



March 2018

FRS 105

The Financial Reporting Standard applicable to the Micro-entities Regime

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March 2018

FRS 105

The Financial Reporting Standard applicable to the Micro-entities Regime

FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* is an accounting standard. It is issued by the Financial Reporting Council, as a prescribed body, in respect of its application in the United Kingdom and the Republic of Ireland.

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Overview

- (i) The FRC's overriding objective in setting accounting standards is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.

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

- (ii) FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* is an accounting standard designed to apply to the financial statements of companies, LLPs and qualifying partnerships that qualify for, and choose to apply, the micro-entities regime.
- (iii) FRS 105 is based on FRS 102, but its accounting requirements are adapted to satisfy the legal requirements applicable to micro-entities and to reflect the simpler nature and smaller size of micro-entities.
- (iv) The application of the micro-entities regime is optional; however, a micro-entity that chooses to prepare its financial statements in accordance with the micro-entities regime is required to apply FRS 105. A company that qualifies for this regime, but chooses not to apply it, is required to apply another accounting standard. The possible options are set out in FRS 100 *Application of Financial Reporting Requirements*.

Organisation of FRS 105

- (v) FRS 105 is organised by topic with each topic presented in a separate numbered section.
- (vi) Terms defined in the glossary are in **bold type** the first time they appear in each section.
- (vii) This edition of FRS 105 issued in March 2018 updates the edition of FRS 105 issued in July 2015 for the following:
 - (a) *Amendments to FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – Limited Liability Partnerships and Qualifying Partnerships* issued in May 2016;
 - (b) *Triennial review 2017 amendments* issued in December 2017; and
 - (c) some minor typographical or presentational corrections.

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

Section 1

Scope

Scope of this Financial Reporting Standard

- 1.1 This FRS applies to the **financial statements** of a **micro-entity**. The financial statements of a micro-entity prepared in accordance with this FRS that include the **micro-entity minimum accounting items** are presumed in law to show a true and fair view of the micro-entity's **financial position** and **profit or loss** in accordance with the **micro-entities regime**.
- 1.2 References to a micro-entity in this FRS are to a micro-entity that chooses to apply the micro-entities regime.
- 1.3 This FRS permits, but does not require, a micro-entity to include information additional to the micro-entity minimum accounting items in its financial statements. If a micro-entity includes additional information it shall have regard to any requirement of Section 1A *Small Entities* of **FRS 102** that relates to that information.

Date from which effective

- 1.4 A micro-entity applying the micro-entities regime in the UK shall apply this FRS for accounting periods beginning on or after 1 January 2016. Early application is permitted.
- 1.4A A micro-entity applying the micro-entities regime in the Republic of Ireland shall apply this FRS for accounting periods beginning on or after 1 January 2017. Early application is permitted provided the *Companies (Accounting) Act 2017* is applied from the same date.
- 1.5 In May 2016 amendments were made to this FRS to extend its scope to include **limited liability partnerships (LLPs)** and **qualifying partnerships** following a change in UK legislation. An LLP or a qualifying partnership which qualifies as a micro-entity in the UK and is applying the micro-entities regime shall apply this FRS for accounting periods beginning on or after 1 January 2016. Early application by a micro-entity that is an LLP or a qualifying partnership is:
- (a) permitted for accounting periods beginning on or after 1 January 2015 provided that *The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016* (SI 2016/575) are applied from the same date; and
 - (b) required if the LLP or qualifying partnership applies *The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016* (SI 2016/575) to an accounting period beginning before 1 January 2016.
- 1.6 In December 2017 amendments were made to this FRS as a result of the triennial review 2017.
- (a) A micro-entity in the UK shall apply the amendments to this FRS as set out in the *Triennial review 2017 amendments* for accounting periods beginning on or after 1 January 2019, except for the amendments to paragraph 3.13A and Section 6 *Notes to the Financial Statements* (including its appendices) which shall apply for accounting periods beginning on or after 1 January 2017¹.

Early application is permitted provided that all the amendments to this FRS are applied at the same time.

¹ These reflect legal requirements that are applicable in the UK for accounting periods beginning on or after 1 January 2016.

- (b) A micro-entity in the Republic of Ireland shall apply the amendments to this FRS that incorporate the micro-entities regime in the Republic of Ireland in accordance with paragraph 1.4A, and shall apply the other amendments set out in the *Triennial review 2017 amendments* for accounting periods beginning on or after 1 January 2019.

Early application of the other amendments is permitted provided that all of these other amendments are applied at the same time.

Section 2

Concepts and Pervasive Principles

Scope of this section

- 2.1 This section sets out the concepts and basic principles that generally underlie the **recognition** and **measurement** of transactions of **micro-entities** within the scope of this FRS.

