CAPS TECHNICAL BULLETIN

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FUTURE CHANGES TO THE UK ANTI-MONEY LAUNDERING REGIME

The UK Government has made several important changes to the UK Anti-Money Laundering (AML) regime, for the following reasons:

- The UK is about to receive a Financial Action Task Force (FATF) mutual evaluation. This means the UK will shortly be assessed for its effectiveness in combatting money laundering and terrorist financing. The evaluation will commence in the summer of 2017 and complete during 2018. The UK Government is therefore taking a number of actions in advance of this evaluation to strengthen the UK AML regime.
- New regulations are needed to bring in the EU 4th Money Laundering Directive. These are called the Money Laundering Regulations 2017. (**https://www.gov.uk/government/consultations/money-laundering-regulations-2017**)
- In addition, the accountancy sector has come under recent increased scrutiny. This resulted in the Government issuing a Call For Information during 2016, for which it issued a formal response (**https://www.gov.uk/government/consultations/anti-money-laundering-supervisory-regime-response-and-call-for-further-information**) in March 2017. The Government response included a few widespread changes to accountancy sector supervision.

What are the main changes?

The pace of change is fast and we will keep you informed of ongoing developments.

The key points include:

- **The Office for Professional Body AML Supervision (OPBAS)** We have a new oversight body called OPBAS which will be responsible for ensuring consistent AML supervision amongst professional body supervisors. We are disappointed that the Government has not scoped in the default accountancy supervisor, HM Revenue & Customs (HMRC), given that we see unqualified accountants as a primary risk in the accountancy sector. This new body will levy professional bodies, and we may need to pass these increased costs on to our firms.
- **Approval process** The new regulations require that the professional bodies approve the principals and management of firms within their supervision by 26 June 2018. Criminality checks (such as Disclosure Scotland checks) on all principals and management in each firm will also be required within

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this timescale. Firms will require to keep ICAS informed of changes in principals/management.

- **Customer due diligence (CDD)** There are some changes to CDD requirements and firms will be required to conduct an overall AML risk assessment on their firm, which ICAS will require to monitor.
- **Monitoring** The scope of AML monitoring is likely to increase and there is a Government expectation that sanctions will be used more frequently.
- **Trust & Company Service Providers (TCSP)** There will be increased monitoring of TCSPs and ICAS will require to notify HMRC of all firms conducting these services, even on an incidental basis, for inclusion on a public register.

ICAS will keep you updated of any further developments, including how to go through the approval process and TCSP notification process in due course.

Firms should also expect to be asked for more AML information in the foreseeable future, via the Firms Annual Return or supplementary information requests. This will be particularly so in the lead up to the FATF Evaluation.

It is clear that we will all have a challenging time ahead. We will do all we can to keep firms informed and supported.

APPEALS, COMPLAINTS AND DISPUTES WITH HMRC – CHOOSING YOUR ROUTE

For taxpayers and their agents in dispute with HM Revenue & Customs (HMRC), there is a broad range of options. Which one is right for you? Which avenues are likely to be most cost effective, and who should undertake the work?

Looking at the problem

Before we can match the problem and the solution, we must be clear what the problem actually is. There are three broad categories:

1. Administrative failings at HMRC, such as getting no response, or systems which don't work
2. Technical disputes about tax. For example, does Entrepreneurs' Relief apply to a particular transaction?
3. Matters of judgement and uncertainty over facts. For example, what is a reasonable add back for private use? What is a fair estimate of unrecorded cash sales?

The snag is, that each problem may involve a combination of each of the above.

1. Administrative failings at HMRC

The baseline here is the HMRC Customer Charter, called 'Your Charter' **https://www.gov.uk/government/publications/your-charter/your-charter**.

This lists seven things taxpayers can expect from HMRC, and seven things HMRC expects of taxpayers (and agents).

On the HMRC side we have commitments to:

1. Respect taxpayers and treat them as honest
2. Provide a helpful, efficient and effective service
3. Be professional and act with integrity
4. Protect taxpayer information and respect their privacy
5. Accept that taxpayers can use a tax agent (someone to represent them)
6. Deal with complaints quickly and fairly
7. Tackle those who bend or break the rules

On the other side, HMRC expects taxpayers to:

1. Be honest and respect our staff
2. Work with HMRC to get things right
3. Find out what they need to do and keep HMRC informed
4. Keep accurate records and protect their own information
5. Know what their representative does on their behalf
6. Respond in good time
7. Take reasonable care to avoid mistakes

It is worth checking the details here. The charter in earlier versions used to include a commitment to "*Do all we can to keep the cost of dealing with us as low as possible and minimise costs*"!

1.1 Solutions for administrative failings at HMRC

Where administration is not working, and usual channels, like the Agent Dedicated Line **https://www.gov.uk/guidance/dedicated-helplines-and-contacts-for-authorised-agents** haven't resolved the issue, it's time to move on to the Agent Account Managers Service.

1.2 Agent Account Managers Service

The Agent Account Managers ("AAM") service is for client specific queries. You need to register before you can use it. You can do this in advance, there is no need to have a current dispute - **https://www.gov.uk/guidance/agent-account-managers-in-hmrc**.

Registration is normally per office, but only one person per office needs to register for the service to be available to everyone based at that office.

The AAM service uses an online form to make initial contact. Your query will be referred to an AAM who will work with you to resolve the issue. Reliance on an online form can be limiting as it is difficult to chase up if you receive no response.

Once your form has been accepted, you should then have a named contact at HMRC until resolution of the case. Cases are closed by HMRC through email and this can be frustrating if you consider part of the matter to be still unresolved. In such a case, you would ned to reapply on a new online form to cover the outstanding issue.

1.3 System faults

If the issue is one which you think may impact a number of agents, you can register for the HMRC Agent Forum. This forum, which replaces the local HMRC Working Together groups, enables you to post issues which are causing widespread problems. For example, issues which have been considered to date include the ability (or rather inability!) to save partly completed HMRC online forms, and issues with payment of class 2 National Insurance since its inclusion within self assessment.

You will be able to view other agent's comments and HMRC's responses, which is helpful as you can see if other agents are experiencing the same problem.

Issues raised by practitioners are given priority rating by a joint group formed of the Professional Bodies. HMRC investigates the issues raised and then reports back. The Professional Bodies then review progress. For the system to work it needs input from practitioners.

If you would like to be involved, please contact ICAS – **icas-tax@icas.com**.

1.4 Formal Complaints

Usually an initial complaint can be taken up directly with the HMRC Business Unit involved. However, when all else fails, it is time to consider a formal complaint **https://www.gov.uk/guidance/complain-to-hm-revenue-and-customs**.

There is guidance on how HMRC approaches complaints in the Complaint Handling Guidance Manual **https://www.gov.uk/hmrc-internal-manuals/complaints-handling-guidance**.

For income tax self assessment, you can complain by phone (0300 200 3310), online (**https://www.tax.service.gov.uk/forms/form/make-your-complaint-online/new**) or write to:

PAYE and Self Assessment Complaints
HM Revenue and Customs
BX9 1AB

Phone numbers and addresses for other taxes are on the Gov uk website **https://www.gov.uk/government/organisations/hm-revenue-customs/contact/complain-about-hmrc**.

Complaints may be made by agents, or by clients. The subject matter of the dispute, as well as the attitude of the client will suggest which route is best.

The key points about complaints are:

a) It is about addressing unsatisfactory, unprofessional service from HMRC.

b) Where possible, identify a specific promise in 'Your Charter' **https://www.gov.uk/government/publications/your-charter/your-charter**, which has been broken.

c) Be specific. Identify the key issues and name the solution you want.

   For example, do you want a written apology from HMRC, or for your client to be put back in the position they would have been in, had HMRC not delayed and/or made a mistake?

   Do you want a consolatory payment to be made to your client? Do you want re-imbursement of additional costs incurred as a result of HMRC's poor service?

d) Head your letter 'complaint', raise your complaint by telephone or use the online complaint form - **https://www.gov.uk/government/organisations/hm-revenue-customs/contact/complain-about-hmrc**. If contact is by phone, keep a note of the time and date of the call, the name of the person you spoke to at HMRC, and details of any actions agreed.

e) Look at the complaint from HMRC's point of view. What factors are most likely to influence their decision in your favour? Has the impact on the client been significant?

