

## 1 Events after the end of the reporting period (Lecture A686 – 13.39 minutes)

Events after the reporting period (or 'post balance sheet events' as many accountants are familiar with) are dealt with in FRS 102 at Section 32 *Events after the end of the Reporting Period*. Such events can have a significant impact on a company's financial statements because of the need to reflect certain transactions which take place after the year end but occur after the year end in the financial statements; and to disclose other material issues whose conditions did not exist at the year end.

Section 32 refers to two types of event under its scope:

- adjusting events; and
- non-adjusting events.

### 1.1 Adjusting events

An adjusting event is one which is reflected within the financial statements and is an event where the conditions existed at the year/period end but which crystallises after the year/period end. The key to identifying whether the event is adjusting is to ensure that it is clear that the conditions giving rise to the event existed at the balance sheet date. FRS 102, paragraph 32.5 contains some examples of adjusting events as follows:

- The settlement of a court case after the balance sheet date which confirms that an entity had present obligation at the balance sheet date. Any previously recognised provision related to this court case is adjusted in accordance with FRS 102, Section 21 *Provisions and Contingencies* or the entity recognises a new provision.
- Receipt of information after the balance sheet date which confirms that an asset has suffered impairment such as:
  - the classic scenario of the bankruptcy of a customer after the balance sheet date which confirms the trade debtor is irrecoverable (ie impaired); and
  - sale of stock after the balance sheet date which may give evidence relating to their estimated selling price less costs to complete and sell (i.e. selling price is less than cost).
- The cost of assets purchased after the balance sheet date, or proceeds received from the sale of assets sold prior to the balance sheet date.
- Determination of profit-sharing bonus payments made after the balance sheet date if the entity had a legal or constructive obligation at the balance sheet date to make such payments as a result of events before that date (see Section 28 *Employee Benefits*).

- Discovery of fraud/error which show that the financial statements are incorrect.

If the conditions relating to the above existed at the balance sheet date, they would be reflected within the financial statements.

#### **Example – Bonus payments**

Bury Co Ltd has always paid bonuses to its two directors based on 5% of profit before tax. The draft management accounts as at 30 November 2019 include a gross bonus, plus employer's NIC amounting to £31,500 each following the resolution to pay a bonus based on the draft figures on 20 November 2019. This bonus is not paid until such time that the financial statements are approved because of various adjustments that are often incorporated into the finalised financial statements. The financial statements are approved four months after the year end and because of a large stock write-down, the profits have reduced to such an extent that the gross bonus, plus the employer's NIC should only be £14,500 each.

This is an example of an adjusting event because the decision to pay the bonuses was made prior to the year end and therefore bonuses will need to be reduced.

### **1.2 Non-adjusting events**

Non-adjusting events are those that are indicative of conditions that arose after the end of the reporting period but before the financial statements are approved. In other words, their conditions did not exist at the balance sheet date.

By their definition, non-adjusting events are not adjusted for in the financial statements. Instead, additional disclosures may be required in the financial statements. Some practitioners have fallen foul to non-compliance with standards regarding post-balance sheet events in the belief that if an event occurs after the year end, then that is all there is to it and the event will be dealt with accordingly in the subsequent accounting period. FRS 102, Section 32 requires disclosure of a non-adjusting event if non-disclosure would influence the decisions that users make on the basis of the financial statements. In other words, if the non-adjusting event is material.

Section 32 offers some (non-exhaustive) examples of non-adjusting events at paragraph 32.7 and 32.11 as follows:

- A decline in the market value of investments between the end of the reporting period and the date when the financial statements are authorised for issue. The decline in market value does not normally relate to the condition of the investments at the end of the reporting period, but reflects circumstances that have arisen subsequently. Therefore, an entity does not adjust the amounts recognised in its financial statements for the investments. Similarly, the entity does not update the amounts disclosed for the investments as at the end of the

reporting period, although it may need to give additional disclosure in accordance with paragraph 32.10.

- An amount that becomes receivable as a result of a favourable judgement or settlement of a court case after the reporting date but before the financial statements are authorised for issue. This would be a contingent asset at the reporting date and disclosure may be required by paragraph 21.16. However, agreement on the amount of damages for a judgement that was reached before the reporting date, but was not previously recognised because the amount could not be measured reliably, may constitute an adjusting event.
- A major business combination or disposal of a major subsidiary.
- Announcement of a plan to discontinue an operation.
- Major purchases of assets, disposals or plans to dispose of assets, or expropriation of major assets by government.
- The destruction of a major production plant by a fire.
- Announcement, or commencement of the implementation, of a major restructuring.
- Issues or repurchases of an entity's debt or equity instruments.
- Abnormally large changes in asset prices or foreign exchange rates.
- Changes in tax rates or tax laws enacted or announced that have a significant effect on current and deferred tax assets and liabilities.
- Entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees.
- Commencement of major litigation arising solely out of events that occurred after the end of the reporting period.

#### **Example – Discontinuation of a division**

Brightmall Ltd is a supermarket which operates four different classes of business division: groceries, mobile telephone providers, internet service providers and domestic appliances. Each division is considered material to the financial statements of the company. The financial statements for the year ended 31 August 2019 have not yet been approved. On 30 September 2019, the company directors decided that because of extremely difficult trading conditions, and a heavy loss, it would discontinue the domestic appliances division. This announcement was made on 1 October 2019.

