

LIMITED COMPANY ACCOUNTS TUTORIAL

UPDATE ON UK ACCOUNTING STANDARDS: AUTUMN 2005

This update relates to UK standards – SSAPs and FRSs – and applies only to those students who are taking the *Drafting Financial Statements* examination in December 2005. It does *not* apply to the June 2006 and subsequent examinations, where assessment is based on international accounting standards.

A number of new FRSs have been issued recently:

- FRS 20 Share-based Payment
- FRS 21 Events after the Balance Sheet Date
- FRS 22 Earnings per share
- FRS 23 The Effects of Changes in Foreign Exchange Rates
- FRS 24 Financial Reporting in Hyperinflationary Economics
- FRS 25 Financial Instruments: Disclosure and Presentation
- FRS 26 Financial Instruments: Measurement
- FRS 27 Life Assurance

For the examination *Drafting Financial Statements* only two of these are assessable: FRS 21 and FRS 22. The page references below relate to *Limited Company Accounts Tutorial*.

There have also been some changes to FRS 2, *Accounting for Subsidiary Undertakings* and FRS 5, *Reporting the Substance of Transactions*. The changes made are *not* assessable for *Drafting Financial Statements*.

FRS 21, Events after the Balance Sheet Date, supersedes SSAP 17 (see page 142) but is very similar in content. The standard covers the period between

- the end of the financial year, and
- the date the financial statements are authorised for issue (usually by approval of the board of directors)

During this period there may be

- adjusting events, which require changes to the amounts shown in the financial statements
- non-adjusting events, which are disclosed by way of notes to the financial statements explaining the nature of the event and an estimate of its financial effect.

Examples of both adjusting events and non-adjusting events are given on pages 142 and 143 of *Limited Company Accounts Tutorial*. Note that dividends proposed after the balance sheet date are no longer an adjusting event: they are no longer to be reported in the profit and loss account but, instead, must be disclosed in the notes to the financial statements.

The standard requires:

- disclosure of the date the financial statements were authorised for issue
- the updating of financial statements for adjusting events
- the disclosure of material non-adjusting events, giving the nature of each event and an estimate of its financial effect

FRS 22, Earnings per share, follows very closely FRS 14 (see page 146) but has been brought into line with international accounting standard (IAS) 33.

Earnings per share relates to ordinary shares – these are equity instruments that are subordinate to all other classes of equity instruments. This means that the holders of ordinary shares will be the last to receive their money in the event of the company winding up.

The main method of calculation of earnings per share allowed by FRS 22 is the *basic method*, which is calculated as follows:

$$\frac{\text{Profit after tax}}{\text{Number of issued ordinary shares}}$$

Note that the profit (or loss) used in the calculation is the amount that is attributable to ordinary equity holders, ie after allowing for:

- tax
- minority interests
- dividends on preference shares

Two EPS calculations are required to be given:

- using the profit or loss attributable to ordinary equity holders
- using the profit or loss from continuing operations

Both of these are to be presented on the face of the profit and loss account (in practice, they are usually shown after, or below, the profit and loss account).

It is important to note that EPS is affected by the issue of additional ordinary shares during a financial year. When an issue has been made at full market price, EPS is calculated on the basis of the average number of shares in issue during the period, using the weighted average. For example:

start of financial year (1 January)	100,000	ordinary shares
new issue at full market price (1 July)	<u>50,000</u>	ordinary shares
average number of shares in issue	<u>*125,000</u>	

* 100,000 + (50,000 ÷ 2 [ie half a year])