortised cost basis does not create a measurement inconsistency and as this is not a group managed debt instrument where the performance of the group is evaluated on a fair value basis, then it is correct to use the amortised cost basis

Step 3: Assess if there is a financing transaction within the arrangement i.e. is the transaction at non market rates; is unusual extended credit terms provided?
Here the loan is at market rates, therefore there is no financing transaction.

Step 4: Determine amount to be recognised on initial recognition.
The amount to be recognised is the total value of the loan received of CU100,000 less the transaction costs of CU10,000 i.e. CU90,000

Step 5: Determine the effective interest rate and determine the carrying amount on subsequent measurement
The effective interest rate is the rate of interest that exactly discounts the estimated future cash flows through the expected life. In this case the rate is 7.469%. This 7.469% can be determined through trial and error or through the use of a mathematical formula in Microsoft Excel.

Calculated EIR	7.469%			
Period Ending	**Opening Balance**	**Interest for Period at 7.469% ***	**Cashflow**	**Closing Balance**
31/12/2015	90,000	6,722	(5,000)	91,722
31/12/2016	91,722	6,851	(5,000)	93,573
31/12/2017	93,573	6,989	(5,000)	95,562
31/12/2018	95,562	7,138	(5,000)	97,699
31/12/2019	97,699	7,301	(5,000)	100,000
31/12/2019	100,000	-	(100,000)	0

Step 6: Decide the journals to be posted at each period end
The journals to be posted in 2015 excluding the payment of the interest are as detailed below such that the amortised cost at 31/12/15 is CU91,722. This will be continued year on year:

	CU	**CU**
Dr Loan Liability	10,000	
Cr Bank		10,000

Being journal to recognise the arrangement fee charged

	CU	**CU**
Dr Interest Expense	CU6,722	
Cr Loan Liability		CU6,722

Being journal to recognise effective interest charge for 2015. The effective interest charge will be posted in each of the 5 years as detailed above. The CU5,000 will be set against the liability as it is paid.

11.6.2.4.7 Changes in cash flow estimates (amortised cost model)

Section 11.20 of FRS 102 states the entity shall adjust the carrying amount of the financial asset or financial liability to reflect actual and revised estimated cash flows. The entity shall recalculate the carrying amount by computing the present value of estimated future cash flows at the financial instrument's original effective interest rate. The entity shall recognise the adjustment as income or expense in profit or loss at the date of the revision. See example 13a below. This will be a common calculation as it is likely that an unforecasted cash flow is made which will then need a reassessment of the amortised cost carrying amount.

NOTE: if anything other than cashflows change then an entity will need to consider if a substantial modification has occurred. See guidance at 11.9.2.2

Example 13a: Change in estimate

If we take example 13 and assume that a repayment of CU10,000 was made at the end of year 2 (i.e. 31/12/16). Therefore the new principal to be repaid at 31/12/19 is CU90,000 and the new interest charge is CU4,500 (i.e. CU90,000*5%) for 2017 to 2019.

Calculate the net present value of estimated future cash flows as per below.

Period Ending	Cashflows	Formula to get PV factor	Discount rate at 7.469% PV factor	Present value of cash flow
31/12/2016	-	1	1	-
31/12/2017	4,500	1/(1.7469)^1	0.9305	4,187
31/12/2018	4,500	1/(1.7469)^2	0.8658	3,896
31/12/2019	4,500	1/(1.7469)^3	0.8057	3,625
31/12/2019	90,000	1/(1.7469)^3	0.8057	72,509
Total NPV				**84,218**

The actual carrying amount at 31/12/16 as per the amortised cost table above in example 13 was CU93,573. If we then take account of the additional payment of CU10,000 made on 31/12/16, the carrying amount in the financial statements is CU83,573. The difference of CU645 (CU83,573-CU84,218) is debited to the interest cost in the profit and loss account at 31/12/16.

The remaining difference of CU5,782 (CU90,000-CU84,218) is then charged to the profit and loss account over the remaining life as follows (assuming there is not a substantial modification as discussed further below):

Period Ending	Opening Balance	Interest for Period at 7.469% *	Cashflow	Closing Balance
At 31/12/2016	84,218		0	84,218
31/12/2017	84,218	6,290	(4,500)	86,008
31/12/2018	86,008	6,424	(4,500)	87,932
31/12/2019	87,932	6,568	(4,500)	90,000
31/12/2019	90,000	-	(90,000)	-

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When to recognise retrospectively adjust for a prior period error and how should this be disclosed?

