Financial Reporting Council

Accounting and Reporting Policy
FRS 102

Staff Education Note 13
Transition to FRS 102

This Staff Education Note was updated as follows:

(a) on 8 January 2014 for minor typographical errors in the suggested reconciliations on pages 11 to 13; and

(b) on 28 April 2015 to clarify the examples and revise the descriptions of the transitional exemptions to align with the requirements in the August 2014 edition of FRS 102.

(c) On 27 October 2015 to align with the September 2015 edition of FRS 102.

Contents

Introduction

Section 35 *Transition to this FRS* of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* applies to the first-time adoption of FRS 102 and sets out how an entity prepares its first financial statements that conform with that standard.

FRS 102 is effective for accounting periods beginning on or after 1 January 2015. It requires the comparative and opening balance sheet at the date of transition to be restated in accordance with FRS 102; the date of transition being the beginning of the earliest period for which an entity presents full comparative information. However, the opening balance sheet itself does not need to be presented.

FRS 102 requires the presentation of reconciliations of equity determined in accordance with its previous financial reporting framework and its equity determined in accordance with FRS 102 at two dates:

(a) the date of transition to FRS 102; and

(b) the end of the latest period presented in the entity's most recent annual financial statements determined in accordance with its previous financial reporting framework.

FRS 102 requires the presentation of a reconciliation of profit or loss determined in accordance with its previous financial reporting framework for the latest period in the entity's most recent annual financial statements to its profit or loss determined in accordance with FRS 102 for the same period.

For example, for an entity with a 31 December year end, the first year of mandatory application will be the year ending 31 December 2015. The entity will need to restate its opening balance sheet at the date of transition (ie at 1 January 2014) and comparative balance sheet (ie at 31 December 2014) in accordance with FRS 102, although the opening balance sheet does not need to be presented. The entity will need to prepare reconciliations of equity at 1 January 2014 and 31 December 2014 and of its profit or loss for the year ending 31 December 2014.

This Staff Education Note is written to highlight key areas of consideration when transitioning to FRS 102 and is not designed to be exhaustive.

This Staff Education Note is based on the requirements of FRS 102 issued in September 2015.

Transitional procedures

FRS 102 requires the balance sheet at the date of transition to be prepared in accordance with the recognition and measurement requirements of FRS 102.

Required amendments – Retrospective restatement

Paragraph 35.7 of FRS 102 requires an entity to:

(a) recognise all assets and liabilities whose recognition is required by FRS 102 (eg forward exchange contracts);

(b) not recognise items as assets or liabilities if FRS 102 does not permit their recognition;

(c) reclassify items (eg into different groupings in the cash flow statement); and

(d) restate certain assets and liabilities at a different value (eg financial instruments measured at amortised cost using the effective interest rate, which in some cases may vary from a previously used historical cost).

Paragraph 35.8 of FRS 102 states that adjustments on transition shall be recognised in retained earnings, or where appropriate, another category within equity.

For example, an entity with a date of transition of 1 January 2014 is required to reassess all its assets and liabilities as at 31 December 2013 and make any adjustments that are necessary to recognise and measure them in accordance with FRS 102.

Exceptions to retrospective restatement

Paragraph 35.9 of FRS 102 states that on first-time adoption of FRS 102, an entity shall not retrospectively change the accounting that it followed under its previous financial reporting framework for any of the following transactions:

(a) ***Derecognition of financial assets and financial liabilities:***
Financial assets and liabilities derecognised under an entity's previous accounting framework before the date of transition shall not be recognised upon adoption of this FRS. Conversely, for financial assets and liabilities that would have been derecognised under this FRS in a transaction that took place before the date of transition, but that were not derecognised under an entity's previous accounting framework, an entity may choose:

(i) to derecognise them on adoption of this FRS; or

(ii) to continue to recognise them until disposed of or settled.

(b) [Not used]

(c) ***Accounting estimates*** (see Example 1 below).

