



MICRO-ENTITIES' ACCOUNTS

The Financial Reporting Faculty updates you on the micro-entities regime and the new financial reporting standard FRS 105.

In November 2013, the UK Government approved regulations that introduced a simpler reporting regime for micro-entities (the 'micro-entities regime'). In July 2015, the Financial Reporting Council (FRC) published a new standard, FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* for use by those micro-entities choosing to adopt this simpler regime. These FAQs have been updated to reflect the fact that in 2016 the micro-entities regime was extended to Limited Liability Partnerships (LLPs) and Qualifying Partnerships.

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1. What are the micro-entity regulations?

[The Small Companies \(Micro-Entities' Accounts\) Regulations 2013](#) (the 'regulations') became effective for financial years ending on or after 30 September 2013, introducing a simpler reporting regime for a new sub-category of small company: the micro-entity.

In May 2016, the UK Government approved [The Limited Liability Partnerships, Partnerships and Groups \(Accounts and Audit\) Regulations 2016](#) (the 'revised LLP regulations'), extending the micro-entities regime for LLPs and Qualifying Partnerships. The revised LLP regulations are effective for accounting periods beginning on or after 1 January 2016, with early adoption generally permitted for accounting periods beginning on or after 1 January 2015.

2. Is qualifying as a micro-entity all about being a very small entity?

No, there is more to qualifying as a micro-entity than being very small. Aside from the size criteria (FAQ 5), a number of entities are specifically excluded from the micro-entities regime (FAQ 3). There are also special considerations for entities which form part of a group (FAQ 4).

3. Which entities are excluded from being treated as micro-entities?

Unsurprisingly, an entity that is excluded from the small companies regime¹ cannot qualify as a micro-entity. However, the micro-entities regime goes further by excluding additional types of entity, most notably charities².

Other entities excluded from the micro-entities regime include investment undertakings, financial holding and insurance undertakings, credit institutions, overseas companies, unregistered companies and companies authorised to register pursuant to s1040 of the Companies Act 2006.

4. What are the special considerations for companies which form part of a group?

A subsidiary included in consolidated group accounts by the method of full (as opposed to proportional) consolidation cannot qualify as a micro-entity.

A parent entity can only qualify as a micro-entity for the purposes of its individual accounts if it qualifies as a micro-entity individually and the group headed by it qualifies as small. Also, a parent entity that prepares group accounts cannot qualify as a micro-entity for the purposes of its individual accounts.

5. What are the size criteria for a micro-entity?

An entity meets the qualifying conditions if it meets at least two out of three of the following thresholds:

Turnover:	Not more than £632,000
Balance sheet total:	Not more than £316,000
Average number of employees:	Not more than 10

The turnover limit is adjusted proportionately if the financial year is longer or shorter than twelve months. The rules for qualifying in the first and subsequent financial year are the same as those under the small companies regime.

¹ Unless otherwise stated, references to the small companies regime in this document also relate to the small LLPs regime.

² This does not include Community Interest Companies (CICs).

6. My organisation qualifies as a micro-entity. Is it required to adopt the micro-entities regime?

No, the regime is **optional** for eligible entities. A micro-entity may therefore choose to prepare accounts under a financial reporting regime applicable to larger sized entities.

The decision to apply the micro-entity exemptions will depend on the individual circumstances of the reporting entity. For example, current and potential creditors and lenders to a business may require more information than micro-entity accounts provide. On the other hand, a micro-entity with an investment property and little or no borrowings may be attracted by the fact that, under the micro-entities regime, investment properties will not need to be revalued each year (FAQ 7).

Entities should consider carefully the various implications before deciding whether or not to take advantage of the micro-entity exemptions.

7. What are the main features of the micro-entities regime?

- A simpler balance sheet and profit and loss account. There are two formats for the balance sheet and one format for the profit and loss account.
- A micro-entity is not required to prepare a directors' report³.
- No notes to the accounts are required. Instead, where applicable, details of any advances, credit and guarantees with directors (companies only), and details of any financial commitments, guarantees and contingencies should be disclosed at the foot of the balance sheet. This reduced information is referred to as the 'minimum accounting items'.
- If a micro-entity chooses to disclose information in addition to the minimum accounting items it must, in respect of that item, follow the disclosure requirements of the relevant accounting standard (FAQ 8).
- The fair value accounting and alternative accounting rules cannot be applied in micro-entity accounts. This means that no revaluations or subsequent measurement at fair value is permitted under the micro-entities regime. For example, a micro-entity with an investment property, choosing to adopt the micro-entities regime, would be required to measure the property at cost and not fair value.
- Accounts prepared in accordance with the regulations are presumed by law to give a true and fair view.
- Only the balance sheet, including the information disclosed at the foot, needs to be filed at Companies House. It is not necessary to file the profit and loss account, or where relevant (see footnote 3), the directors' report.

8. Which accounting standard is applicable to reporting entities adopting the micro-entities regime?

The FRSSE was amended in 2014 to enable companies adopting the micro-entity exemptions to continue to prepare accounts that are in compliance with the FRSSE.

³ This exemption was introduced as part of the recent changes to UK company law arising from the new EU Accounting Directive. It is therefore only available for accounting periods beginning on or after 1 January 2016, although it can be early adopted for accounting periods beginning on or after 1 January 2015 provided that all other relevant changes to UK company law are also adopted from the same date.