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Extracts from Section 10 Detailed Guide

Section 10 – Prior period error - Extracts

10.9.2.1 Assessment and accounting for a prior period error

The point to consider in determining whether a prior year adjustment/restatement is required as a result of a prior year error is whether the error is material to the current and/or past periods (Section 10.21 of FRS 102). See 10.2.2.1 for a discussion on materiality.

As stated in Section 10.21 of FRS 102 where the error is material it must be corrected retrospectively whereby the comparative amounts are restated to correct the error or if the error was made before the start of the prior period presented, the opening balances at that date must be restated. Section 10.22 of FRS 102 makes it clear where the restatement to correct the comparative period is impracticable then it must be corrected at the start of the current period. Our view would be that it would be very rare to have a situation where this would be seen as impracticable.

As per Section 10.19 of FRS 102 a prior period error is an omission or misstatement in the financial statements for one or more prior periods from a failure to use, or misuse of:-

- Reliable information that was available up to the date of authorization of the financial statements; or
- Could reasonably be expected to be obtained and taken into account in the presentation and preparation of the accounts.

A key question to ask oneself is, if the directors had had the information up to date of sign off of the financial statements, would they have adjusted the financial statements. If the answer is yes then a prior period adjustment is required.

10.9.2.2 Disclosures of prior period errors

Section 10.23 of FRS 102 requires the entity to disclose:

- The nature of the prior period error
- For each prior period presented
    - The amount of the correction for each financial statement line affected
    - The amount of the correction at the earliest prior period presented where practicable

When disclosing this in the financial statements, the word ‘restated’ should be shown in the prior year comparatives in the balance sheet and profit and loss as well as being included at the top of any notes to the financial statements which were affected by the error.

On transition to FRS 102 as the whole of the prior year comparative will have changed since the prior period financial statements were issued, the prior year disclosure will be shown in the equity reconciliation and full details of the error provided in the notes detailing the transition adjustments. See an example of same in example 7 below.

See below the application of the above guidance.

Example 6: Prior period error

During the 31 December 2015 year end, Company A noticed that the prior year financial statements omitted stock of CU100,000 which was material to the financial statements. Stock in the same location was also omitted at year ended 31 December 2013. The inventory in this location at that time was CU95,000. Given the materiality, this error requires a prior year adjustment. Assume a corporation tax rate of 10%. The adjustments required to correct this error are:

In the 31 December 2014 accounts to restate the opening balance

	CU	CU
Dr Inventory	95,000	
Cr Profit and Loss Reserves (CU95,000-CU9,500 of current tax)		85,500
Cr Corporation Tax Liability (CU95,000*10%)		9,500

Being journal to reflect adjustment in respect of prior years' including the additional tax payable

	CU	CU
Dr Inventory	5,000	
Cr Cost of Sales		5,000
Dr Current Income Tax in P&L (CU5,000*10%)	500	
Cr Corporation Tax Liability		500

Being journal to reflect movement on stock incorrectly excluded from 2013 to 2014 and the related corporation tax payable as a result

See below an example of how this should be disclosed so as to meet the disclosure requirements.

Profit and Loss Account

	2015 CU	2014 Restated CU
Turnover	1,600,000	1,500,000
Cost of sales	(1,220,000)	(1,100,000)
Operating profit	380,000	400,000
Interest receivable	5,000	5,000
Interest payable	(1,000)	(10,000)
Profit before taxation	384,000	395,000
Tax on profit	(38,400)	(39,500)
Profit for the financial year	345,600	355,500

Balance Sheet

	2015 CU	2015 Restated CU
Fixed assets		
Tangible assets	190,000	150,000
Current assets		
Inventory	400,000	300,000
Cash at bank and in hand	360,000	150,000
	760,000	450,000
Creditors - amounts falling due within one year	(99,700)	(95,300)
Net current assets	660,300	354,700
Total assets less current liabilities	850,300	504,700
Capital and reserves		
Called up share capital presented as equity	100	100
Profit and loss account	850,200	504,600
Shareholders' funds	850,300	504,700

Prior year adjustment

Prior year adjustment - material error

The prior year adjustment is due to the omission of inventory located in an outside warehouse being excluded from the inventory at 31 December 2014 and 31 December 2013. The value of the inventory at 31 December 2014 was CU100,000 and the value of the inventory at 31 December 2013 was CU95,000. The financial statements for 2014 has been restated to correct this error.