Consider looking at case studies from the Adjudicator's Office (**http://www.adjudicatorsoffice.gov.uk/casestud.htm**) when making your complaint. The Adjudicator's Annual report may also shed some light on the best grounds for complaint and possible remedies **http://www.adjudicatorsoffice.gov.uk/publications.htm**.

There is a separate route for complaints about serious misconduct by HMRC staff **https://www.gov.uk/government/organisations/hm-revenue-customs/contact/complain-about-hmrc-serious-staff-misconduct.**

HMRC's internal manual "Complaints and Remedy Guidance" gives useful information on how HMRC considers and processes complaints **https://www.gov.uk/hmrc-internal-manuals/complaints-and-remedy-guidance**.

1.5 Taking a complaint to the Adjudicator

Within six months of HMRC's final decision on a complaint, the issue can be taken to the Adjudicator **http://www.adjudicatorsoffice.gov.uk/**. The Adjudicator looks into complaints about HMRC, and the Valuation Office Agency, across the United Kingdom. The Adjudicator will look at unreasonable use of discretion by HMRC, mistakes or poor/misleading advice from HMRC, unreasonable delays, and issues of staff attitudes or behaviours.

The procedure is outlined on the Adjudicator's website **http://www.adjudicatorsoffice.gov.uk/howcomp.htm**.

Normally, a client will take the case to the Adjudicator themselves, but an adviser can give significant help in drafting an outline of the case. The Adjudicator's Office staff are often ex-HMRC employees, with considerable expertise and great willingness to assist taxpayers with their case.

Resolution is by a mediated solution where possible, but the Adjudicator will make a ruling if agreement cannot be reached. Though not legally obliged to, HMRC will normally accept the Adjudicator's verdict.

After the Adjudicator, the final option is via the taxpayer's MP to the Parliamentary and Health Service Ombudsman **https://www.ombudsman.org.uk/**.

1.6 Complaints on Scottish Taxes

The procedures outlined above are for taxes administered by HMRC. The procedure for Scottish devolved taxes is different. For partially devolved taxes, like Scottish Income Tax, and assigned taxes, like VAT, these are still administered by HMRC, so you should follow the usual HMRC complaints channels.

The Scottish procedures apply currently to Land and Buildings Transactions Tax (LBTT) and Scottish Landfill tax (SLfT), and will be joined by Air Departure Tax and Aggregates Levy in due course.

The complaints route is to Revenue Scotland via their website **https://www.revenue.scot/contact-us/making-complaint**.

Where a complaint is not resolved to the taxpayer's satisfaction by Revenue Scotland, the next stage is to contact the Scottish Public Services Ombudsman (SPSO). This can be done in person at SPSO, 4 Melville Street, Edinburgh EH3 7NS. By Post to SPSO Freepost EH641 Edinburgh EH3 0BR, or by phone 0800 377 7330.

There is also an online form **www.spso.org.uk/contact-us**. For more details see the SPSO website **www.spso.org.uk;** mobile site: **http://m.spso.org.uk**.

2. Technical disputes about tax

There are three main routes here:

- Independent HMRC review
- Alternative Dispute Resolution (ADR)
- Appeal to the Tribunal

A key point is that you can only ask for an Independent Review, or appeal to the Tribunal, if HMRC has actually made a decision. Where there is a disagreement and no formal decision has been made, you may be able to take the case to ADR.

Tax disputes are covered by HMRC's Litigation and Settlement Strategy **https://www.gov.uk/government/publications/litigation-and-settlement-strategy-lss**. It is worth reading this before escalating matters by making an appeal. HMRC's Litigation and Settlement Strategy makes it clear that:

- In general, HMRC will not take up a tax dispute unless the overall revenue flows potentially involved justify doing so;
- HMRC will seek to handle disputes non-confrontationally and by working collaboratively with the customer wherever possible;
- Where HMRC believes that it is likely to succeed in litigation, and that litigation would be both effective and efficient, it will not reach an out of court settlement for less than 100% of the tax, interest and penalties at stake.

2.1 Independent HMRC review

An "independent review" is a new look at your case by an HMRC official unconnected with the initial HMRC decision. It is not 'third party' independent, but nevertheless offers advantages over going straight on to Tribunal.

Some decisions cannot be reviewed, for example decisions about whether to allow a late review or a late appeal. (See HMRC Appeals reviews and tribunals guidance manual - **https://www.gov.uk/hmrc-internal-manuals/appeals-reviews-and-tribunals-guidance/artg4050**).

In recent years, HMRC's decisions have been varied or cancelled by independent review in just under half of cases relating to penalties, and in around a third of non-penalty cases.

It is a low cost option, and worthy of careful consideration and preparation. If your arguments are strong, why would HMRC want to take the case to the Tribunal? Independent review can be particularly useful if new facts have come to light. It is also an opportunity for the taxpayer and agent to reconsider the strength of their arguments and refine their case.

For indirect taxes, HMRC will usually offer a review following its initial decision. With direct taxes, it is normally up to the taxpayer, or their agent, to ask for a review.

There is normally 30 days in which to ask for review, or to accept HMRC's offer of a review. Don't ignore HMRC's offer of a review as, in default, the case is deemed to be agreed. Either ask for a review, or make an appeal to Tribunal.

It will usually make sense to ask for and/or accept the offer of an Independent Review. Use it as an opportunity to take a fresh look at the case, discuss the details with the client, and ensure that all possible new evidence and arguments are considered and submitted.

There is 30 days from the HMRC reviewer's decision to appeal to the Tribunal.

2.2 Alternative Dispute Resolution (ADR)

ADR can be used both where there is a disputed decision or simply where negotiations have broken down. If your dispute is over an HMRC decision which can be taken to the Tribunal, make sure you lodge your Tribunal appeal within the time limit (usually 30 days from the date of the decision). Unlike an HMRC Review, asking for ADR does not stop the clock.

If a case listed for Tribunal is accepted for ADR, the Tribunal proceedings will normally be stayed until ADR is completed.

ADR is not suitable for all types of dispute. In particular, it does not cover 'reasonable excuse' for fixed penalties, PAYE coding issues, criminal cases, or issues such as delays in HMRC using information, which might form grounds for a complaint.

Using ADR can be less expensive and faster than going to Tribunal. The arrangements are also less formal and more open to compromise. Outcomes are not published, so confidentiality is maintained. However, it is not necessarily a cheaper option; part of its merits is in reaching a compromise positon which is much less likely to happen in a tribunal case.

ADR will test the strength of your arguments, and is valuable where a 'common sense' outcome is sought, and facts or attitudes are disputed. It should make sure that both sides of the dispute can be understood by the other party. It is surprising how often misunderstandings prolong a dispute. ADR can therefore assist early settlement.

ADR can also enable the limits of the dispute to be more carefully defined, so that only core issues remain outstanding and can then be litigated.

Application for ADR is online for SME businesses - **https://www.gov.uk/guidance/tax-disputes-alternative-dispute-resolution-adr** and can be arranged via a Customer Relationship Manager for large businesses.

2.3 Appeals to First-Tier Tribunal Tax (FTT)

Appealing to the FTT brings practitioners into a completely different world. Proceedings are more formal. It is strongly recommended that anyone thinking of appealing to the FTT attends a public hearing to gain an understanding of procedures, or discusses the position with someone who is familiar with taking cases to FTT. It involves a separate set of skills - advocacy- from those normally exercised by tax practitioners and accountants.

Many cases under appeal are decided by agreement before they reach the FTT. In recent years, over three quarters of cases reaching FTT were decided in HMRC's favour.

FTT is a much more formal and legal set up than other dispute resolutions methods. It is decided on strict legal criteria. Decisions are often all or nothing, with a negative result often exacerbated by poor preparation.

If the taxpayer's case is good, it is best to present the strongest case to HMRC before reaching the Tribunal. HMRC policy is not to take hopeless cases to FTT, so weak HMRC cases should be the exception.

Appealing to the FTT can set the taxpayer on an upward spiral of costs, even when the case is reasonable. HMRC may appeal to the Upper Tribunal if it is unhappy with the FTT decision, and the taxpayer may then feel obliged to take on these additional costs or risk losing the case.

