

# Changes in financial reporting

## New small and micro-entity accounting standards



The FRC has published a suite of updated accounting standards that will change the face of small and micro-entity financial reporting. These new standards are applicable for periods commencing on or after 1 January 2016 and with many clients now in their transition period (or looking to early-adopt), we look at some of the key areas and implications of the new Section 1A of FRS 102 for small entities and FRS 105 for micro-entities.

### Overview of changes

Following a period of consultation, the FRC has published a number of changes to accounting standards that dovetail with recent changes to company law.

The changes outlined in this commentary are applicable for periods commencing on or after 1 January 2016 and result from FRC amendments to FRS 100 that:

- remove FRSSE 2015 and move small entities onto FRS 102
- introduce FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime.

This commentary provides an overview of the changes as applicable to small and micro-entities. Changes to company law and the practical implications of new UK GAAP transition have been discussed in previous commentaries available on our [new UK GAAP website](#).

Many of the new UK GAAP transition implications will now apply to small and micro entities. They include assessing the impact, choosing the most appropriate reporting framework, retaining transitional information and thinking about tax and, where relevant, audit consequences.

### FRS 102 section 1A – Small entities

#### Key facts

##### Amendments to FRS 102: Small entities and other minor amendments.

- Amendments mandatory for periods commencing on or after 1 January 2016.
- Early adoption available for periods commencing on or after 1 January 2015.
- Introduces a new Section 1A to FRS 102 that reduces full FRS 102 disclosures for small entities.
- Makes other consequential amendments to FRS 102 arising from changes to company law.
- Introduces new small entity transition exemptions.

### FRS 102 Section 1A - Scope

Entities that are ineligible for, or choose not to apply, the micro-entity regime, full IFRS or FRS 101 will automatically fall within the scope of FRS 102 once the FRSSE is removed.

However, small entities applying FRS 102 will be entitled to a number of financial reporting simplifications as laid out in the new Section 1A of the standard. A small entity is defined as a company that qualifies as small under sections 382 to 384 of the Companies Act 2006 (or would do had it been incorporated under company law) or an LLP qualifying as small under the LLP regulations.

The relevant size thresholds for a company, for example, would be:

Company size thresholds – 1 January 2016	
	Small
Turnover	£10.2m
Balance sheet total	£5.1m
Average employees	50

These limits would also apply where a company chooses to early adopt the amendments to FRS 102 as a condition of early adoption is that a company must apply [The Companies, Partnerships and Groups \(Accounts and Reports\) Regulations 2015 \(SI 2015/980\)](#) from the same date. If a company chooses to early adopt SI 2015/980, it must adopt the amended FRS 102 (rather than FRSSE 2015).

Entities are only permitted to early adopt the amendments to FRS 102 for periods commencing on or after 1 January 2015.

### Comment

#### Is early adoption the right option?

Entities will need to consider carefully whether early adoption of the amendments (and, where applicable, associated legislative requirements) is the right option for them. With changes to disclosures and company accounts filing requirements to consider as well, early adoption may be more attractive for some than others, for example, companies that are currently medium sized, but would be small under the new size thresholds.

## FRS 102 Section 1A – Required disclosures

An entity that is eligible for, and chooses to apply, FRS 102 Section 1A must comply with its disclosure requirements, which are generally less extensive than the full disclosure requirements in other sections of the standard. This also includes compliance with the Small Companies Regulations (or Small LLP Regulations) where they are referred to, unless those requirements are not permitted by any other statutory framework under which the entity reports.

### Accounts requirements

FRS 102 Section 1A requires that a full set of accounts contains:

- a balance sheet (statement of financial position)
- a profit and loss account (balance sheet)
- notes to the accounts (see below).

Companies, though, will still be required to address company law requirements, and hence include a directors' report in the annual report for their members.

FRS 102 Section 1A also contains four appendices that lay out various other requirements, guidance and recommendations. These are:

- Appendix A – Guidance on adapting the balance sheet formats
- Appendix B – Guidance on adapting the profit and loss formats
- Appendix C – Disclosure requirements for small entities
- Appendix D – Additional disclosures encouraged for small entities.

Appendices A and B address considerations such as the interaction of true and fair requirements and the option to prepare abridged accounts as well as the application of increased primary statement presentation flexibility under the amended company law (SI 2015/980).

Appendix C moves on to specify the mandatory disclosure requirements for small entities which are based on the requirements from the updated company law. This appendix also cross refers into other sections of FRS 102 where similar requirements are addressed.

These disclosure requirements are summarised in the comment box to the right.

### Encouraged disclosures

Whilst some disclosures, as noted above, are absolutely required (unless immaterial), FRS 100, FRS 102 Section 1A and its Appendix D make numerous references to the requirement to show a true and fair view. In this context, the standard also encourages:



## Comment



### What does Appendix C to Section 1A require?

Appendix C of FRS 102 Section 1A requires small entities to make disclosures in the following areas:

- Accounting policies
- Changes in presentation and accounting policies and correction of prior period errors
- True and fair override
- Assets or liabilities relating to more than one item in the balance sheet
- Fixed assets movements
- Revalued fixed assets
- Capitalisation of borrowing costs
- Impairment of assets
- Financial instruments and other assets measured at fair value through profit or loss
- Indebtedness, guarantees and financial commitments
- Income or expenses of exceptional size or incidence
- Average number of employees
- Related party transactions and advances, credits and guarantees to directors
- Other (including entity information, combined items and post balance sheet events).