The prior year adjustment resulted in an increase to the inventory balance at 31 December 2013 and 2014 of CU95,000 and CU100,000 respectively. This has resulted in the cost of sales for 31 December 2014 year end decreasing by CU5,000 and the profit and loss reserves increasing by CU85,500 being the net of tax adjustment and the tax charge for 2014 increasing by CU500. The effect of the restatement on each financial statement line item affected as shown.

Option 1 - Analysis of prior year adjustments	2014 CU
Cost of sales for year ended 31 December 2014	
Cost of sales as previously stated	1,005,000
Adjustment for inventory previously excluded	(5,000)
Cost of sales as restated	1,100,000
Inventory for year ended 31 December 2014	
Inventory at 31 December 2014 as previously stated	200,000
Adjustment for inventory previously excluded	100,000
Inventory as restated	300,000
Income tax expense for year ended 31 December 2014	
Income tax expense as previously stated	39,000
Tax effect on adjustment for inventory previously excluded	500
Income tax expense as restated	(39,500)
Income tax payable	
Income tax payable at 31 December 2014 as previously stated	(39,000)
Tax effect on adjustment for inventory previously excluded	(9,500)
Tax effect on adjustment for inventory previously excluded	(500)
Income tax payable as restated	(49,000)
Profit and loss reserves at 31 December 2014	
Profit and loss reserves at 31 December 2014 as previously stated	414,600
Adjustment for inventory previously excluded net of tax at 31 December 2013.	85,500
Adjustment for movement of inventory previously excluded net of tax in the 31 December 2014 year	4,500
Profit and loss reserves at 31 December 2014 as restated	504,600
Profit and loss reserves at 1 January 2014	
Profit and loss reserves at 1 January 2014 as previously stated	63,600
Adjustment for inventory previously excluded net of tax	85,500
Profit and loss reserves at 1 January 2014 as restated	149,100
Profit for the year after taxation for year ended 31 December 2014	
Profit after tax for year ended 31 December 2014 as previously stated	351,000
Movement on inventory previously excluded net of tax	4,500
Profit after tax for year ended 31 December 2014 as restated	355,500
Profit for the year after taxation for year ended 31 December 2013	
Profit after tax for year ended 31 December 2013 as previously stated	63,600
Inventory previously excluded net of tax	85,500
Profit after tax for year ended 31 December 2013 as restated	149,100

Option 2 – Analysis of prior year adjustments

The other option here is to show the prior year P&L and balance sheet with the adjustment & then the restated version as per below – you would still need the narrative in the section above,

Profit and Loss Account

	2014 As previously stated CU	Adjustments CU	2014 Restated CU
Turnover	1,500,000	-	1,500,000
Cost of sales	(1,105,000)	5,000	(1,100,000)
Operating profit	395,000	5,000	400,000
Interest receivable	5,000	-	5,000
Interest payable	(10,000)	-	(10,000)
Profit before taxation	390,000	5,000	395,000
Tax on profit	(39,000)	(500)	(39,500)
Profit for the financial year	351,000	4,500	355,500

Balance Sheet

	2014 As previously stated CU	Adjustments CU	2015 Restated CU
Fixed assets			
Tangible assets	150,000	-	150,000
Current assets			
Inventory	200,000	100,000	300,000
Cash at bank and in hand	150,000	-	150,000
	450,000	100,000	450,000
Creditors - amounts falling due within one year	(85,300)	(10,000)	(95,300)
Net current assets	354,700	90,000	354,700
Total assets less current liabilities	504,700	90,000	504,700
Capital and reserves			
Called up share capital presented as equity	100	-	100
Profit and loss account	504,600	90,000	504,600
Shareholders' funds	504,700	90,000	504,700