The position on fees for an appeal to the FTT is currently under review. The original proposed structure was:

- Default paper cases £50 (essentially penalty cases where the amount due is no more than £2000)
- Basic cases – an issue fee of £50 and a hearing fee of £200 (mainly penalty cases and requests to allow late appeals)
- Standard cases – an issue fee of £200 and a hearing fee of £500
- Complex cases – an issue fee of £200 and a hearing fee of £1,000

Once the new online appeals system is fully operational, we are likely to have some clarification.

More information on appeal procedures:

https://www.gov.uk/guidance/appeals-and-tribunals-an-overview-for-agents-and-advisers.

Appeals reviews and tribunals guidance

https://www.gov.uk/hmrc-internal-manuals/appeals-reviews-and-tribunals-guidance.

2.4 Scottish devolved taxes

For Scottish Tax appeals, there is a review, option to mediate, and escalation prior to going to the Tribunal: **https://www.revenue.scot/compliance-dispute-resolution/dispute-resolution-process**.

This covers Land and Buildings Transactions Tax and Scottish Landfill tax (and, in due course, Air Departure Tax and Aggregates Levy).

From 24 April 2017, appeals in Scotland regarding these devolved taxes are dealt with by the newly formed Scottish Tribunal Service. The system here is changing– the Scottish Taxes will be dealt with by the Tax Chamber of the Scottish Tribunals - **http://www.taxtribunals.scot/**. The process and procedures are broadly similar to the UK tribunals (but not identical).

3. Matters of judgement and uncertainty over facts

Disputes over facts and matters of judgement are likely to be best dealt with by HMRC Independent Review and ADR. Only in exceptional cases are such matters likely to be suitable for FTT.

HMRC CHANGE PROCESS FOR AGENTS OBTAINING CLIENT INFORMATION

Ruth Owen, Director General of Customer Services at HM Revenue & Customs (HMRC), recently sent the following message for agents about obtaining details on behalf of their clients.

"We have recently seen a large increase in requests from agents for their clients' pay, tax and employment history information, often in bulk, mainly to claim employment expenses, and involving a growing number of security issues. These include agents pretending to be their clients, and calling on behalf of clients who have not given the necessary permission.

As a result, we are making changes to the way we supply this confidential data. While we can continue to take requests for this information on our helplines, we can no longer provide the detailed personal information directly to agents over the phone. From now on, we will send the requested information directly to your clients, who will then be able to forward it to you for the relevant claim to be made or tax return completed.

*I appreciate that this security measure will add some time to the process, and I am sorry about that. As a quicker alternative, please note that your clients can access this information through the online service in their Personal Tax Account. They can now view, print and download their pay and tax details in just a few minutes at **gov.uk/personal-tax-account** – they'll need their National Insurance number and a recent payslip, P60 or passport to sign-in for the first time.*

As you may know, we are working on a digital facility that will enable agents to access their clients' details securely online, which I expect to go live later in the year. In the meantime, I hope you can understand the reasons for the urgent changes to our phone service in respect of this matter."

In our view, this is a backward step in customer service from HMRC which not only inconveniences tax payers but also further hinders the work of agents. ICAS has voiced our objections to this change and is actively lobbying to have it reversed.

TAX ADVISERS – TIME IS RUNNING OUT TO SEND NOTIFICATION LETTERS TO CLIENTS

If you fall within the obligation to notify clients but don't do it by 31 August 2017 you could face a one-off penalty of £3,000. This article identifies key aspects of the obligation. For full details and to check your position, visit the HM Revenue & Customs (HMRC) client notification landing page (**https://www.gov.uk/government/publications/client-notification-income-or-assets-abroad**) which includes links to HMRCs' detailed guidance.

The obligation to notify

Amendments to the International Tax Compliance Regulations have placed an obligation on financial institutions and relevant persons (including tax advisers) to inform their clients:

- That HMRC will soon be getting data on overseas financial accounts;
- That there are opportunities to come forward to make disclosures about overseas affairs;
- Of the possible consequences for those who don't come forward.

Under the Common Reporting Standard, tax authorities around the world will be sharing data on financial accounts and will be using that data to check that taxable income has been properly reported. HMRC believes financial institutions and advisers know more than HMRC about whether clients have, or are likely to have, assets and income overseas.

Who needs to send notification letters to clients?

Specified financial institutions, such as banks, building societies, insurers and fund managers (not covered further in this article) and 'specified relevant persons' (SRPs). SRPs include:

- Tax agents and advisers;
- Solicitors;
- Financial advisers.

There is a limited exclusion for SRPs in certain circumstances where services are provided solely in preparation of a tax return and various conditions are met.

Clients who must be notified

The notification letter only needs to be sent to clients who are UK tax residents in either the:

- 2015 to 2016 tax year; or
- 2016 to 2017 tax year.

SRPs can choose how to identify the clients they need to notify. They can opt for:

1. The specific approach – identify individual clients they have provided with offshore advice, or referred overseas for this (ie the advice, products or services do not have to have been provided directly to the client); or
2. The general approach – identify all clients they have provided with advice or services for their personal tax affairs (between 1 October 2015 and 30 September 2016).

SRPs only need to use one of these approaches and if they don't find any clients to notify they do not need to do anything else.

How to send notification letters

SRPs must send the notification letter together with a covering letter (or email). These must be sent to clients by:

- Post; or
- Email – if this is the way the adviser usually communicates with clients and reasonably believes they will read it.

For SRPs the wording for the covering letter (or which must be included in the covering email) reads:

"From 2016, HM Revenue & Customs (HMRC) is getting an unprecedented amount of information about people's overseas accounts, structures, trusts, and investments from more than 100 jurisdictions worldwide, thanks to agreements to increase global tax transparency. This gives HMRC unprecedented levels of information to check that, as in most cases, the right tax has been paid.

If you have already declared all of your past and present income or gains to HMRC, including from overseas, you do not need to worry. But if you are in any doubt, HMRC recommends that you read the factsheet attached to help you decide now what to do next."

Content of the notification

The letter highlights that HMRC will be getting new financial information from over 100 jurisdictions about its 'customers', including details of overseas accounts, structures, trusts and investments.

Some individuals may not have realised that they needed to disclose offshore income – perhaps because they inherited assets overseas, or because their circumstances or tax legislation have changed since they took advice. The letter tries to address them, as well as those who have deliberately concealed offshore income, by placing emphasis on checking that tax affairs are up to date and mentioning inherited assets and changes in personal circumstances.

The letter directs taxpayers who need to bring their affairs up to date to HMRC's online disclosure facility, and suggests anyone who is unsure should talk to a tax adviser. It also outlines the possible consequences of failing to pay the correct tax on offshore assets.

Timing

The notification letters must be sent to any qualifying clients by 31 August 2017.

Penalties

Advisers who do not identify relevant clients and send them the letter could be charged a one-off penalty of £3,000.

Useful links

Websites relevant to the client notification obligation:

- Client notification landing page - **https://www.gov.uk/government/publications/client-notification-income-or-assets-abroad**
- Guidance for recipients of the client notification - **https://www.gov.uk/guidance/income-or-assets-abroad-letter-about-your-uk-tax-affairs**
- Guide to sending the client notification letter - **https://www.gov.uk/government/publications/client-notification-income-or-assets-abroad/notes-on-how-and-when-to-send-the-client-notification-letter**
- Full guidance on client notification in the HMRC manual - **https://www.gov.uk/hmrc-internal-manuals/international-exchange-of-information/ieim600000**
- The regulations - **http://www.legislation.gov.uk/uksi/2016/899/contents/made**
- Worldwide Disclosure Facility landing page - **https://www.gov.uk/guidance/worldwide-disclosure-facility-make-a-disclosure**

EMPLOYMENT CORNER - GENDER PAY GAP REPORTING (GPGR) UPDATE FOR PUBLIC SECTOR EMPLOYERS

The Government recently confirmed that Public Sector employers, including universities, will be required to report on their gender pay gaps from 31 March 2017 and not 5 April 2017. The draft regulations stipulated 5 April.

This will change the sample for GPGR when compared to private sector businesses. It is not clear why this has changed, although the definitions of what pay, bonus pay and employees have now been finalised.

Public Sector bodies should be aware that the reporting requirements under GPGR is focusing on a different set of criteria to the existing reporting regime, as it requires the body to assess the whole workforce as one rather than grade by grade. It is expected that this will produce a greater variance in gender pay and highlight gender imbalances in certain grades.

