

Welcome to the latest issue of Update, a WK electronic communication that keeps you up to date with topical audit and accounting issues.

IFRS for Small and Medium Sized Entities (SME's)

The International Accounting Standards Board has published an exposure draft of an IFRS for SME's, the aim of which is to provide a simplified, self-contained set of standards appropriate for small and non listed companies.

The IFRS is intended for an entity with no public accountability and typically up to 50 employees. There is no quantified size test included in the draft although it is likely that these will be added by jurisdictions when adopting the IFRS.

Some topics in full IFRS's have been omitted including interim reporting, lessor accounting, recoverable amount of goodwill, earnings per share and segmental reporting and insurance contracts. In other IFRS's, only the simpler option has been included e.g. grants, expense borrowing costs, cost – amortization impairment model for property, plant and intangibles and cost – depreciation model for investment property. There are also various simplifications of the recognition measurement principles e.g. financial instruments, goodwill, impairment, research and development costs, share-based payments, finance leases and defined benefit schemes.

In addition, many disclosures have been dropped and according to the IASB, it has been written in plain English! However, it has not removed the need to prepare a cash flow or consolidate and neither has it included the proposals to treat all leases as operating, all pensions as defined contribution, have fewer provisions, to have no deferred tax liabilities and have non- recognition of share-based payments or derivatives.

Before issuing the final standard expected in mid 2008, the ASB is giving further consideration to what it believes are its three main implications. Firstly, the role of the IFRS for SME's within the ASB's convergence project i.e. its suitability for mid tier entities between the existing FRSSE and those required to apply the full IFRS. Secondly, whether it should be a replacement for the FRSSE and thirdly, what changes will need to be made if it is considered suitable for either of the above.

SME Thresholds and Audit Exemption

The thresholds for small companies currently entitled to audit exemption will be increased for periods commencing 6 April 2008 onwards as follows:

| | | |
|------------------------------|----------|--------------------|
| Turnover | < £6.5m | (previously £5.6m) |
| Balance sheet (gross assets) | < £3.26m | (previously £2.8m) |

In addition, the gross exemption limits for groups will be increased to £7.8m and £3.9m respectively.

These thresholds will also apply for abbreviated accounts with the medium sized company and related group thresholds being increased as follows:

| | |
|---------------|---------------------------------|
| Turnover | < £25.9m (group < £31.1m gross) |
| Balance Sheet | < £12.9m (group < £15.5m gross) |

Note: Employee thresholds remain the same - small companies < 50
- medium companies < 250

Related Party Disclosures

Under FRED41, which it is anticipated will become effective in 2009, there will be several changes to the disclosures currently required under FRS8. In particular, FRED41:

- will require disclosure of remuneration and other benefits paid to key management personnel;
- will require a statement that transactions are at arm's length if the terms can be substantiated – in other words silence will imply that not all transactions are at arm's length whereas silence under FRS8 implies currently the opposite.

Current EU Proposals for Small Companies

Possible changes being considered by the EU include the following radical proposals:

- the establishment of new micro companies with more significant exemptions including possibly dispensing with the need to prepare statutory accounts

(the possible definition of a micro company being one with less than 10 employees, balance sheet total below € 500,000 and a turnover of below € 1m).

- will permit all disclosures to be given in aggregated form;
- extension of the years rules – five to lose small company status and just one to be small again;
- abolition of the requirement to publish small company accounts;
- extension of small company exemptions to certain medium sized companies – companies where the managers are the owners (provided that no other member has more than 5%) and unlimited liability companies and
- audit exemption for subsidiaries.

Business Review

Under the provisions of the Companies Act 2006, Directors will be protected from being sued on comments included within a business review in the Directors' Report, providing they can prove that they did not act recklessly. However, any comments made in a Chairman's Statement, will not receive this "safe harbour" as this statement is not a Companies Act requirement.

Directors' Duties

The 2006 Companies Act has codified Directors' duties setting out that as well as having a duty to members as a whole, Directors must have regard to the following:

- the likely consequences of any decision in the long term;
- the interests of the company's employees;
- the need to foster the company's business relationships with suppliers, customers and others;
- the impact of the company's operations on the community and the environment;
- the desirability of thep
- company maintaining a reputation for higher standards of business conduct and
- the need to act fairly as between members of the company.

How or what difference this has in practice remains to be seen.

Transactions with Directors Requiring Approval of Members

Under the Companies Act 2006, with effect from 1 October 2007, the de minimus level for requiring members' approval of a substantial property transaction has been increased to £5,000 (sections 190 and 191),

In addition, companies are not permitted to make a loan to a director or give a guarantee to provide security in connection with a loan to a director without members' approval (section 197).

Further sections deal with quasi loans and other issues relating to loans as well as payments for loss of office which also generally require members' approval and under section 223 all of the above requirements are extended to shadow directors.

Charity Accounting – Compact and Impact

One of the most significant areas of change in charity accounting regulations, SORP 2005, effective for periods commencing on or after 1 April 2005, is the disclosure requirements for charity trustee reports. The impact of this being that it is the main area where many charities are still failing to comply and for those that are complying it has led to a considerable increase in the number of pages in some charity's accounts. Some accounts can now run into 10's of pages which although full of very useful and interesting information are probably read by very few people. The Trustee report should set out amongst other information:

- Governance information including trustee training and induction
- Vision and Mission – optional
- Objects – as set out in the governing document
- Aims – strategies of achieving the objects
- Objectives - activities during the year
- Measurement of achievements against performance including outputs and impact
- Future plans
- Policies in place, eg reserve policy
- Commentary on risk review

Charity accounts can be accessed free of charge by anyone interested in reading them so are an important marketing medium for the charity – therefore information should be kept **simple, readable, be transparent and compact** whilst giving the reader of the accounts an idea of the **activities, performance and outputs of the charity** as well as the **impact** the charity has made to its beneficiaries.

For further information please contact the following members of our charity and not-for-profit team - John Howard (0207 403 1877) or Michelle Wilkes (01689 827505).

You are welcome to contact us

If you would like further information on any of the topics raised in this Update, please do not hesitate to contact the Wilkins Kennedy partner or manager who normally handles your affairs or any of the individuals below.

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