Statement of changes in Equity or Movement in profit and loss reserves note

Note the lines **'**Prior year adjustment – change in accounting policy (see note X)' is just included for illustrative purposes

	Called up Share Capital CU	Profit and Reserves CU	Total Equity CU
Balance at 1 January 2014 as previously reported	100	63,600	63,600
Prior year adjustment – change in accounting policy (see note X)	-	-	-
Prior year adjustment – correction of material error (see note X)		85,500	85,500
Balance at 1 January 2014 as restated	100	149,100	149,100
Profit for the year as previously reported		351,000	351,000
Prior year adjustment – change in accounting policy (see note X)	-	-	-
Prior year adjustment – correction of material error (see note X)		4,500	4,500
Profit for the year as restated (see note X)		355,500	351,000
Balance at 31 December 2014	**100**	504,600	504,700
Balance at 1 January 2015	**100**	**504,600**	**504,700**
Profit for the year		345,600	345,600
Balance at 31 December 2015	**100**	**850,200**	**850,300**

Note the inventory comparative figures would also be update and the word 'Restated' would be included under the comparative year as was done for the profit and loss and balance sheet above. Note the above shows a statement of changes in equity however a movement on profit and loss reserves note is only required if Section 1A is applied. So therefore, the P&L reserves column would only be required here.

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FRS 102

Consolidation and golden shares – how to do we account for these and what is the basis?

www.FRS102.com

Extracts from Section 9 Detailed Guide

9.3.2.2 Definition of a subsidiary and control

As per section 9.4 of FRS 102 in order for an entity to have control (and therefore for the entity to be classified as a parent with a parent subsidiary relationship) it must have:

- The power over the financial and operating policies (see 9.3.2.2.1); and
- Benefits must be obtained as a result of that power from the entities activities (see 9.3.2.2.2)

Section 9.5 of FRS 102 makes it clear that control is presumed where greater than 50% of the voting power is held by an entity. However control can also exist when the parent owns 50% or less of the voting power but it has:

- power over more than half of the voting rights by virtue of an agreement with other investors; or
- power to govern the financial and operating policies of the entity under a statute or an agreement; or
- power to appoint or remove the majority of members of the board of directors or equivalent (i.e.a golden share agreement); or
- power to cast the majority of votes at meetings of the board of directors; or
- having options or convertible instruments which are exercisable at the date of acquisition.

9.3.2.2.1 Strategic, financial and operating decisions

Although FRS 102 does not define what the strategic, financial and operating decisions would cover, these are generally understood to include areas such as:

- budgeting
- capital expenditure
- treasury management
- dividend policy
- production
- marketing
- sales and human resources
- decisions of acquiring or disposal of significant assets
- a right to block customary or expected dividends
- decisions over liquidation of the company
- issuance and repurchase of equity shares.

The most important here is the control over distributions and the reinvestment decisions.

9.3.2.2.2 Interpretation of benefits to be obtained as a result of power to control

In relation to the benefit test, this does not specifically mean the benefits from ownership but also relates to other benefits such as brand related goodwill generating more customers, cost savings, access to new customers etc.

9.3.2.2.3 Power to control even if not exercised

In determining control, the key thing to consider is whether the entity has the power to govern the entity, it is irrelevant whether they exercise this control or not. Section 9.6 of FRS 102 refers

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Example 1: Exercise of dominant influence

Company A owns 60% of the voting rights of Company B. However Company A allows the other investor who owns the remaining 40% to run Company B with little or no input from Company A. In this case although Company A is not getting involved in the financial and operating policies this is irrelevant when assessing control, as the key point is that they have the ability if Company A wanted to prevent the other investor from making decisions.

9.3.2.3 Potential voting rights

When assessing whether control exists, an entity should not only review all shares/rights held at that point in time but also options/rights which are exercisable at that point in time (Section 9.6 of FRS 102). If voting rights cannot be converted or exercised until a future date these are not considered in determining whether control exists.

Example 2: Potential voting rights

Company A owns 40% of the share capital and voting rights of Company B. It also hold 100% preference shares in Company B which provide a right to a dividend of 5% per annum. These preference shares can be converted at the option of Company A into ordinary shares after 3 years time which would result in the Company obtaining more than 50% of the voting rights (assume 70%).