(d) ***Discontinued operations.***

(e) *Measuring* ***non-controlling interests***:
The requirements:

(i) to allocate profit or loss and total comprehensive income between non-controlling interest and owners of the parent;

(ii) for accounting for changes in the parent's ownership interest in a subsidiary that do not result in a loss of control; and

(iii) for accounting for a loss of control over a subsidiary

shall be applied prospectively from the date of transition to this FRS (or from such earlier date as this FRS is applied to restate business combinations).

Optional exemptions

Paragraph 35.10 of FRS 102 provides a number of exemptions that entities may elect to use on transition to FRS 102. These aim to ease or remove the requirements of paragraph 35.7 of FRS 102 for the restatement of assets and liabilities at the date of transition. The optional exemptions in paragraph 35.10 of FRS 102 are (some of these have been summarised):

(a) ***Business combinations including group reconstructions:*** An entity may elect not to restate business combinations that occurred before the transition date (see Example 2). However, if a first-time adopter restates any business combination to comply with FRS 102, it shall restate all later combinations. If a first-time adopter chooses not to apply Section 19 *Business Combinations* retrospectively, the first-time adopter shall recognise and measure all of its assets and liabilities acquired or assumed in a past business combination at the date of transition to FRS 102 in accordance with the requirements of FRS 102, except for goodwill and intangible assets subsumed in goodwill.

If a first-time adopter elects not to apply Section 19 retrospectively, it will still need to apply Section 19 prospectively to any goodwill recognised in its balance sheet at the date of transition. As noted above, the carrying amount of the goodwill would not be adjusted on transition, however it would be amortised over a finite useful life going forward. For an entity that has previously determined a finite useful life for goodwill, the entity can continue to amortise that goodwill over this period so long as it is a reliable estimate of the useful life. For an entity that has previously determined an indefinite useful life for goodwill, the entity will need to reassess the remaining useful life going forward. If an entity is unable to reliably estimate the useful life of goodwill, then the useful life shall not exceed ten years.

(b) ***Share-based payment transactions (revised in July 2015):*** An entity may elect not to apply FRS 102 to equity instruments (including the equity component of an instrument that was under previous GAAP treated as a compound instrument) that were granted before the date of transition. Entities selecting this option that have previously applied FRS 20 *(IFRS 2) Share-based payments* or IFRS 2 *Share-based payments* shall continue to apply either FRS 20 or IFRS 2 to these instruments. Entities are not required to apply FRS 102 to liabilities arising from share-based payment transactions that were settled before the transition date. For small entities[1] that have not previously applied either FRS 20 or IFRS 2, the exemption is extended to all equity instruments granted before the start of the first

[1] Small entities are defined in FRS 102 (refer to the Glossary).

reporting period in which the entity adopts FRS 102, provided that they apply FRS 102 for the first time before 1 January 2017.

(c) ***Fair value as deemed cost:*** An entity may elect for an item of property, plant or equipment, an investment property, or an intangible asset that meets the recognition criteria and the criteria for revaluation, to be measured at its fair value at the date of transition and for that fair value to be used as the deemed cost of the item going forward.

(d) ***Revaluation as deemed cost:*** For a revalued item of property, plant or equipment, investment property, or intangible asset that meets the recognition criteria and the criteria for revaluation, an entity may elect to use as its deemed cost, its revalued amount either at, or before the date of transition (see Example 3).

(e) [Not used]

(f) ***Individual and separate financial statements:*** For investments in subsidiaries, associates and jointly controlled entities, an entity may elect to use the carrying amount at the date of transition determined under its previous GAAP as its deemed cost going forward.

(g) ***Compound financial instruments:*** For compound financial instruments where the liability component is not outstanding at the date of transition, an entity may elect not to separate out the liability and equity components.

(h) [Not used]

(i) ***Service concession arrangements – Accounting by operators:*** An entity may elect not to apply FRS 102 to service concessions arrangements that were entered into before the date of transition. Instead, its previous accounting policies would continue to be applied. A similar exemption is not available to grantors.

(j) ***Extractive activities:*** Oil and gas exploration and evaluation assets and other oil and gas assets in development or production phases may be measured at an amount determined under previous GAAP, subject to impairment tests at the date of transition.