Whilst a number of the disclosure requirements are similar to those required under the full FRS 102, they generally require less detail. For example, related party transaction disclosures under Section 1A are only required for material transactions that have not been concluded under normal market conditions with directors, owners with a participating interest and companies in which the entity has a participating interest.

However, when combined with updated company law filing requirements (including the removal of the option to file abbreviated accounts), information in the public domain may increase for some companies.

- a statement of compliance with Section 1A of FRS 102 including, where applicable, that the July 2015 amendments were applied before 1 January 2016
- presentation of a statement of comprehensive income where gains or losses are recognised in other comprehensive income
- presentation of a statement of comprehensive income or a statement of income and retained earnings where there are transactions with equity holders
- certain disclosures (FRS 102.9.23) relating to consolidation where a parent entity voluntarily prepares consolidated accounts

- a statement that the entity is a public benefit entity (as applicable)
- disclosure of going concern material uncertainties or, where applicable, that accounts not prepared on a going concern basis and why
- dividends paid or payable in the period
- first-time adoption reconciliations and descriptions of how transition has affected the entity's financial performance and position
- consideration and provision of any other disclosures within Sections 3 and 8 to 35 of FRS 102 that are relevant to material transactions, other events or conditions.

## Comment



### How do you present a true and fair view?

One of the more difficult areas within FRS 102 Section 1A will be the judgement required in determining how to apply the disclosures that are 'encouraged' by the FRC.

As a result of the restrictions in the EU Accounting Directive (of which SI 2015/980, and hence FRS 102 Section 1A are derivatives), the FRC were unable to mandate additional requirements. However, by specifying additional encouraged items as well as very widely scoped encouraged disclosures (eg. the final bullet point above), the FRC may be setting the bar high for some smaller entities.

For companies, the directors will need to assess the level of disclosure required to present a true and fair view. However, their view may also be swayed by the potential implications of more of the information being filed at the registrar due to the removal of the option to file true abbreviated accounts and this information being available to anyone, for free, from Companies House.

## FRS 102 Section 1A – Recognition and measurement

Whilst small entities benefit from reduced mandatory disclosures when compared to a full FRS 102 adopter, the recognition and measurement requirements of the rest of the standard still apply.

As such, there can be an increased prominence of fair value accounting, greater volatility of profits and losses, increased instances of deferred tax, removal of the use of contract rate accounting for foreign currency transactions, more financial instruments appearing on balance sheet and some financial instruments (eg. below market rate transactions) being held at different values.



As noted earlier, the practical impact of these recognition and measurement changes are similar to those outlined in our earlier commentaries available on our [new UK GAAP website](#). In some cases the impact would be more pronounced as exemptions previously used under the FRSSE will no longer be available.

### Small entity transition exemptions

For areas affected by the recognition and measurement requirements of FRS 102, the standard position is to process adjustments at the date of transition and apply FRS 102 from there on in.

However, as with non-small adopters, section 35 of FRS 102 offers numerous exemptions on transition that may be taken. Small entities are also entitled to additional exemptions that apply not at the date of transition, but at the start of the 'current' year in those first FRS 102 financial statements. These include:

- the ability to avoid accounting for share based payments regarding equity instruments issued on/before the comparative date
- the ability to process the fair values of financial instruments as at the current period start date, rather than using transition date values, as an adjustment to the current period opening equity
- the ability to use assumptions and process changes to the treatment of financing transactions involving related parties at the current period start date as an adjustment to the current period opening equity.

These exemptions appear to be a pragmatic solution to problems that arise where many small entities have already passed their FRS 102 transition date.

## Comment



### How do small entity transition exemptions work?

Let's assume a small company with a 31 December 2016 year end is preparing its first set of accounts under FRS 102 Section 1A.

The date of transition for this company is 1 January 2015 (which has already passed). Where taking advantage of the additional transition exemptions for small entities it is not required to, for example, restate for the fair value of financial instruments or adjust the treatment of financing transactions involving related parties at 1 January 2015.

It is, however, required to introduce the 1 January 2016 value of the instrument into the accounts in the year to 31 December 2016 as an adjustment to the opening equity position.

As such, this company will still need information in these areas as at 1 January 2016.

# FRS 105 – Micro-entities

## Key facts

### FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime.

- New standard applicable to micro-entities for periods commencing on or after 1 January 2016.
- Early adoption available.
- Introduces simplified recognition and measurement requirements.
- Replaces the FRSSE regime as applicable to micro-entities.
- Transposes simplified financial statements formats from company law.

## FRS 105 - Scope and effective date

In 2014, the FRSSE was updated for legislation that permitted qualifying micro-entity companies to prepare and present simplified financial statements. Whilst FRS 105 is effectively a replacement for the FRSSE for these micro-entity companies, it can be early adopted straight away.