With regard to the convertible rights here, these cannot be considered by Company A in the control test until after 3 years. So for the first three years assuming Company A does not have the ability to control the composition of the board, Company A would not control Company B and therefore it is not a subsidiary.

However after year 3, even if Company A does not exercise its right to convert at that time, in assessing whether control exists, these exercisable rights should be taken into account and therefore Company B would be a subsidiary of Company A from that date. Note if the option is not exercised after the three years in the consolidated financial statements 60% of the net assets would be allocated to non-controlling interests as that is what the NCI owns at that point in time as the options have not been exercised.

Where the rights are exercisable/convertible in the very near future they may be taken into account so if this is the case judgement will need to be exercised. In addition consideration should be given as to whether an entity will be able to exercise dominant influences i.e. do they have the financial resources etc. to convert rights into shares.

9.3.2.4 Less than 50% of share capital held but still have control

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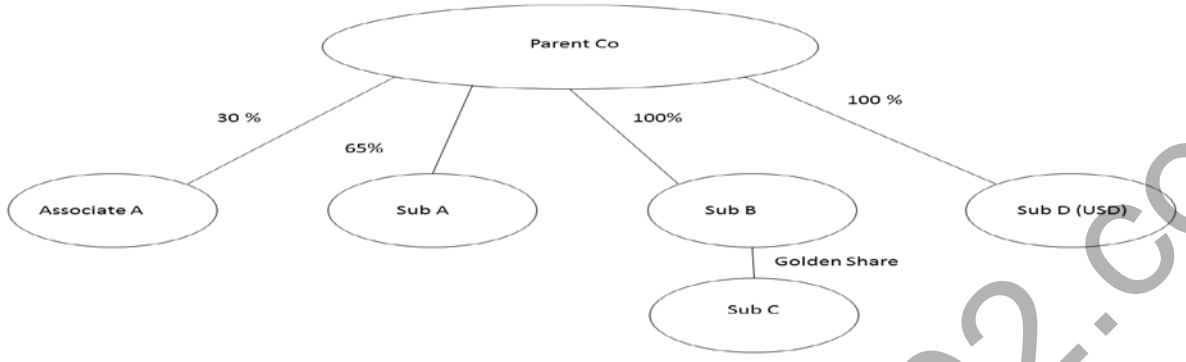
Example 3: Ability to control composition of the board

Company A owns 40% of Company B with the remaining 60% held by another party. However, Company A also holds one golden share which gives Company A the right to control the composition of the board of directors.

In this situation as the board of directors dictate the financial and operating policies of the company since Company A has the ability to appoint or force directors to resign this gives Company A control and therefore Company B is a subsidiary of Company A. In the consolidated financial statements 60% of the net assets would be allocated to non-controlling interests.

Example – Consolidations and golden shares

Question
Group structure:



The golden share held in subsidiary C was acquired 2 years ago for €1 which gives the company the ability to control the composition of the board. The book value of the net assets at that date was €300,000 (split €50,000 ordinary share capital; €20,000 share premium and €230,000 profit and loss reserves). The net assets at the start of the current year are €360,000. Details of the results for the year are as follows:

	Parent Co	Sub A	Sub B	Sub C	Sub D
	2014	2014	2014	2014	2014
	€	€	€	€	€
Turnover	-	5,000,000	11,902,422	3,000,000	187,500
Cost of sales	-	(4,000,000)	(8,117,700)	(2,500,000)	(93,750)
Gross profit	**0**	**1,000,000**	**3,784,722**	**500,000**	**93,750**
Distribution costs	-	(70,000)	(2,610,451)	-	-
Administrative expenses	-	(700,000)	(899,152)	(450,000)	(37,500)
Income from participating interest	3,500	-	-	-	
Income from group undertakings	45,000	0	0	0	
Operating profit	**48,500**	**230,000**	**275,119**	**50,000**	**56,250**
Share of profit in associate	-	0			
Interest receivable and similar income	-	2,000	22,422	800	0
Interest payable	-	(1,500)	(2,628)	-	0
Profit before taxation	**48,500**	**230,500**	**294,913**	**50,800**	**56,250**
Taxation	-	(28,813)	(149,787)	6,350	-
Profit for the financial year	**48,500**	**201,687**	**145,126**	**57,150**	**56,250**
Other Comprehensive Income					
Retranslation of goodwill on foreign operation	-	-	-	-	
Retranslation of foreign operation	0	0	0	0	15,000
Share of other comprehensive of associate	0	0	0	0	
Profit for the financial year	**48,500**	**201,687**	**145,126**	**57,150**	**71,250**
Profit for the financial year attributable to:					
Non-controlling interests	0	0	0	0	
Owners of the parent company	0	0	0	0	
	-	-	-	-	-