(k) ***Arrangements containing a lease:*** An entity may elect to determine whether an arrangement contains a lease based on the facts and circumstances existing at the date of transition, rather than when the arrangement was entered into.

(l) ***Decommissioning liabilities included in the cost of property, plant and equipment:*** An entity may elect to measure the component of the cost of an item of property, plant and equipment resulting from decommissioning liabilities at the date of transition rather than on the date when the obligation initially arose.

(m) ***Dormant companies:*** There is no requirement for dormant companies to restate the opening balance sheet at the date of transition (nor any subsequent balance sheets) until there is a change in its existing balances or the company undertakes any new transactions.

(n) ***Deferred development costs as deemed cost:*** An entity may elect to carry forward the carrying amount of development costs deferred in accordance with SSAP 13 *Research and development* as the deemed cost at that date (see Example 4).

(o) ***Borrowing costs:*** An entity electing to adopt an accounting policy of capitalising borrowing costs may elect to treat the date of transition as the date on which capitalisation of borrowing costs commences (see Example 5).

(p) ***Lease incentives:*** An entity may elect not to apply FRS 102 to lease incentives provided the term of the lease commenced before the date of transition. Instead, the previous accounting treatment would continue to apply.

(q) ***Public benefit entity combinations:*** An entity may elect not to apply FRS 102 to public benefit entity combinations that were effected before the date of transition. However, if a public benefit entity restates any entity combination to comply with this section, it shall restate all later entity combinations.

(r) ***Assets and liabilities of subsidiaries, associates and joint ventures:*** Where the transition date of a subsidiary differs from that of its parent, the subsidiary, may elect to measure its assets and liabilities either at the date of transition of the parent or at the date the subsidiary transitions to FRS 102. A similar election is available to associates and joint ventures.

(s) ***Designation of previously recognised financial instruments:*** An entity may elect to designate previously recognised financial instruments at fair value through profit or loss on the date of transition provided they meet the criteria set out in paragraph 11.14(b) of FRS 102.

(t) ***Hedge accounting (revised in July 2014):*** An entity may apply hedge accounting prior to the documentation requirements set out in paragraphs 12.18(d) and (e) of FRS 102 being met, provided the required documentation is in place no later than the date the first FRS 102 compliant financial statements are authorised for issue. Further, when a hedging relationship has ceased to exist prior to the date of transition, an entity is not required to adjust the carrying amount of a hedged item. An entity that chooses to apply IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 9 *Financial Instruments*, as permitted by FRS 102, applies IFRS 1 *First-time adoption of International Financial Reporting Standards* instead of the transitional requirements and exemptions in FRS 102, subject to certain reliefs that apply in respect of the documentation requirements.

(u) ***Small entities[2] — fair value measurement of financial instruments:*** A small entity that did not measure financial instruments at fair value under its previous GAAP is not required to restate the comparative period information to comply with the fair value measurement requirements for financial instruments (eg for derivatives) of FRS 102. This exemption is only available to small entities applying FRS 102 for the first time before 1 January 2017.

(v) ***Small entities[2] — financing transactions involving related parties:*** A small entity is not required to restate comparative information in accordance with the accounting requirements for financing transactions[3] involving related parties in Section 11 *Basic Financial Instruments*. This exemption is only available to small entities applying FRS 102 for the first time before 1 January 2017.

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[2] Small entities are defined in FRS 102 (refer to the Glossary).
[3] Please refer to Staff Education Note 16 *Financing transactions* for more detail on this topic.

Examples

Examples 1 to 5 in this Education Note relate to entities which have a 31 December 2015 year end and prepare their first set of financial statements that are compliant with FRS 102 as at that date. Their date of transition to FRS 102 is 1 January 2014.

Example 1 Accounting estimates

At 31 December 2013, Entity A had a debtor balance of CU500. At 31 December 2013 Entity A was concerned about the credit risk of the debtor and was in discussion with the debtor as to how the debt might be settled. As a consequence Entity A had made a provision of CU250, ie for 50 per cent of the balance as at that date. During 2014 the debtor collapsed and was liquidated.