This is a non-adjusting event because the decision to discontinue the division took place after the balance sheet date. However, because the division is considered to be material to the financial statements, it would need to make disclosure concerning the closure of the appliances division.

#### **Example – Share issue post year end**

Hardacre Co Limited has a year end of 31 July 2019. On 4 August 2019, it issues a further 1,000 shares in an attempt to raise finance as the company has recently been experiencing cash flow difficulties and the bank have requested shareholders make further investment to demonstrate their commitment to the company before the bank will agree to further lending.

FRS 102, paragraph 32.11 recognises issues or repurchases of an entity's debt or equity instruments as a non-adjusting event and therefore this transaction should be disclosed as such within the financial statements as a non-adjusting event.

### **1.3 Going concern**

The issue of going concern is a material one in all companies – large and small. When preparing financial statements, the company usually does so on the going concern basis. However, a company will not be able to use the going concern basis of preparing the financial statements if management determines *after* the reporting date that it either intends to cease trading or liquidate the business, or has no realistic alternative but to cease trade or liquidate (FRS 102, para 32.7A).

In situations when the directors conclude that the financial statements are not to be prepared on the going concern basis, the effect is so pervasive that there has to be a change in the basis of preparation (i.e. a basis other than the going concern basis). This alternative basis should not merely be an adjustment to the amounts recognised in the financial statements, but should be a complete change to the basis of accounting. In such a situation a basis other than the going concern basis must be used.

The 'break up' basis of accounting or 'liquidation basis' is inconsistent with FRS 102 because these bases recognise the future costs of closing the business whereas FRS 102 only permits the entity to recognise costs which it has incurred up to and including the balance sheet date. Therefore, the break up or liquidation basis would not be used if the financial statements are prepared under FRS 102, except in very rare circumstances.

If the going concern basis is not appropriate, the entity must disclose the basis on which the financial statements have been prepared together with the reason(s) why the entity is no longer a going concern.

### Example – Going concern basis is not appropriate

Cordley Co Ltd is preparing financial statements to 31 October 2019. On 4 December 2019, following negotiations, the bank have 'called in' the overdraft of £500,000 immediately to the company's ongoing trading difficulties. This has had a catastrophic effect on the company as they have failed to secure borrowing facilities with other financiers and the directors have decided that they have no realistic alternative but to cease trading with immediate effect and liquidate the company.

The going concern basis is not appropriate in this company's circumstances, and therefore the directors may make disclosures as follows (**please note the following disclosures are illustrative disclosures only and may not be appropriate in every situation**).

In the directors' report:

#### **Statement of directors' responsibilities**

The last bullet point regarding the responsibility of the directors to prepare the financial statements on a going concern basis should be amended to make it clear that, despite their responsibilities still remaining the same, the going concern basis is no longer appropriate. Such a disclosure may be as follows:

*As explained in Note X to the financial statements, the directors do not consider the going concern basis to be appropriate and these financial statements have therefore not been prepared on that basis.*

#### **Basis of preparation of the financial statements**

The basis of preparation paragraph should explain the reasons why the going concern basis is no longer appropriate in the circumstances and the effect of this approach. Such a disclosure could be as follows:

*The company has failed to reach agreement with its bankers concerning the renewal of the company's borrowing facilities. The company has ceased trading with immediate effect and therefore the financial statements have been prepared on a basis other than the going concern basis. This basis includes, where applicable, writing the company's assets down to net realisable value. Provisions have also been made in respect of contracts which have become onerous at the balance sheet date. No provision has been made for the future costs of terminating the business unless such costs were committed to at the reporting date.*

#### **Event after the reporting period (note to the financial statements)**

This would be relevant in this scenario because the event causing the going concern presumption to be departed from occurred after the year end. A disclosure example is as follows:

*As disclosed in the accounting policies note at Note X, the company ceased to trade on 4 December 2019 on the grounds that the directors have been unable to source additional finance to enable the business to continue as a going concern. The going concern basis is not appropriate and the directors have therefore not prepared the financial statements on that basis.*

#### **1.4 Dividends**

Dividends which are proposed after the balance sheet date cannot be recognised in the financial statements at the balance sheet date. This requirement also applies where the financial statements have not yet been authorised for issue. This is because at the balance sheet date, no obligation to pay the dividend exists. However, the dividends proposed may be disclosed within the financial statements and could be shown as a separate component of retained earnings at the end of the reporting period.

#### **1.5 Date of authorisation of the financial statements**

Under Section 32, the entity must disclose the date on which the financial statements were authorised for issue and who gave that authorisation. This disclosure is usually generated automatically by the accounts production software system and may look something as follows:

*The financial statements were approved by the Board of Directors on [insert date of approval] and were signed by:*

.....

*J Smith – Director*

.....

*B Jones – Director*

#### **1.6 Disclosure requirements – non-adjusting events**

As non-adjusting events require disclosure within the financial statements, an entity must disclose the following for each category of non-adjusting event(s) after the end of the reporting period:

- (a) *the nature of the event; and*
- (b) *an estimate of its financial effect or a statement that such an estimate cannot be made.*

*FRS 102 para 32.10  
(a) and (b)*