It is recommended that some form of wording is produced, not only to explain the pay gaps, but also to outline what is being done to address gaps over a set period. Advisers should be aware that reporting requirements will apply to public bodies in England, some cross-border authorities. and all non-devolved authorities operating across Great Britain with 250 employees or more from 31 March 2017. Scotland and Wales are introducing corresponding regulations, with their own gender pay reporting requirements (**http://www.equalpayportal.co.uk/scotland/**). Reporting on GPGR is an extension of the public sector equality duty, rather than as a standalone requirement as is the case with private sector employers.

REDUNDANCY PROTECTION FOR NEW AND EXPECTANT MOTHERS

The UK Government is reviewing legislation covering redundancy discrimination protections for new and expectant mothers, in a response to calls for changes to the law by the Women & Equalities Select Committee, who claim there has been an exponential rise in discrimination claims being brought by new and expectant mothers.

At present, women who have been on maternity for 26 weeks or less are at lower risk of redundancy than other workers. However, the Committee believes that it is vital UK law is changed to mirror laws introduced in Germany, which allow only for redundancy in very specific circumstances.

The Taylor Review into modern working practices (**http://www.personneltoday.com/hr/taylor-review-modern-employment-practices-launched**), which began in October 2016, is reviewing, amongst other things, the issues surrounding agency and zero-hours contracts, as well as permissions to attend ante-natal and other pregnancy and maternity leave related appointments.

DECISION IN 'HUGHES' CASE LEADS TO PENSION TRANSFER CASES BEING DROPPED

The Pensions Ombudsman has confirmed that some cases taken against pension providers who refused to transfer pension accruals into schemes with suspected connections to pension 'liberation' have been dropped following the "Hughes" decision (**Hughes v The Royal London Mutual Insurance Society Limited [2016] EWHC 319 (Ch)**). The High Court concluded that a person does not need to prove a 'genuine employment link' before a transfer to another pension scheme could proceed.

However, the Government is looking at legislation to protect pension savers from scams as a result of this decision, because currently the existing legislation does not offer much authority to pension schemes to refuse to transfer a saver's funds into another scheme. Pension providers often used to ask for evidence of an "earnings relationship" between the saver and the new provider, but the Hughes case put paid to this. The Government is concerned that pension scheme members could be scammed, especially where the new provider is not regulated by the Financial Conduct Authority.

Current legislation gives pension schemes limited scope to refuse a statutory transfer request to a scheme which looks like a scam. Before the High Court's decision in the Hughes case, it was common for providers to request proof of an earnings relationship between the scheme member and the potential receiving scheme, giving them legitimate grounds on which to justify a refusal to transfer into a scheme they suspected was a scam where this could not be provided.

The consultation (**https://www.gov.uk/government/consultations/pension-scams/pensions-scams-consultation**), which closed on 13 February 2017 also recommends a complete prohibition on pensions transfer cold calling and revised registration requirements for small self-administered schemes and single-member occupational pension schemes due to the massive rise in cold calling in this area.

GOVERNMENT TO IMPLEMENT PENSIONS ADVICE ALLOWANCE

From April 2017, the Government is to introduce an allowance (**https://www.gov.uk/government/consultations/introducing-a-pensions-advice-allowance**) designed to permit individuals to withdraw a tax free amount of up to £500 from their pension pots. The amount can be withdrawn on no more than three occasions during their lifetime, but only once in any given tax year, and must be used to pay for retirement advice in relation to their pension pots, specifically defined contribution and hybrid pensions with a money purchase or cash balance element savings plans. This allowance is independent of the exemption for employer-arranged pension advice (**https://www.gov.uk/government/publications/employer-arranged-pensions-advice-exemption**), and will be available to any saver of any age regardless of income. It must be paid straight to the regulated financial adviser by the pension scheme administrator.

VAT: THE OPTION TO TAX – A REMINDER OF THE BASIC PRINCIPLES AND SOME PRACTICAL GUIDANCE

The default VAT treatment of supplies of land and buildings is exempt. However, as is often the case, there are many exceptions.

If a piece of land or commercial property that is not intended for residential or non-business use does not fall within an exception, it can be opted to tax. The effect of this is that any supply of that property is now taxed at the standard rate of VAT rather than being exempt from VAT.

The effects of this are fairly obvious. VAT must be charged on all sales or lettings of the property by the opter. This election is essentially irrevocable for 20 years apart from a six month cooling off period which can only be relied on if no supply has been made of the property since the election was made. In addition, assuming no other exempt use is made of the property, input tax incurred with respect to it can be fully reclaimed. This is usually the main reason why options to tax are made.

With respect to the scope of this election, the option to tax will apply to the entire property. If land is opted and that land is later built on, the opter has also automatically opted to tax the new building. A building is deemed to include all parts that are internally linked. Thus, someone opting to tax a unit in an internally linked retail complex will have opted to tax the entire building.

In terms of administration, the making of an option to tax is a two stage process. The decision is taken by the owner to make the election. This is an internal process and should be documented. The second stage is notifying HM Revenue & Customs (HMRC) and this should be done within 30 days of the date on which the property is opted. HMRC will acknowledge the election and this acknowledgement should be retained as evidence. The position is more complicated if the opter has already made exempt supplies of the property as then, permission will be needed from HMRC in order to make the election. In most cases, this permission is given automatically but advice should be sought in these circumstances in case that permission is not granted.

It is very often the process of making the option to tax that causes problems in practice.

A regular problem that arises when a property is being sold, or a business is being sold as a going concern (in VAT speak, a TOGC – a transfer of a business as a going concern) which includes a property, is the question as to whether the property has in fact been opted to tax. The buyer will want to see evidence that HMRC have accepted the seller's option to tax. Given that options to tax can exist for at least 20 years, it is very often the case that the seller is unable to demonstrate that the option to tax was actually made.

If there is plenty of time available before the sale is concluded, it may be possible to ask HMRC's Option to Tax Unit to confirm that the option to tax has been validly made and notified. However, it is rare in practice to be able to obtain this information from HMRC and even more rare to obtain it quickly.

In the event that no evidence of an option to tax notification can be found, and assuming that the seller believes that the option to tax was made in the past, it may be necessary to make a late notification of the option to tax to HMRC. This is acceptable to HMRC as long as evidence can be provided that the option to tax was in fact made on the date claimed. It would therefore be necessary to provide perhaps a board minute or meeting note which would demonstrate that the decision was taken to make the election on a particular date. In practice, such evidence may not exist, as this decision may well have been made but not documented. In such a case, HMRC will usually accept a statement from a responsible person within the business stating that the option was made and the date on which it was made; that output tax has always been charged on all supplies made of the property since the date of the option to tax; and that relevant input tax has been appropriately treated.

Thus, where the property has been regularly let prior to sale and VAT has always been charged on any rents, then clearly the seller's behaviour very much suggests that the option to tax has been made.

HMRC does, in practice, take a reasonable line with respect to such late notifications of options to tax. However, what will never be accepted is a retrospective option to tax, such that the trader requests that an option to tax should now be made on a past date (usually because it had been forgotten about at the time). The election had to actually have been made on the date claimed.

As mentioned above, problems arise with option to tax notifications when a property is being sold, or a business which includes a piece of land or building is sold as a TOGC. In the former case, the buyer will want to know if VAT will be charged on the transaction and will want evidence that the charge is proper. Assuming the sale is taxable as a result of an option to tax, this evidence would be HMRC's acknowledgement of the option to tax.

In the latter case (a TOGC including property), the impact of the option to tax is more complicated. Assuming all of the necessary conditions for a TOGC have been met (thus allowing the sale to be outside the scope of VAT) and the seller has opted to tax the relevant property, the part of the consideration that reflects the value of the property is only deemed to be outside the scope of VAT if the purchaser has also opted to tax on or before the date of the sale. Thus the seller must provide evidence of his own option to tax well in advance of the sale in order to allow the purchaser to do the same (and obtain HMRC's acknowledgement of that option to tax). In addition, as part of the conditions for the property to be treated as outwith the scope of VAT, the purchaser must provide written confirmation that the option to tax will not disapply soon after the sale. (A disapplication occurs in a number of situations but most commonly, when the purchaser intends to use the property for residential purposes).