When Entity A prepares its opening balance sheet as at 1 January 2014 in accordance with FRS 102 it no longer believes it will collect any of the outstanding debt. However, Entity A does not revise its previous estimate taking into account hindsight for preparing its opening balance sheet as at 1 January 2014, because paragraph 35.9(c) of FRS 102 prohibits retrospective adjustments to accounting estimates on the date of transition.

Example 2 Business combination before the date of transition

On 1 January 2010, Entity B acquired a wholly owned subsidiary and applied the requirements of FRS 6 *Acquisitions and Mergers* and FRS 7 *Fair Values in Acquisition Accounting*. In accordance with these FRSs, Entity B recognised the following opening fair values in its consolidated financial statements: Entity B did not recognise deferred tax in respect of any of the fair value adjustments made on acquisition.

	CU	**CU**
Property, plant and equipment	30,000	
Goodwill	10,000	
		40,000
Stock	1,000	
Debtors	1,500	
Net current assets	2,500	
Creditors	(3,000)	
Net current liabilities		(500)
Net assets acquired at fair value		39,500

On transition (1 January 2014):

(1) Measurement of goodwill

Paragraph 19.23(a) of FRS 102 states that goodwill shall be considered to have a finite useful life and in the exceptional cases when an entity is unable to make a reliable estimate of the useful life, the life shall not exceed 10 years.

On acquisition in 2010, Entity B decided that in accordance with FRS 10 *Goodwill and intangible assets* the goodwill had an economic life of 15 years. At 31 December 2013 the carrying amount for the goodwill is therefore CU7,333[4] and has a remaining useful life of 11 years.

Entity B considers there is evidence to support the remaining useful economic life of 11 years and provides adequate evidence to support this. It is therefore not required to adjust the expected amortisation profile.

(2) Measurement of other acquired assets and liabilities

As permitted by paragraph 35.10(a) of FRS 102 Entity B decides not to apply the requirements of Section 19 *Business Combinations and Goodwill* retrospectively to the acquired assets and liabilities. In this case Entity B is still required to recognise and measure those acquired assets and liabilities that remain within the group at the date of transition in accordance with the other first-time adoption accounting requirements set out in paragraphs 35.7 to 35.9 and paragraphs 35.10 (b) to (t) of FRS 102.

Entity B determines that no adjustments to the acquired assets and liabilities are required in accordance with the first-time adoption accounting requirements of FRS 102, except for deferred tax. Paragraph 29.6 of FRS 102 requires the recognition of deferred tax on all timing differences. Entity B still owns the acquired property, plant and equipment which were fair valued on the date of acquisition. Entity B measures the deferred tax liability on the fair value adjustments (to the extent that they have not been reduced by depreciation prior to the date of transition) based on tax rates enacted or substantively enacted at the date of transition and records the corresponding adjustment in equity.

Example 3 Revaluation as deemed cost

Entity C has two properties, A and B. Neither Property A nor Property B is an investment property. Entity C has an accounting policy to revalue its properties and to depreciate them over a useful life of 50 years.

Property A was acquired on 31 December 1980 at a cost of CU1,000 and has been revalued on a regular basis; the last time was on 31 December 2010 when its value was recorded in the financial statements at CU100,000 and its remaining useful life was 20 years. There has been no significant change in the value of Property A since that revaluation.

Property B was acquired on 31 December 2010, at a cost of CU50,000. Property B has never been revalued as it was purchased in the same year that the most recent valuation was carried out and at that time its cost was the best available evidence of its valuation. There has been no impairment in its value.

On transition (1 January 2014):

Entity C decides not to continue its policy of revaluation as permitted by FRS 102.

Property A

Paragraph 35.10(d) provides an optional exemption from restating the value of the property based on its original cost. Therefore Entity C has the following two choices in relation to Property A:

a) it could elect to use the most recent revaluation from 2010 (being CU100,000) as its deemed cost at that date and no further adjustment is required; or
b) it could restate the property to its original cost of CU1,000.

[4] Being CU10,000 x 11/15 years

If the revalued amount of CU100,000 were used as its deemed cost, in order to comply with company law the revaluation reserve would be retained and the excess depreciation would continue to be offset against it.