### Micro-entity company size thresholds

	Micro
Turnover	£632k
Balance sheet total	£316k
Average employees	10

FRS 105 only includes within its scope companies that qualify as a micro-entity in law.

## Recognition and measurement simplification

As noted above, from 2016 a small company must apply the recognition and measurement requirements of FRS 102. If a company qualifies as a micro-entity it may instead choose to apply the micro-entities' regime, including the new FRS 105. Key accounting simplifications incorporated in FRS 105 are highlighted below.

Micro-entities cannot, by law, adopt the fair value or alternative accounting rules. This leads to a number of simplifications in FRS 105 that echo those seen when FRSSE was amended to accommodate micro-entities. These include:

- no revaluation of tangible fixed assets or investment properties being permitted
- simplified accounting for financial instruments such as current asset investments.

Whilst the lack of fair value accounting has little practical effect for most micro-entity companies currently, in a world where the alternative is FRS 102 the effect is more marked. The FRC have also included a number of other simplifications when compared to FRS 102 (and the FRSSE in some areas). These simplifications

are wide ranging, and include:

- prohibition of accounting for deferred tax
- prohibition of accounting for share based payments prior to the issue of the shares
- simplification of defined benefit pension plan accounting requirements
- requirement to use contracted rates to translate foreign currency denominated assets and liabilities where a forward contract exists
- no option to capitalise borrowing or development costs
- mandating the accrual model of accounting for government grants
- simplification of accounting for financial instruments including accounting for interest, transaction costs and non-market rate lending arrangements.

## Comment



### Will FRS 105 kick-start the micros' regime?

With micro-entity company requirements already embedded in law, early adoption of FRS 105 may prove popular due to the simplification in recognition and measurement requirements, even when compared to the requirements of the current FRSSE.

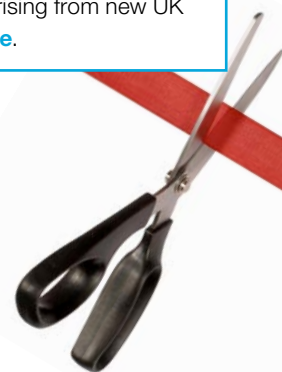
When compared to an eventual move to FRS 102 with its tricky areas of accounting, the FRC have offered micro-entity companies a viable and cost-effective reporting route going forward.

With the practicalities of unwinding historical transactions, the potential implications on distributable profits, judgement as to what a client needs and wants to show in the accounts, and what will happen when they grow too big for FRS 105 and into FRS 102 Section 1A; there is certainly much to consider when assessing the best financial reporting framework fit for respective clients.

For further information you may be interested in our webinars: [Life after FRSSE](#) or [The Micro Maze - Micro entities under FRS105](#), available in September.

We will be updating the disclosure checklists and example accounts in our [Audit Manual](#), [Audit Exemption](#), [Assurance and other affected Specialist Assignment manuals](#) ready for early adopters of the new and updated accounting standards.

For more information on the changes arising from new UK GAAP, see our [new UK GAAP website](#).







Wilmington Finance

# New UK GAAP Transition Library

To help you and your entire team get ready to implement New UK GAAP we have developed a library of **31 easy reference FRS 102 e-learning modules**.

**Definition**  
property... held to earn rentals or for capital appreciation (or for both)...

**Comparison between current and new UK GAAP**

**Current UK GAAP**  
SSAP 19 explicitly states that the following are not investment properties:  
(a) A property which is owned and occupied by a company for its own purposes is not an investment property.  
(b) A property let to and occupied by another group company is not an investment property for the purposes of the group accounts

**FRS 102**  
FRS 102 requires that mixed use property shall be separated between investment property and property, plant and equipment unless the fair value of the investment property component cannot be measured reliably (without undue cost or effort). If it cannot be measured reliably then it shall be accounted for as property, plant and equipment (16.4).  
FRS 102 does not exclude properties which are let to and occupied by group companies. These would be recognised as investment properties in individual financial statements.

**Background**

**Practical examples**

**Test me**

**Investment Properties**  
An overview of section 16 of FRS 102

**Case study 1: Mauve Ltd**  
Mauve Ltd has a year end of 30 June and its first set of FRS 102 accounts will be to 30 June 2016 with a transition date of 1 July 2014. On transition, the carrying amount of the entity's investment property was £1.2m (being its open market valuation under SSAP 19). This is also considered to be its fair value under FRS 102. It had an original cost of £900k.  
At 30 June 2015, a further valuation was obtained and this amounted to £1.4m and by 30 June 2016 it stood at a fair value of £1.5m. Assume that the deferred tax liability relating to this property amounts to £60k at transition, £100k at June 2015 and £120k at June 2016.  
How are these entries reflected in the 2016 accounts?

FRS 102 June 2016	£'000	£'000
Dr investment property	100	
Dr tax charge	20	

**Frequently asked questions**  
Hi I'm Amy and I'm here to answer your questions. Click on each question below to see the answer.  
What about transition?  
If applying the fair value model, does the fair value need to be determined by an external valuer? What about a professionally qualified valuer?  
We used to include a true and fair override disclosure for investment properties. Is this still needed?

**FAQs**

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