Solution
Calculation of goodwill and fair value adjustments on Subsidiary C and derecognition of investment on the Parent balance sheet:

Golden share exists here – therefore all results and assets are attributable to the non-controlling interest

Journals required in the consolidated financial statements at the date of acquisition:

	€	**€**
Dr Ordinary Share Capital of Subsidiary C	50,000	
Dr Share Premium	20,000	
Dr Profit and Loss Reserves (i.e. profit and loss reserves in existence at date of acquisition)	230,000	
Cr Investment in the Individual Entity Financial Statements of Subsidiary B		1
Cr Non-Controlling Interest in Equity (i.e. fair value of net assets of subsidiary at the date of acquisition * 100% owned at date of acquisition)		299,999

Being journal to recognise Subsidiary C at fair value at the date of acquisition and eliminate the investment on the parent balance sheet

	€	**€**
Dr Group Profit and Loss Reserves B/f	60,000	
Cr Non-controlling Interest (€60,000 * 100%)		60,000

Being journal to reflect the correct amount in NCI at the start of the current year for Subsidiary C

Current Year

	€	**€**
Dr Group Profit and Loss Reserves B/f	57,150	
Cr Non-controlling Interest (€57,150 * 100%)		57,150

Being journal to reflect the transfer of the NCI portion of the result of Subsidiary C for the period

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FRS 102

How to account for grants previously recognised under the accruals model on transition to SORP FRS 102

www.FRS102.com

Extracts from SORP FRS 102 Detailed Guide

SORP FRS 102 – The performance model – Extracts

4) Grants of all natures **(including optional grants) – Performance model**

NOTE FULL FRS 102 SORP ONLY PERMITS THE PERFORMANCE MODEL TO BE UTILISED FOR GRANTS. FRS 102 GIVES A CHOICE TO EITHER APPLY THE PERFORMANCE MODEL OR THE ACCRUALS MODEL
Grants of all natures (including capital grants) – note change here from full FRS 102

a) If there are no performance conditions attached then recognise (ignore restriction on how the funds are to be used):

   – Immediately assuming the charity has:

      • Entitlement

      • Probable economic benefits will flow

      • Can be reliably measured

   – Even if costs have not been incurred the income must be recognised in the SOFA (applies to capital grants also)

   – If there are performance conditions attached then recognise:

      • Only when the performance conditions are met

      • Even if costs have not been incurred the income must be recognised in the SOFA (applies to capital grants also)

b) Example of performance conditions:
   – service level conditions, or
   – a set number of output to be done, or
   – opening hours of facilities, or
   – number of meals to be provided
   – Requirement to employ a certain number of staff for a set period
c) Terms attaching to a grant which can be ignored when looking if the performance conditions have been met:
   – Rules restricting the use of the funds
   – Conditions that allow for the recovery of the grant by the donor of any unexpended part of a grant:
      • Terms which are within the charity's control & there is sufficient evidence that the terms will be met. Examples include:
      • Submission of accounts or certification of expenditure
      • The requirement to hold it for charitable purposes and if sold to invest in charitable activities (as this is stated in the charity constitution then this is a given)

d) Accruals model with regard to government grants cannot be used under FRS 102 SORP (however it can be used if FRS 102 non SORP accounts are being prepared).

   – Must be recognised in income when performance conditions are met (regardless if costs have not been incurred).