If the property is restated to the original cost of CU1,000 the following adjustment would be required:

Dr	Revaluation Reserve	CU84,660
Dr	Accumulated depreciation	CU14,340[5]
Cr	Property, plant and equipment	CU99,000

Property B

No adjustment is required on transition for Property B[6].

Example 4 Carrying value of development costs

Entity D had previously made an accounting policy choice to capitalise development costs meeting the criteria set out in SSAP 13 *Accounting for research and development*.[7]In 2010 Entity D undertook a programme to develop the products it acquired as part of an earlier acquisition to make them compatible with products it had developed in-house. In accordance with SSAP 13, it capitalised CU2,500 of expenditure which it is amortising over five years. Four years later at 31 December 2013, the carrying amount of asset was therefore CU500.

Paragraph 18.8H of FRS 102 permits an entity to recognise an intangible asset arising from the development phase of an internal project providing it meets certain criteria. Entity D makes the accounting policy choice to capitalise development costs meeting the criteria set out in Section 18 *Intangible Assets other than Goodwill* of FRS 102.

As permitted by paragraph 35.10(n), Entity D may elect to take the carrying amount of those development costs deferred in accordance with SSAP 13 at the date of transition to be the deemed cost going forward. Therefore, although in this example it is unlikely that there is a material difference between the carrying value of the development costs measured using SSAP 13 or FRS 102, for ease Entity D elects to retain the value determined in accordance with SSAP 13 as the deemed cost of deferred development costs and makes no adjustment to the carrying value of the deferred development costs at the date of transition.

Example 5 Borrowing costs

Entity E decided to construct a new building for its own use. Work on the construction commenced during 2013. Entity E capitalised tangible fixed assets on the basis of cost, in accordance with FRS 15 *Tangible Fixed Assets*, but had not previously constructed any significant assets and therefore its accounting policy did not include the capitalisation of finance costs.

As at 31 December 2013, Entity E had capitalised construction costs of CU25,000 and estimated that it still had approximately nine months of construction work ahead. Had Entity E

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5 This represents three years depreciation (from 31 December 2010 to 1 January 2014) on the revalued amount being £15,000 in total (CU100,000 x 3 / 20 years remaining) less 33 years depreciation (from 31 Dec 1980 to 1 January 2014) on the historical cost being CU660 in total (CU1,000 x 33 / 50 years) which is not adjusted for.

6 The exemption to permit revaluation as deemed cost is available at the level of individual items of property, plant and equipment. Entity C could choose to revalue Property B at the date of transition and use that new valuation as deemed cost. Similarly, as an alternative to using the 2010 valuation for Property A, Entity C could revalue it at the transition date (irrespective of whether Property B is revalued at transition date).

7 Research expenditure must be expensed as incurred (SSAP 13 paragraph 24), but SSAP 13 permits a choice of accounting policy for development expenditure meeting certain criteria. Development expenditure may be written off as incurred, or deferred to future periods and amortised (SSAP 13 paragraphs 25 to 28).

had a policy of capitalisation, finance costs that could have been capitalised amounted to CU300.

During 2014 Entity E completed construction of the building. The total cost to be capitalised in accordance with FRS 102 (excluding borrowing costs) is CU90,000. Qualifying borrowing costs calculated in accordance with FRS 102 relating to the project as a whole are CU2,500.

On transition to FRS 102, Entity E reviews its accounting policies and decides that it will now elect to capitalise borrowing costs in accordance with Section 25 *Borrowing Costs* of FRS 102, and in accordance with paragraph 35.10(o) it elects to capitalise costs prospectively from 1 January 2014. As a result, no adjustment is made to the carrying value of the asset at the date of transition (ie 1 January 2014); the CU300 previously written off are not capitalised, but CU2,200[8] of borrowing costs are capitalised during the year ended 31 December 2014.

[8] The amount capitalised is £2,200 = £2,500 (total qualifying borrowing costs) - £300 (borrowing costs incurred prior to 1 January 2014 and elected not to be capitalised).

