FRS 102 – Valuation issues

The adoption of FRS 102 will mean that many companies, with little previous exposure to accounting valuations, may find fair value requirements to be a significant part of their reporting procedures

What are the specific changes arising under FRS 102 giving rise to valuation requirements?

Intangible Assets

Under FRS 102 companies have the one-off option of changing the value of intangible assets to "deemed cost" at transition, meaning that it is possible to include specific items or classes of assets at either original cost or fair value at transition date. This may provide certain companies with the opportunity to increase the value of their existing intangible assets on the balance sheet.

Business Combinations

Under current UK GAAP, intangible assets arising on acquisition should be treated as goodwill unless they can be sold or transferred separately. Under FRS 102 on acquiring another business a company must now identify and recognise all of the intangible assets of the acquisition, reducing the value of goodwill and giving rise to a need to value intangible assets acquired (e.g. brand names, internally-generated software, non-contractual customer relationships, supplier agreements, patents, formulations and recipes, etc.).

Investments in Shares

Non subsidiary/associate equity share investments are now required to be included at fair value in the accounts where fair value can be reliably estimated for that investment. For companies that hold equity investments, this provides another opportunity to increase the carrying value of their balance sheets if the fair value of those investments permits.

Fair value adjustments are recognised in the income statement, giving rise to more volatile results.

Who can perform the valuations?

There are certain generally accepted approaches for the valuation of intangible assets, equity investments and other financial instruments, and familiarity with these approaches will be essential for anybody attempting to undertake these valuations. Furthermore most approaches will tend to rely heavily on market data, which is most readily available from data providers who will charge for access to this data. Therefore, while it may be possible to take it on yourself, you may find it more efficient to involve a specialist valuer.

A company's auditors are unable to perform the valuation themselves because these numbers feed into the financial statements of a company and therefore a conflict would arise in reviewing their own work.

If your accounts are audited, we would advise that you consult with your auditors in any case, despite them not being permitted to perform the valuation. Not only may they be able to refer you to competent valuers who they believe will perform a good valuation, they may also wish to discuss the valuation approach at an early stage in order to agree the reasonableness of certain approaches and parameters. This should ensure the process runs as smoothly and efficiently as possible. If your accountants do not audit your accounts, they may be able to help you directly.

What are these valuation approaches?

There is no 'one size fits all' valuation approach that is suitable for every new valuation that is required under FRS 102. In fact, even within a specific asset class (e.g. intangible assets) there are a number of different valuations which may be applicable.

For example, when valuing equity investments the relevant approach will depend upon a number of factors, such as whether the subject company is mature, whether it is generating profits, whether it is paying dividends, what sector it is in or the availability of forecasts.

How can Menzies help?

Menzies' specialist Business Valuations team has extensive knowledge and experience in the valuation of shares, derivatives and intangible assets for accounting purposes.

To discuss how the adoption of these changes might affect your company and for further information contact your relationship partner or email David Stears dstears@menzies.co.uk