Example: Grants and the performance model (Example of adjustment on transition from Accruals model to performance model when Charities SORP first adopted)

Charity A applied a policy of recognising grants on an accruals basis under FRS 102. For the year ended 31 December 2016 the charity has decided to apply Charities SORP FRS 102 for the first time. At the 31 December 2014 and 2015 the charity held a liability for deferred capital grants on the balance sheet of CU769,000 and CU719,000 respectively (as the government grants were released to the

income and expenditure statement over the life of the asset). These grants were provided on condition that the charity construct a specialist treatment unit for a certain type of beneficiary a number of years ago and on condition that it continue to be used by the charity for that purpose and if it is sold the disposals proceeds must be utilised for charitable purposes.

The amortisation credit recognised in the income and expenditure in the 2015 financial statements was CU50,000.

On adoption of the SORP the charity is required to change its accounting policy from the accruals basis to the performance basis. Given that the grants was given for a specific purpose this is a restricted grant and therefore should be recognised in a restricted fund.

From the facts above it is evident that under the performance basis the charity has complied with grant conditions and therefore the grant should have been recognised in full a number of years ago if the performance basis had of been applied. The requirement that the charity has to continue to use the property for charitable purposes does not prevent it from being recognised as this is within the control of the charity and the charity has full intention to abide by this condition.
The adjustments required are as follows:

Journals for year ended 31 December 2015:

	CU	**CU**
Dr Government grants on balance sheet	769,000	
Cr restricted fund in the 'funds of the charity' section of the balance sheet		769,000

Being journal to reflect the restatement of the prior year opening reserve balance due to the change of accounting policy

	CU	**CU**
Dr expenditure on charitable activities in SOFA with the reversal of amortisation – restricted column (assuming the amortisation was originally posted to expenses as opposed to income). This then gets recognised in the restricted fund in the 'funds of the charity' section of the balance sheet which reflects the depreciation on the cost element of the asset covered by the grant	50,000	
Cr Government grants on balance sheet		50,000

Being journal to reflect the restatement of the prior year results for the reversal of amortisation charged on government grants due to the change of accounting policy and instead reflect this as depreciation

OR

	CU	**CU**
1) Dr income with the reversal of amortisation (assuming the amortisation was originally posted to income as opposed to expenses).	50,000	
2)*Dr expenditure on charitable activities – restricted fund	50,000	
2) Cr expenditure on charitable activities		50,000
1) Cr Government grants on balance sheet		50,000

Being journal to reverse the amortisation of the capital grant recognised in 2016 and reflect the depreciation on the cost element of the asset covered by the grant being shown in the restricted fund.

*Journal 2 above reflects the reclassification of depreciation on the cost element of the asset covered by the grant from unrestricted as previously reported under FRS 102 to restricted. This then gets recognised in the restricted fund in the 'funds of the charity' section of the balance sheet.

The journals required in the 2016 year assuming the 2016 trial balance was not prepared under SORP and the above journals were posted to reserves etc.:

	CU	CU
Dr expenditure on charitable activities in SOFA with the reversal of amortisation – restricted column (assuming the amortisation was originally posted to expenses as opposed to income). This reflects the depreciation on the cost element of the asset covered by the grant. Then this gets recognised in the restricted fund in the 'funds of the charity' section of the balance sheet	50,000	
Cr Government grants on balance sheet		50,000
Being journal to reverse the amortisation of the capital grant recognised in 2016		

OR

	CU	CU
1) Dr income with the reversal of amortisation (assuming the amortisation was originally posted to income as opposed to expenses).	50,000	
1) Cr Government grants on balance sheet		50,000
2) Dr expenditure on charitable activities - restricted fund	50,000	
2) Cr expenditure on charitable activities - unrestricted fund		50,000

Being journal to reverse the amortisation of the capital grant recognised in 2016 and reflect the depreciation on the cost element of the asset covered by the grant being shown in the restricted fund

*Journal 2 above reflects the reclassification of depreciation on the cost element of the asset covered by the grant from unrestricted as previously reported under FRS 102 to restricted. This then gets recognised in the restricted fund in the 'funds of the charity' section of the balance sheet.

Illustration in the SORP financial statements:

1. PRIOR PERIOD ADJUSTMENT – CHANGE IN ACCOUNTING POLICY (IF APPLICABLE)

Previously the company applied FRS 102 as its accounting framework but did not apply the Statement of Recommended Practice "Accounting and Reporting by Charities" effective 1 January 2015. As a result of adopting the Charities SORP (FRS 102) in the current period a change in accounting policy was required so as to ensure compliance with the Charities SORP FRS 102.