Required transitional disclosures

Explanation of transition to FRS 102

Paragraph 35.12 states that an entity[9] shall explain how the transition from its previous financial reporting framework to FRS 102 affected its reported financial position and performance.

Paragraph 35.13 states that to comply with the above an entity's first financial statements prepared using FRS 102 shall include:

(a) a description of the nature of each change in accounting policy.

(b) reconciliations of its equity determined in accordance with its previous financial reporting framework to its equity determined in accordance with this FRS [FRS 102] for both of the following dates:

   (i) the date of transition to this FRS [FRS 102]; and

   (ii) the end of the latest period presented in the entity's most recent annual financial statements determined in accordance with its previous financial reporting framework.

(c) a reconciliation of the profit or loss determined in accordance with its previous financial reporting framework for the latest period in the entity's most recent annual financial statements to its profit or loss determined in accordance with this FRS [FRS 102] for the same period.

Paragraph 35.14 states that if an entity becomes aware of errors made under its previous financial reporting framework, the reconciliations required shall, to the extent practicable, distinguish the correction of those errors from changes in accounting policies.

FRS 102 does not specify the format of the reconciliations of equity and profit or loss. Set out below are suggested formats for the reconciliations, but entities will need to determine the most suitable format for their reconciliations taking into account the nature and amount of their own adjustments.

Example 6 Disclosure of transition to FRS 102

Entity F prepares its first financial statements that comply with FRS 102 for the year ended 31 December 2015. Entity F's date of transition to FRS 102 is 1 January 2014. For Entity F the transition to FRS 102 has resulted in only a small number of changes in accounting policies compared to those used previously.

The following examples of notes to the financial statements of Entity F describe the differences between equity and profit or loss presented previously, and the amounts as restated to comply with the accounting policies selected in accordance with FRS 102 for the reporting period ended at 31 December 2014 (ie comparative information), as well as equity presented in the opening statement of financial position (ie at 1 January 2014). It also describes all the required changes in accounting policies made on first-time adoption of FRS 102.

[9] Small entities (as defined in the Glossary of FRS 102) are not required to make the disclosures set out in Section 35, but should consider whether they are necessary for their financial statements to give a true and fair view (paragraph 1A.17 of FRS 102). Small entities are required to make the disclosures required by paragraphs 1AC.7 to 1AC.9 of FRS 102 in respect of changes in presentation and accounting policies and correction of errors.

Reconciliations
Suggested Option 1
Reconciliation of equity

	Note	At 1 Jan 2014 As previously stated	At 1 Jan 2014 Effect of transition	At 1 Jan 2014 FRS 102 (as restated)	At 31 Dec 2014 As previously stated	At 31 Dec 2014 Effect of transition	At 31 Dec 2014 FRS 102 (as restated)
		CU '000	CU '000	CU '000	CU '000	CU '000	CU '000
Fixed assets		5,868	-	5,868	5,416	-	5,416
Current assets	(i) (ii)	2,475	15	2,490	2,520	17[a]	2,537
Creditors: amounts falling due within one year	(i) (iii)	(2,355)	(16)[b]	(2,371)	(1,824)	(20)[c]	(1,844)
Net current assets		120	(1)	119	696	(3)	693
Total assets less current liabilities		5,988	(1)	5,987	6,112	(3)	6,109
Creditors: amounts falling due after more than one year	(i)	(2,900)	(6)	(2,906)	(2,840)	(3)	(2,843)
Provisions for liabilities		(410)	-	(410)	(465)	-	(465)
Net assets		2,678	(7)	2,671	2,807	(6)	2,801
Capital and reserves		2,678	(7)	2,671	2,807	(6)	2,801

Reconciliation of profit or loss for the year

	Note	Year ended 31 Dec 2014 As previously stated	Effect of transition	FRS 102 (as restated)
		CU '000	CU '000	CU '000
Turnover		832	-	832
Cost of sales	(i) (ii)	(520)	1[d]	(519)
Gross profit		312	1	313
Administrative expenses	(i) (ii) (iii)	(65)	0[e]	(65)
Other operating income		42	-	42
Operating profit		289	1	290
Interest receivable and similar income		5	-	5
Interest payable and similar charges		(130)	-	(130)
Taxation		(35)	-	(35)
Profit on ordinary activities after taxation and for the financial year		129	1	130