It is very common for the existence or otherwise of an option to tax to become a major complication in a property or business transaction. Very early questions should be raised about options to tax in order to avoid problems in finalising the deal.

UPDATED GUIDANCE ON DISTRIBUTABLE PROFITS

Updated guidance (Tech 02/17 BL) on realised and distributable profits under the Companies Act 2006 (as amended) (the Act) has been issued by ICAS and the Institute of Chartered Accountants in England and Wales (ICAEW). The purpose of the guidance is to identify, interpret and apply the principles relating to the determination of realised profits and losses for the purposes of making distributions under the Act.

The guidance is based on that previously issued as TECH 02/10 in October 2010 but has been updated as proposed in TECH 05/16, which was issued for comment in March 2016. For the convenience of users, paragraph numbering has been kept consistent with TECH 02/10 so far as possible and consequently some paragraph numbers are not used where material has been deleted or moved. Most of the comments received in response to TECH 05/16 focussed on the definition of a distribution and the consequences of accounting for off-market intragroup loans in accordance with Financial Reporting Standard (FRS) 102. In the former case, additional footnotes have been added to make it clearer that the guidance reflects case law. In the latter case, the material has been extensively redrafted to address comments received but without changing the overall conclusions reached. Some of the responses raised additional comments where the guidance could be expanded or made clearer. The opportunity has been taken to address some of these comments through improved drafting but they raise no new issues of substance.

This Technical Release also addresses the consequences of the change in the law concerning distributable profits in relation to long-term insurance business made by The Companies Act 2006

(Distributions of Insurance Companies) Regulations 2016 (SI 2016/1194) which were made on 7 December 2016.

ICAS and the ICAEW are aware of the calls by some investors for greater transparency about dividend policy and capacity, including distributable reserves. The Financial Reporting Council's (FRC) Financial Reporting Lab issued a report 'Disclosure of dividends – policy and practice' in November 2015 exploring how companies can make dividend disclosures more relevant for investors. An update to this was issued in December 2016. Paragraph 2.25 of TECH 02/17 BL states that there is no requirement under law or accounting standards for financial statements to distinguish between realised profits and unrealised profits, or between distributable profits and non-distributable profits. The Institutes consider, based on legal advice, that this is a correct statement of the law. Listed companies may, however, wish to consider how to address the calls for greater transparency from the investor community.

This guidance should be referred to in the determination of realised profits and losses under the Companies 2006. It represents generally accepted practice at 31 December 2016 in relation to the meaning of realised profits. Whilst many of the revisions to TECH 02/10 made by this Technical Release represent principles that were generally accepted prior to that date, the revisions introduced now should not be used to question the lawfulness of distributions made at an earlier date. However, balances on reserves will need to be re-examined in the light of the Technical Release, and the position should be re-assessed before a distribution is made. It should also be noted that the additional guidance about the definition of a distribution in paragraphs 2.6A to 2.6D is based on legal advice and is not a question of generally accepted practice. Therefore, it is possible that some transactions previously entered into were distributions at the time they were entered into, and would have been unlawful distributions in the absence of adequate distributable reserves. For example, this may apply to some intragroup loans on off market terms.

The Act permits companies to prepare their individual accounts using UK Generally Accepted Accounting Practice (GAAP) or EU-adopted International Financial Reporting Standards (IFRS). This guidance applies to companies reporting under both UK GAAP and EU-adopted IFRSs except where otherwise stated. The guidance has been written on the basis of 'full' IFRSs as issued by the International Accounting Standrads Board (the IASB) but should be equally applicable to EU-adopted IFRSs.

Reference to an IFRS or International Accounting Standard (IAS) should be read as applying to the equivalent requirements of UK GAAP unless the context requires otherwise. The guidance uses the terminology 'in profit or loss' which has the same meaning as 'in the profit and loss account'. References to the 'Accounting Regulations' are to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) and to the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (SI 2008/409) as appropriate. Where relevant, these take into account the amendments made up to 31 December 2016.

IFRSs and FRS 102 use terminology that is different from that in the Act, for example referring to a statement of financial position instead of a balance sheet. IFRSs also include a requirement for a statement of profit or loss and other comprehensive income. FRS 102 refers to this statement as a statement of comprehensive income. Under IFRSs and FRS 102, this statement may be presented either as a single statement or as two statements. The second statement starts with profit or loss and then shows the items of other comprehensive income. For simplicity, company law terminology has generally been used in this guidance.

FRS 101 Reduced Disclosure Framework generally requires recognition and measurement on a basis that is consistent with IFRSs as adopted by the EU. It does not, therefore, raise any new issues about realised and distributable profits and is not generally referred to separately in TECH 02/17 BL.

Certain companies are permitted to prepare their accounts in accordance with the micro-entities regime in company law and in accordance with FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime. Accounts prepared in accordance with the micro-entities regime are 'presumed' to give a true and fair view if prepared in accordance with the applicable legal requirements (s393(2A)). Such accounts will be a company's 'relevant accounts' for the purposes of determining realised profits when it chooses to apply the micro-

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entities regime. The micro-entities regime does not raise any significant new issues in relation to distributable profits and is not generally referred to separately in TECH 02/17 BL. FRS 105 prohibits provisions for deferred tax, and therefore a micro-entity's realised profits will not take into account any deferred tax which might have been provided under IFRSs or FRS 102. However, the directors of a micro-entity should have regard to the need to retain sufficient cash to pay the company's tax liabilities as they fall due in accordance with the guidance in paragraph 2.3A the technical release.

Companies should consider taking their own legal advice, particularly in relation to any matters not covered by this guidance.

English and Scottish Counsel have confirmed that the guidance is consistent with the law at 31 December 2016. Counsel accept no responsibility (other than to the Institutes) in relation to advice ascribed to them in this guidance.

TECH 02/17 BL is avaialble to download at: **https://www.icas.com/__data/assets/pdf_file/0004/289075/TECH-02-17BL-Guidance-on-Distributable-Profits.pdf**.

FRC PROPOSES REVISIONS TO FRS 102

The Financial Reporting Council (FRC) first published Financial Reporting Standard (FRS) 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' in March 2013. At that time, the Financial Reporting Council (FRC) indicated that the standard would be reviewed every three years. The FRC is currently nearing completion of its first triennial review and has recently published Financial Reporting Exposure Draft (FRED) 67 which proposes incremental improvements and clarifications to the standard. This FRED also includes proposed consequential amendments to the other UK and Ireland accounting standards. The deadline for comments is 30 June 2017.

The FRC's proposals have been developed in response to stakeholder feedback and therefore address some of the implementation issues reported to the FRC. ICAS fed in comments to the FRC that had been received from members via various channels on practical issues being experienced whilst applying FRS 102. These included the comments received at two interactive surgeries. It is welcomed that some of the key problem areas highlighted by CAs are being addressed by the FRC.

1. FRED 67 – Key Proposed Changes to FRS 102

FRED 67 includes many proposed amendments, although the majority are editorial and/or intended to merely clarify, rather than change, the accounting treatment. The principal amendments to have an impact on the financial statements are:

(a) The removal of the ability to adopt the cost model based on circumstances relating to "*undue cost or effort*". Additionally, an accounting policy choice is proposed for entities that rent investment property to another group entity, whereby the entity concerned can choose to measure the investment property either at cost (less depreciation and impairment) or at fair value.

(b) The introduction of a description of a basic financial instrument to support the detailed conditions for classification as basic. Making this change should result in a relatively small number of financial instruments that breach the detailed conditions for classification as a basic financial instrument.

(c) For small entities, a more proportionate accounting solution for a loan from a director who is a natural person and a shareholder in the small entity (or a close member of the family of that person), which will permit the loan to be initially measured at transaction price rather than present value ie for small entities there will no longer be a need to estimate a market rate of interest when measuring loans from a director who is also a shareholder.

(d) Entities will be required to recognise fewer intangible assets acquired in a business combination separately from goodwill. This will reduce the costs of compliance. Entities may, on an asset-by-asset basis, choose to separately recognise additional intangible assets acquired in a business combination if this provides useful information to the entity and the users of its financial statements. When an entity chooses to recognise such intangible assets separately from goodwill, it will be required to apply that policy consistently to the relevant class of intangible assets.

(e) The principle included in the financial institution definition has been amended to remove references to 'generate wealth' and 'manage risk'. This change is intended to reduce the interpretational difficulties in relation to implementing these concepts, and should reduce the number of entities meeting the definition of a financial institution.