The FRSSE is withdrawn for accounting periods beginning on or after 1 January 2016 and the FRC has issued a new standard, FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*. FRS 105 is applicable to entities that meet the definition of a micro-entity and choose to apply the micro-entities regime. It comes into effect for accounting periods beginning on or after 1 January 2016, with early adoption permitted.

In May 2016, the FRC issued [amendments](#) to FRS 105 to reflect the fact that eligible Qualifying Partnerships and LLPs are now permitted by law to apply the micro-entities regime (FAQ 1). These amendments to FRS 105 are effective for accounting periods beginning on or after 1 January 2016, with early adoption permitted for accounting periods beginning on or after 1 January 2015. This means that an eligible Qualifying Partnership or LLP choosing to apply the micro-entities regime will be required to apply FRS 105. Any Qualifying Partnership or LLP choosing to early adopt the micro-entities regime for an accounting period beginning on or after 1 January 2015, must apply FRS 105 from the same date, and vice versa.

At the time of updating these FAQs, work was also underway to update the LLP SORP to reflect the revised LLP regulations.

9. Can unincorporated businesses apply FRS 105?

The FRC has not explicitly permitted or prohibited use of FRS 105 by unincorporated businesses or individuals (which, if set up as companies, would be eligible for the micro-entities regime) for the purpose of calculating trading profits for submission to the tax authorities. Instead, the FRC note that this is a matter for the tax authorities.

HMRC has confirmed to ICAEW that it will accept calculations of trading profits for income tax purposes prepared under FRS 105 if the size criteria have been met.

10. What are the requirements of FRS 105?

FRS 105 is based on FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, although it has been adapted significantly to accommodate the legal requirements of the micro-entities regime (see FAQ 7). In addition, further simplifications, over and above those required by law, have been made in order to reflect the smaller size and simpler nature of micro-entities.

Micro-entities will need to consider carefully the requirements of FRS 105, including any relevant exemptions or exemptions available on transition (FAQ 11).

Key simplifications include:

- No accounting policy options are available. Borrowing costs and development costs must be expensed to the profit and loss account in the period in which they are incurred, and government grants must be recognised on the accruals basis.
- No accounting for deferred tax or equity-settled share-based payments prior to the issue of the shares.
- Further simplifications to the recognition and measurement requirements, including the accounting for post-employment benefit plans, financial instruments, and foreign currency transactions.

These additional simplifications mean that, in many respects, the recognition and measurement requirements of FRS 105 do not differ significantly from the FRSSE 2015.

However, there are some important differences, in particular the prohibition of deferred tax. The overall impact of taking advantage of the exemptions will depend very much on the individual circumstances of the reporting entity.

11. Will FRS 105 need to be applied retrospectively?

Yes. When preparing the first set of FRS 105 financial statements, the comparative balance sheet and profit and loss account will need to be restated, and an opening balance sheet at the date of transition prepared in accordance with FRS 105 (although this balance sheet will not need to be presented). There are some limited exceptions from retrospective application and some exemptions, which can be selected on an individual basis. These exemptions are designed to make the transition to FRS 105 easier, so should be considered sooner rather than later.

12. How do micro-entity accounts compare to those prepared under the small companies regime?

The amount of information included in the micro-entity accounts is significantly less than that included in small company accounts. There is also less flexibility. For example, the line items within the profit and loss account cannot be combined or renamed, whereas they can under the small companies regime. However, a line item should not be included in the accounts when there is nothing to include for that item in both the current and comparative periods.

In addition, micro-entities are not be permitted to take advantage of the recent amendment to UK law (effective from 1 January 2016) which allows companies (and LLPs), in certain circumstances, to adapt their balance sheet and profit and loss account formats in order to adopt an IFRS layout and IFRS terminology.

13. How do I show that the accounts have been prepared in accordance with the micro-entities regime?

There should be a statement on the balance sheet, in a prominent place above the signature, to the effect that the accounts have been prepared in accordance with the micro-entity provisions.

14. Are there any special considerations that auditors should be aware of?

In practice, it is unlikely that many micro-entities will choose to have an audit. However, should this situation arise, there are special considerations for auditors set out in the regulations.

ICAEW members may wish to consider contacting the ICAEW Technical Enquiry Service on +44(0)1908 248 250 should they encounter any technical and/or ethical issues regarding acceptance of a micro-entity engagement.

15. Will HMRC accept micro-entity accounts as part of a company's annual self assessment?

Yes, micro-entity accounts prepared in accordance with the micro-entities regime will represent accounts prepared under GAAP and therefore can be submitted, along with the directors' report (where applicable), to HMRC as part of a company's annual self-assessment.

There is no change in the requirement to keep and retain adequate business and accounting records.

16. Where can I get further information about the micro-entities regime?

Further information on FRS 105 can be found on the financial reporting technical pages on the ICAEW [website](#). The Financial Reporting Faculty will continue to keep under review the need for more guidance for ICAEW members.

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Chartered Accountants' Hall
Moorgate Place, London
icaew.com

T +44 (0) 20 7920 8100
F +44 (0) 20 7920 8533
E frfac@icaew.com

TECPLN12570