Reconciliations
Suggested Option 2
Reconciliation of equity

	Note	At 1 Jan 2014	At 31 Dec 2014
	Note	CU '000	CU '000
Capital and reserves (as previously stated)		2,678	2,807
Recognition of derivative financial instruments	(i)	(2)	1
Re-measurement of stock using spot exchange rate	(ii)	-	(1)
Short-term compensated absences	(iii)	(5)	(6)
Capital and reserves (as restated)		2,671	2,801

Reconciliation of profit or loss for the year

	Note	Year ended 31 Dec 2014
		CU '000
Profit for the year (as previously stated)		129
Recognition of derivative financial instruments	(i)	3
Re-measurement of stock using spot exchange rate	(ii)	(1)
Short-term compensated absences	(iii)	(1)
Profit for the year (as restated)		130

Notes to the reconciliations

The following notes are applicable to both formats set out above.

Financial instruments

(i) Entity F was not previously required to recognise derivative financial instruments on the balance sheet. Instead the effects of the derivative financial instruments were recognised in profit or loss when the instruments were settled. Derivative financial instruments are classified as 'other financial instruments' in FRS 102 and are recognised as a financial asset or a financial liability, at fair value, when an entity becomes party to the contractual provisions of the instrument. Consequently financial assets of CU15,000 and financial liabilities of CU17,000 have been recognised in the opening balance sheet at 1 January 2014. Financial assets of CU18,000 and financial liabilities of CU17,000 have been recognised in the balance sheet as at 31 December 2014. Derivatives are measured to fair value with gains (losses) from changes in fair value recognised in profit or loss. The effect on profit for the year ended 31 December 2014 is an increase of CU3,000.

(ii) The derivative financial instruments are foreign exchange forward contracts. In applying SSAP 20 *Foreign currency translation*, Entity F previously chose to translate purchases in foreign currencies at the rate of exchange specified in a matching forward contract. This is not permitted by FRS 102, which requires purchases to be translated using the spot exchange rate on the date of the transaction. FRS 102 does not provide an exemption from measuring stock bought in a foreign currency and paid for before the transition date in accordance with its required accounting policies, but the difference is not material and accordingly no adjustment has been made. Items purchased since the transition date have been re-measured based on spot exchange rate. Consequently stock at 31 December 2014 has been reduced and cost of sales for the year end has been increased by CU1,000 and costs of CU2,000 have been reclassified as administrative expenses rather than cost of sales.

Short-term compensated absences

(iii) Prior to applying FRS 102, Entity F did not make provision for holiday pay (ie holiday earned but not taken prior to the year-end). FRS 102 requires the cost of short-term compensated absences to be recognised when employees render the service that increases their entitlement. Consequently an additional accrual of CU5,000 at 1 January 2014 has been made to reflect this. The additional provision at 31 December 2014 is CU6,000 and the effect on profit for the year ended 31 December 2014 is an additional expense of CU1,000.

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[a] Made up of financial assets of CU18,000 (Note (i)) and the decrease in stock of CU1,000 (Note (ii)).

[b] Made up of financial liabilities of CU17,000 (Note (i)) less creditors amounts falling due after more than one year of CU6,000 plus the holiday pay accrual of CU5,000 (Note (iii)).

[c] Made up of financial liabilities of CU17,000 (Note (i)) less creditors amounts falling due after more than one year of CU3,000 plus the holiday pay accrual of CU6,000 (Note (iii)).

[d] Made up of an increase of CU1,000 (Note (ii)) less the reclassification of CU2,000 to administrative expenses (Note (ii)) giving an overall reduction in cost of sales of CU1,000.

[e] Made up of a profit (ie a reduction in administrative expenses) from the recognition of the derivatives of CU3,000 (Note (i)), an increase from the reclassification of CU2,000 (Note (ii)) and an increase in the holiday pay accrual of CU1,000 (Note (iii)) giving an overall nil effect.