(vi) The proposed effective date for these amendments is accounting periods beginning on or after 1 January 2019, and it is envisaged that early application will be permitted provided all amendments are applied at the same time. Limited transitional provisions are also proposed. It should be noted that these proposals are not yet part of FRS 102 and can only be applied when/if they are included in the forthcoming revised version of the standard. The FRC expects to finalise the amendments to FRS 102 in December 2017.

Points (a) to (e) above, are now addressed in more detail.

(a) Investment Properties

(i) Removal of "Undue Cost or Effort" Rationale for applying cost model

The FRC is proposing that the ability for some entities to claim that fair values could not be obtained for an investment property without undue cost or effort will be removed. Therefore, the general requirement would be that the ongoing measurement of investment properties should be at fair value. This is line with the ICAS policy position that it was difficult to argue "*undue cost or effort*" given that old UK GAAP, Statement of Accounting Practice 19 'Accounting for Investment Properties' and the Financial Reporting Standard for Smaller Entities (FRSSE) had long required this, and businesses and stakeholders were accustomed to this accounting treatment. This clarification therefore removes the ability to circumnavigate the intended spirit of the standard. As per the extant version of the standard, the proposed revised standard does not require that an annual valuation is performed by an independent professional. However, the financial statements do (also currently a requirement, so no change) need to disclose the following in terms of the valuation:

(a) the methods and significant assumptions applied in determining the fair value of investment property;

(b) the extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification, and has recent experience in the location and class of the investment property being valued. If there has been no such valuation, that fact shall be disclosed.

(ii) Properties let to Group Companies

The proposals also improve, from an ICAS perspective, the treatment of situations where a group company rents an investment property to another member of the group. Currently the company that holds the asset has to show the asset as an investment property at its fair value in its individual accounts whereas in the group accounts this would need to be restated to cost. However, the proposed amendment will allow such companies the choice of showing such assets in their individual financial statements either at fair value with changes in fair value recognised in profit or loss; or to transfer them to property, plant and equipment and apply the cost model in accordance with Section 17 of FRS 102 Property, Plant and Equipment. We would anticipate that many groups would adopt the latter approach.

(b) Basic Financial Instrument

A new principle-based description has been introduced for the classification of financial instruments which will allow more of them to be measured based on cost, rather than fair value.

FRS 102 introduced requirements which split financial instruments into two categories:

- Basic financial instruments (such as straightforward loans) which are measured at amortised cost; and
- Other financial instruments (such as derivatives, including interest rate swaps and foreign currency forward contracts and non-basic loans) which are measured at fair value.

Feedback from stakeholders highlighted that this rule-based classification causes significant problems for those applying FRS 102. To address this, FRED 67 proposes that a debt instrument can be categorized as "basic" if it is consistent with a principle-based description of a "basic" financial instrument. This means that a debt can be categorized as "basic" if it gives rise to cash flows on specified dates which constitute reasonable compensation for the time value of money, credit risk and other basic lending risks and costs. The proposed changes to FRS 102 are set out below. These track the proposed changes from the extant text of FRS 102. In effect. The main changes are the insertion of a new subsection (bA) at paragraph 11.8 of FRS 102 and a new paragraph 11.9A.

"*11.8 An entity shall account for the following financial instruments as basic financial instruments in accordance with ~~Section 11~~this section:*

(a) cash;

(b) a debt instrument (such as an account, note, or loan receivable or payable) that meets the conditions in paragraph 11.9 and is not a derivative financial instrument ~~described in paragraph 11.6(b)~~;

(bA) a debt instrument that, whilst not meeting the conditions in paragraph 11.9, nevertheless is consistent with the description in paragraph 11.9A, and is not a derivative financial instrument;

(c) commitments to receive or make a loan to another entity that:

(i) cannot be settled net in cash; and

(ii) when the commitment is executed,

are expected to meet the conditions in paragraph 11.9 or be consistent with the description in paragraph 11.9A; and

(d) an investment in a non-derivative instrument that is equity of the issuer (eg most ordinary shares and certain preference shares) ~~non-convertible preference shares and non-puttable ordinary shares or preference shares~~."

"11.9 A debt instrument that satisfies the following conditions shall be considered a basic financial instrument~~The conditions a debt instrument shall satisfy in accordance with paragraph 11.8(b) are~~:

(a) The contractual return to the holder (the lender), assessed in the currency in which the debt instrument is denominated, is:

(i) a fixed amount;

(ii) a positive fixed rate or a positive variable rate[11]; or

[11]A variable rate for this purpose is a rate which varies over time and is linked to a single observable interest rate or to a single relevant observable index of general price inflation of the currency in which the instrument is denominated, provided such links are not leveraged.

(iii) [not used]

(iv) a combination of a positive or a negative fixed rate and a positive variable rate (eg LIBOR plus 200 basis points or LIBOR less 50 basis points, but not 500 basis points less LIBOR).

(aA) The contract may provide for repayments of the principal or the return to the holder (but not both) to be linked to a single relevant observable index of general price inflation of the currency in which the debt instrument is denominated, provided such links are not leveraged.

(aB) The contract may provide for a determinable variation of the return to the holder during the life of the instrument, provided that:

(i) the new rate satisfies condition (a) and the variation is not contingent on future events other than:

(1) a change of a contractual variable rate;

(2) to protect the holder against credit deterioration of the issuer;

(3) changes in levies applied by a central bank or arising from changes in relevant taxation or law; or

(ii) the new rate is a market rate of interest and satisfies condition (a).

Contractual terms that give the lender the unilateral option to change the terms of the contract are not determinable for this purpose.

(b) There is no contractual provision that could, by its terms, result in the holder losing the principal amount or any interest attributable to the current period or prior periods. The fact that a debt instrument is subordinated to other debt instruments is not an example of such a contractual provision.

(c) There are no c~~C~~ontractual provisions contingent on future events that permit or require the issuer (the borrower) to prepay a debt instrument or permit or require the holder (the lender) to put it back to the issuer before maturity ~~are not contingent on future events~~ other than to protect:

(i) the holder against the credit deterioration of the issuer (eg defaults, credit downgrades or loan covenant violations), or a change in control of the issuer; or

(ii) the holder or issuer against changes in levies applied by a central bank or arising from changes in relevant taxation or law.

The inclusion of contractual terms that, as a result of the early termination, require the issuer to compensate the holder for the early termination do~~es~~ not, in themselves~~itself~~, constitute a breach of ~~this~~ the conditions of paragraph 11.9.

(d) [Not used]

(e) Contractual provisions may permit the extension of the term of the debt instrument, provided that the return to the holder and any other contractual provisions applicable during the extended term satisfy the conditions of paragraphs (a) to (c)."

"11.9A A debt instrument not meeting the conditions in paragraph 11.9 shall, nevertheless, be considered a basic financial instrument if it gives rise to cash flows on specified dates that constitute repayment of the principal advanced, together with reasonable compensation for the time value of money, credit risk and other basic lending risks and costs (eg liquidity risk, administrative costs associated with holding the instrument and lender's profit margin). Contractual terms that introduce exposure to unrelated risks or volatility (eg changes in equity prices or commodity prices) are inconsistent with this."

(c) Directors' Loans

The FRC is proposing an exemption to the financing transaction requirement contained in paragraph 11.13 of FRS 102. Concerns were raised about the practicalities of this in relation to directors' loans where, because commercial funding is often unavailable, it is difficult to determine an appropriate market rate. This will allow transactions where a director (human being) loans money to a company in which he is also a shareholder to be exempt from the requirement to account for this as a financing transaction, but rather to be included at the transaction price from the outset. This exemption is also available to a close member of the family of that person. The proposed wording is as follows:

"11.13 When a financial asset or financial liability is recognised initially, an entity shall measure it at the transaction price (~~including~~ adjusted for transaction costs, except in the initial measurement of financial assets and liabilities that are subsequently measured at fair value through profit or loss) unless the arrangement constitutes, in effect, a financing transaction. An arrangement constitutes a financing transaction ~~may take place in connection with the sale of goods or services, for example~~, if payment is deferred beyond normal business terms, for example, providing interest-free credit to a buyer for the sale of goods, or is financed at a rate of interest that is not a market rate, for example, an interest-free or below market interest rate loan made to an employee. Except as set out in paragraph 11.13A, i~~I~~f the arrangement constitutes a financing transaction, the entity shall measure the financial asset or financial liability at the present value of the future payments discounted at a market rate of interest for a similar debt instrument as determined at initial recognition adjusted for transactions costs."