Under FRS 102 the company adopted an accounting policy to recognise all grants on an accruals basis as opposed to on a performance basis. However, under the FRS 102 Charities SORP all grants including capital grants should be recognised as income in the SOFA on a performance basis (i.e. when the charity has entitlement to the funds, any performance conditions attached to the grants have been met, it is probable that the income will be received and the amount can be measured reliably). Given that the Charities SORP (FRS 102) represents best practice for all charities as it seeks to provide information relevant to the understanding of the directors and the performance and financial position of the Charity the directors believe the change in accounting policy is required.

As a result of the change in accounting policy from the accruals basis to the performance basis it has resulted in:

- the amount previously recognised as deferred income on the balance sheet at 31 December 2014 and 2013 of €719,000 and €769,000 respectively being released to a restricted fund within charity's funds where the grant was given for a specific purpose **OR** to a general fund where the grants were not required to be applied for a specific purpose. The reason for this is that this €719,000 and €769,000 respectively would previously have been recognised in the SOFA had the performance model been applied from inception. If the performance basis had of being applied from inception this income would have been released to the SOFA in the years 201X, (€XXX) and 201X (€XXX) respectively.

- the amortisation credited/recognised in income **OR** in expenses in the year ended 31 December 2014 of €50,000 on capital grants accounted for under the accruals model being reversed.
- the depreciation of €XXXX on the element of the fixed asset cost covered by the grant being allocated to restricted funds in the SOFA from the unrestricted fund.
- the recognition of additional income in the SOFA of €XXX with regard to grants received for capital purposes where the conditions of the grant were complied with which was recognised as deferred income on the balance sheet under the accruals model previously (**for illustrative purposes**).

The impact of applying the performance model as opposed to the accruals model for the current year is that:

- additional income of €100,000 has been recognised in the SOFA with regard to capital grants received where the performance conditions have been met which previously would have been deferred and included in deferred income under the accruals model; and
- the amount recognised in expenditure on charitable activities would have been €55,000 lower for the amortisation that would have been released on the capital grants under the accruals model.
- there would be no requirement to show the depreciation on the element of the fixed asset cost covered by the grant being allocated to restricted funds in the SOFA.

Below is the analysis of the adjustments to the SOFA and the balance sheet in the comparative year:

BALANCE SHEET	**As previously stated 2014 €'000**	**Prior year Adjustment €'000**	**As Restated 2014 €'000**
Fixed assets			
Tangible assets	1,500	-	1,500
Investments	996	-	996
	2,496	**-**	**2,496**
Current assets			
Stocks	-	-	-
Debtors	1,300	-	1,300
Cash at bank and in hand	500	-	500
	1,800	**-**	**1,800**
Creditors: amounts falling due within one year	**(577)**	**-**	**(577)**
Net current assets	**1,223**	**-**	**1,223**
Total assets less current liabilities	**3,719**	**-**	**3,719**
Capital grants	**(719)**	**719**	**-**
Provision for liabilities	**-**	**-**	**-**
Total net assets	**3,000**	**719**	**3,719**
The funds of the charity:			
Restricted funds	-	719	719
Unrestricted funds	3,000	-	3,000
Total charity funds	**3,000**	**719**	**3,719**

STATEMENT OF FINANCIAL ACTIVITIES

	As previously stated 2014 €'000	Prior year Adjustment €'000	As Restated 2014 €'000
Income from:			
Donations and legacies	2,400	-	2,400
Charitable activities	1,500	-	1,500
Other trading activities	105	-	105
Investments	2	-	2
Other income	-	-	-
Total income	**4,007**	**-**	**4,007**
Expenditure on:			
Raising funds	1,636	-	1,636
Charitable activities	1,225	50	1,275
Total expenditure	**2,860**	**50**	**2,910**
Net gain on investments	3	-	3
Net income for financial year	**1,150**	**50**	**1,100**
Transfer between funds	**-**	**-**	**-**
Net movement in funds	**1,150**	**50**	**1,100**
Reconciliation of funds:			
Total funds brought forward	1,850	769	2,669
Total funds carried forward	**3,000**	**-**	**3,719**