"11.13A As an exception to paragraph 11.13, the following financing transactions may be measured initially at transaction price:

(a) a basic financial liability of a small entity that is a loan from a director who is a natural person and a shareholder in the small entity (or a close member of the family of that person); and

(b) a public benefit entity concessionary loan (see paragraph PBE11.1A)."

(d) Intangible Assets

The FRC is proposing greater flexibility in relation to the intangible assets that need to be recognised on an acquisition. This appears a more proportionate approach as it will reduce the need to identify and recognise certain intangible assets. This is a result of feedback on the practical issues arising from applying paragraph 18.8 of FRS 102, in particular, the meaning and purpose of the phrase "immeasurable variables" was highlighted by stakeholders. FRED 67 has introduced conditions which require the recognition of some, but not all assets acquired in a business combination separately from goodwill, and this will result in fewer intangible assets being recognised separately and valued. The conditions requiring separate recognition are:

(A) They meet the recognition criteria; and

(B) They are separable and arise from contractual or other legal rights.

In addition, an entity may choose to recognise other intangible assets acquired in a business combination.

The proposed revised wording of paragraph 18.8 of FRS 102 is as follows:

"Acquisition as part of a business combination

18.8 ~~An i~~Intangible assets acquired in a business combination ~~is normally~~shall be recognised ~~as an asset~~ separately from goodwill when: ~~because its fair value can be measured with sufficient reliability. However, an intangible asset acquired in a business combination is not recognised when it arises from legal or other contractual rights and there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would be dependent on immeasurable variables.~~

(a) the recognition criteria set out in paragraph 18.4 are met;

(b) the intangible asset arises from contractual or other legal rights; and

(c) the intangible asset is separable (ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged either individually or together with a related contract, asset or liability).

An entity may additionally choose to recognise any or all intangible assets separately from goodwill for which only condition (a) above is met. When an entity chooses to recognise such intangible assets separately from goodwill it shall apply that policy consistently to the relevant class of intangible assets."

The FRC considers that this is a proportionate solution to providing useful information to the users of financial statements. The decision to separately recognise assets may be exercised on an asset-by-asset basis and, when exercised, must be applied consistently to the relevant class of intangible assets to ensure comparability between years. The nature of the intangible assets separated from goodwill, and the reasons why, should be disclosed to assist users in drawing comparisons between different entities.

(e) Definition of a Financial Institution

Changes have been made to the definition of a financial institution with the result that fewer entities will be classified as such. FRS 102 required financial institutions to comply with additional disclosure requirements. These additional disclosures focused on risks relating to financial instruments recognised on the balance sheet and the entity's capital management policies, and such entities were not permitted to take advantage of reduced disclosure requirements. FRED 67 has amended the definition by removing references to "generate wealth" and "manage risk" and this should reduce the number of entities meeting the definition of a financial institution.

Impact on Other UK GAAP Standards including FRS 105

The FRC is proposing consequential amendments to the other UK and Ireland accounting standards for consistency with FRS 102. For example, common definitions or phrases will be updated.

Most of the consequential amendments apply to the micro-entities regime (FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime) because it was developed from FRS 102. However, they will not result in significant changes in accounting for micro-entities because the principal changes to FRS 102 relate to areas where FRS 105 is already simplified. However, some of the changes proposed address specific feedback or legal requirements, for example disclosure requirements for micro-entities.

Impact of New International Financial Reporting Standards (IFRS)

These proposals do not incorporate into FRS 102 major changes in IFRS. The FRC will consider whether, and if so how, to incorporate elements of the expected loss model of IFRS 9 Financial Instruments, IFRS 15 Revenue from Contracts with Customers, and IFRS 16 Leases, as a separate phase of the triennial review. Any proposals for changes will only be made after consideration of responses received to the Consultation Document issued in September 2016. Any resulting amendments to FRS 102 will not be effective before 1 January 2022.

FRED 67 can be viewed at: **https://frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/FRED-67-Draft-Amendments-to-FRS-102-Triennial-Re-File.pdf.**

A worked up draft version of the proposed revised FRS 102 can be viewed at: **https://frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/FRED-67-Draft-Amendments-to-FRS-102-Triennial-Re/FRS-102-Draft.aspx.**

NEW GUIDE FOR SMALL AND MICRO-SIZED ENTITIES HELPS WITH FINANCIAL REPORTING REQUIREMENTS

ICAS has published a new guide (**https://www.icas.com/__data/assets/pdf_file/0006/279942/New-FR-standards-A-Hutchinson-29.11.17.pdf**) for members, which aims to help them apply the new financial reporting requirements for small and micro-sized entities.

With the withdrawal of the FRSSE for accounting periods beginning on or after 1 January 2016, all small entities in the UK must start preparing their accounts under one of the new UK accounting standards – FRS 105, FRS 102 or FRS 102 Section 1A.

Company law has also changed recently as result of the implementation of the EU Accounting Directive, affecting areas such as the size thresholds for small companies. The aim of the guide is therefore to summarise the key areas of change that small entities and their advisors need to be aware of.

The guidance covers the following topics:

- The accounting options available to small entities under new UK GAAP.
- The requirements of the micro-entities regime under company law and FRS 105.
- The key accounting changes necessitated by FRS 102 and FRS 102 section 1A.
- The filing requirements for small companies.
- The tax implications of the new accounting standards.

The guide has now been updated to reflect the main changes to FRS 102 proposed by the FRC as part of their triennial review of the standard, which is currently open for comment until 30 June 2017.

The proposed changes are expected to take effect for accounting periods beginning on or after 1 January 2019.

ACCOUNTING AND AUDITING QUERIES

Query: *I am a partner in a medium sized firm of chartered accountants. We are currently working on the audit of a long-standing client which is a group of limited companies for year ended 31 December 2016. During that year, the parent company of the group acquired a new limited company subsidiary. We have recently been appointed as auditor to that subsidiary. We are currently condsidering the impact of this new group company on our audit of the group and, in particular, whether this event by itself will have any impact on our audit report, both at the individual subsidiary and group level.*

We have set out our preliminary views below and would appreciate your comments on these.

Preliminary Views

In accordance with International Standard on Auditing (ISA) 710 (UK), we believe that we will need to include an 'Other Matter' paragraph in the audit report on the subsidiary company's financial statements, indicating that the financial statements of the prior period were audited by a predecessor auditor (including date and type of report issued).

In relation to the consolidated group accounts, which include this subsidiary for the first time, we are unsure as to whether we also need to include an 'Other Matter' paragraph in this audit report similar to the one mentioned above. The consolidated accounts do not include any comparative information in relation to this subsidiary, so we were unsure if this would be appropriate in the group audit report.

It would be greatly appreciated if you could provide any guidance on this issue.

Answer: As you note, ISA 710 (UK) contains the requirements concerning "Comparative Information – corresponding figures and comparative financial statements" and paragraph 13 of the 2009 standard (available at **https://frc.org.uk/Our-Work/Publications/APB/ISA-710-Comparative-information-corresponding-figu.pdf**) states the following:

"*Prior Period Financial Statements Audited by a Predecessor Auditor*

13. If the financial statements of the prior period were audited by a predecessor auditor and the auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures and decides to do so, the auditor shall state in an Other Matter paragraph in the auditor's report:

(a) That the financial statements of the prior period were audited by the predecessor auditor;

(b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and

(c) The date of that report. (Ref: Para. A7 – A7-2)"

However, Section A7 of the "Application and Other Explanatory Material" within ISA 710 (2009) (pages 7 and 8), to which paragraph 13 (c) refers, and specifically the grey shaded areas within this section which provide the UK specific guidance relating to paragraph 13 (see further explanation of grey shaded areas below) says:

"***Prior Period Financial Statements Audited by a Predecessor Auditor (Ref: Para. 13)***

A7. An illustrative example of the auditor's report if the prior period financial statements were audited by a predecessor auditor and the auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures is contained in Illustration 3 of the Appendix.

A7-1. In the UK and Ireland the incoming auditor does not refer to the predecessor auditor's report on the corresponding figures in the incoming auditor's report for the current period. The incoming auditor assumes audit responsibility for the corresponding figures only in the context of the financial statements as a whole. The incoming auditor reads the preceding period's financial statements and, using the knowledge gained during the current audit, considers whether they have been properly reflected as corresponding figures in the current period's financial statements.

A7-2. Although the incoming auditor is not required to re-audit the financial statements of the preceding period, if the incoming auditor becomes aware of a possible material misstatement of corresponding figures, the requirement and guidance in paragraphs 12 and A6 apply."

As explained in the following document on the FRC website **https://frc.org.uk/Our-Work/Publications/APB/Summary-of-changes-in-the-new-ISAs-(UK-and-Ireland.pdf**, the FRC augments the international auditing standards with additional requirements to address specific UK and Irish legal and regulatory requirements; and gives additional guidance that is appropriate in the UK and Irish national legislative, cultural and business context. This additional material is differentiated from the original text of the international standards by the use of grey shading.

In accordance with paragraph A7-1 of ISA 710 (UK), your audit reports would therefore **NOT** contain an "Other matter" paragraph in either the subsidiary's financial statements or the group financial statements. However, if you become aware of a possible misstatement of the corresponding figures paragraph A7-2 of ISA 710 would be followed.

I also refer you to ISA 510 (UK) "Initial audit engagements – Opening balances" available via the FRC website at: **https://frc.org.uk/Our-Work/Audit-and-Actuarial-Regulation/Audit-and-assurance/Standards-and-guidance/Standards-and-guidance-for-auditors/Auditing-standards.aspx** which discusses the auditor's responsibilities relating to opening balances in an initial audit engagement.

Please note that this response refers to ISA 710 "Comparative Information – corresponding figures and comparative financial statements" of the 2009 Auditing Standards. The FRC's 2016 Auditing Standards are effective for audits of financial statements for periods commencing on or after 17 June 2016.

Query: *I am a partner in a small audit firm and I am currently working on a set of accounts for a new client which is a small private company with a year-end of 31 December 2016. This is the first occasion that the accounts require to be prepared under Financial Reporting Standard (FRS) 102 Section 1A. Previously the accounts were prepared under the Financial Reporting Standard for Smaller Entities (FRSSE). Under this framework the company's goodwill policy stated that goodwill was not amortized because the directors were of the opinion that the value of goodwill was increasing. The goodwill arose on the incorporation of an unincorporated entity beforehand. I have highlighted that this treatment was not what was permitted by the FRSSE. I* *have discussed this matter with the client who informed me that he had resisted the amortization approach because he believed that rather than decreasing in value the value of the goodwill was increasing. I also now have to consider what the requirements of FRS 102 Section 1A and potentially even FRS 105 'The Financial Reporting Standard applicable to the Micro-entities Regime' will mean for the client's accounting for goodwill. Does the fact that the residual value of the goodwill was apparently greater at the year-end date than that stated in the balance sheet mean that there is no need to amortise? As the client is likely to resist amortization what should the firm be advising the client?*

Answer: Under FRS 102 and FRS 102 Section 1A the recognition requirements are as follows:

"*Goodwill*

19.22 The acquirer shall, at the acquisition date:

(a) recognise goodwill acquired in a business combination as an asset; and

(b) initially measure that goodwill at its cost, being the excess of the cost of the business combination over the acquirer's interest in the net amount of the identifiable assets, liabilities and contingent liabilities recognised and measured in accordance with paragraphs 19.15, 19.15A to 19.15C.

19.23 After initial recognition, the acquirer shall measure goodwill acquired in a business combination at cost less accumulated amortisation and accumulated impairment losses:

(a) An entity shall follow the principles in paragraphs 18.19 to 18.24 for amortisation of goodwill. Goodwill shall be considered to have a finite useful life, and shall be amortised on a systematic basis over its life. If, in exceptional cases, an entity is unable to make a reliable estimate of the useful life of goodwill, the life shall not exceed 10 years.

(b) An entity shall follow Section 27 Impairment of Assets for recognising and measuring the impairment of goodwill."

Therefore, goodwill should be included initially at cost. Thereafter, it should be included at cost less accumulated amortisation/accumulated impairment losses.

Under FRS 102 goodwill has a finite life therefore the cost needs to be amortised over a defined period. In response to the client's objection, the goodwill on acquisition or possibly incorporation is generally viewed as being different to that which then develops over time. This is, of course, easier to argue in an acquisition as the old goodwill (people leave etc) is replaced by new goodwill (the latter, of course, being deemed as inherent and not capable of being capitalised).

In terms of disclosure, Section 1A contains the following:

1AC.6 Where in exceptional cases the useful life of intangible assets cannot be reliably estimated, there must be disclosed in a note to the financial statements the period over which those intangible assets are being written off and the reasons for choosing that period. (Schedule 1, paragraph 22(4)) Intangible assets include goodwill. Paragraphs 18.27(a) and 19.25(g) address similar requirements.

1AC.12 In respect of each item which is shown under the general item 'fixed assets' in the small entity's statement of financial position, the following information must be given:

(a) the aggregate amounts (on the basis of cost or revaluation) in respect of that item as at the date of the beginning of the reporting period and as at the reporting date respectively.

(b) the effect on any amount shown in the statement of financial position in respect of that item of:

(i) any revision of the amount in respect of any assets included under that item made during the reporting period as a result of revaluation;

(ii) acquisitions during the reporting period of any assets;

(iii) disposals during the reporting period of any assets; and

(iv) any transfers of assets of the small entity to and from that item during the reporting period. (Schedule 1, paragraphs 48(1) and 48(2))

FRS 105

As illustrated below, the situation under FRS 105 also does not permit the client's previous accounting treatment of goodwill.

"G*oodwill arising on a trade and asset acquisition*

14.2 Where a micro-entity has recognised goodwill acquired in a trade and asset acquisition (in accordance with paragraph 19.22 of FRS 102), the micro-entity shall measure that goodwill at cost less accumulated amortisation and accumulated impairment losses:

(a) A micro-entity shall follow the principles in paragraphs 13.9 to 13.14 of this FRS for amortisation of goodwill. Goodwill shall be considered to have a finite useful life, and shall be amortised on a systematic basis over its life. If, in exceptional cases, a micro-entity is unable to make a reliable estimate of the useful life of goodwill, the life shall not exceed ten years.

(b) A micro-entity shall follow Section 22 Impairment of Assets of this FRS for recognising and measuring the impairment of goodwill."

NATIONAL MINIMUM WAGE AND NATIONAL LIVING WAGE

The National Minimum Wage and National Living Wage limits were increased with effect from 1 April 2017.

Workers aged 25 and over, and not in the first year of an apprenticeship, are legally entitled to at least the National Living Wage. Workers aged under 25, or an apprentice, are legally entitled to at least the National Minimum Wage. The National Minimum Wage and National Living Wage are set out in the Table 1.

Table 1

Date	25 & over	21 to 24	18 to 20	Under 18	Apprentice
1 October 2016 (current rate)	£7.20	£6.95	£5.55	£4.00	£3.40
1 April 2017	£7.50	£7.05	£5.60	£4.05	£3.50

Further information is available from the Government's Check your pay campaign website at: **https://checkyourpay.campaign.gov.uk/**.

Statutory redundancy pay and employment tribunal awards

In addition, the maximum amount of statutory redundancy pay and the limit on the amount employment tribunals can award for unfair dismissal were increased from 6 April 2017. These increase every year in line with the retail prices index.

From 6 April 2017, the maximum weekly rate payable as statutory redundancy is £489, increasing from £479. The maximum award of statutory redundancy pay also increased to £14,670 from £14,370. Where an employer is insolvent, employees are subject to these limits in respect of claims which can be made from the Redundancy Payments Office, even if they are contractually entitled to a higher rate.

Employers that dismiss employees for redundancy must pay those with two years' service an amount based on the employee's weekly pay, length of service and age.

The maximum compensatory award for unfair dismissal also increased to £80,541 from the current £78,962.

The increased rates apply where the date of redundancy, or the effective date of termination, is on or after 6 April 2017.

The new rates are set out in the Employment Rights (Increase of Limits) Order 2017 which can be found at: **http://www.legislation.gov.uk/uksi/2017/175/made**.

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