Financial position

- 2.2 The **financial position** of a micro-entity is the relationship of its **assets**, **liabilities** and **equity** as of a specific date as presented in the **statement of financial position**. These are defined as follows:
- (a) An asset is a resource controlled by the micro-entity as a result of past events and from which future economic benefits are expected to flow to the micro-entity.
 - (b) A liability is a present obligation of the micro-entity arising from past events, the settlement of which is expected to result in an outflow from the micro-entity of resources embodying economic benefits.
 - (c) Equity is the residual interest in the assets of the micro-entity after deducting all its liabilities.
- 2.3 Some items that meet the definition of an asset or a liability may not be recognised as assets or liabilities in the statement of financial position because they do not satisfy the criteria for recognition in paragraphs 2.22 and 2.24. In particular, the expectation that future economic benefits will flow to or from a micro-entity must be sufficiently certain to meet the probability criterion before an asset or liability is recognised.

Assets

- 2.4 The future economic benefit of an asset is its potential to contribute, directly or indirectly, to the flow of cash to the micro-entity. Those cash flows may come from using the asset or from disposing of it.
- 2.5 Many assets, for example **property, plant and equipment**, have a physical form. However, physical form is not essential to the existence of an asset. Some assets are intangible.
- 2.6 In determining the existence of an asset, the right of ownership is not essential. Thus, for example, property held on a **lease** is an asset if the micro-entity controls the benefits that are expected to flow from the property.

Liabilities

- 2.7 An essential characteristic of a liability is that the micro-entity has a present obligation to act or perform in a particular way. The obligation may be either a legal obligation or a **constructive obligation**. A legal obligation is legally enforceable as a consequence of a binding contract or statutory requirement. A constructive obligation is an obligation that derives from a micro-entity's actions when:
- (a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the micro-entity has indicated to other parties that it will accept certain responsibilities; and

- (b) as a result, the micro-entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.
- 2.8 The settlement of a present obligation usually involves the payment of cash, transfer of other assets, provision of services, the replacement of that obligation with another obligation, or conversion of the obligation to equity. An obligation may also be extinguished by other means, such as a creditor waiving or forfeiting its rights.

Equity

- 2.9 Equity is the residual interest in the assets of the micro-entity after deducting all its liabilities.

Performance

- 2.10 **Performance** is the relationship of the **income** and **expenses** of a micro-entity during a **reporting period**. Income and expenses are defined as follows:
- (a) Income is increases in economic benefits during the reporting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity investors.
 - (b) Expenses are decreases in economic benefits during the reporting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity investors.
- 2.11 The recognition of income and expenses results directly from the recognition and measurement of assets and liabilities. Criteria for the recognition of income and expenses are discussed in paragraphs 2.26 and 2.27.

Income

- 2.12 The definition of income encompasses both **revenue** and **gains**.
- (a) Revenue is income that arises in the course of the ordinary activities of a micro-entity and is referred to by a variety of names including sales, fees, interest, dividends, royalties and rent.
 - (b) Gains are other items that meet the definition of income but are not revenue.

Expenses

- 2.13 The definition of expenses encompasses losses as well as those expenses that arise in the course of the ordinary activities of the micro-entity.
- (a) Expenses that arise in the course of the ordinary activities of the micro-entity include, for example, cost of sales, wages and **depreciation**. They usually take the form of an outflow or depletion of assets such as cash, **inventory**, or property, plant and equipment.
 - (b) Losses are other items that meet the definition of expenses and may arise in the course of the ordinary activities of the micro-entity.

Recognition of assets, liabilities, income and expenses

- 2.14 Recognition is the process of incorporating in the statement of financial position or **income statement** an item that meets the definition of an asset, liability, equity, income or expense and satisfies the following criteria:
- (a) it is **probable** that any future economic benefit associated with the item will flow to or from the micro-entity; and
 - (b) the item has a cost or value that can be measured reliably.
- 2.15 The uncertainties that inevitably surround many events and circumstances are acknowledged by the exercise of **prudence** in the preparation of the **financial statements**. Prudence is the inclusion of a degree of caution in the exercise of the judgements needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated. However, the exercise of prudence does not allow the deliberate understatement of assets or income, or the deliberate overstatement of liabilities or expenses. In short, prudence does not permit bias.

The probability of future economic benefit

- 2.16 The concept of probability is used in the first recognition criterion to refer to the degree of uncertainty that the future economic benefits associated with the item will flow to or from the micro-entity. Assessments of the degree of uncertainty attaching to the flow of future economic benefits are made on the basis of the evidence relating to conditions at the end of the reporting period available when the financial statements are prepared. Those assessments are made individually for individually significant items, and for a group for a large population of individually insignificant items.

Reliability of measurement

- 2.17 The second criterion for the recognition of an item is that it possesses a cost or value that can be measured with reliability. In many cases, the cost or value of an item is known. In other cases it must be estimated. The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability. When a reasonable estimate cannot be made, the item is not recognised in the financial statements.
- 2.18 An item that fails to meet the recognition criteria may qualify for recognition at a later date as a result of subsequent circumstances or events.

Measurement of assets, liabilities, income and expenses

- 2.19 Measurement is the process of determining the monetary amounts at which a micro-entity measures assets, liabilities, income and expenses in its financial statements. Measurement involves the selection of a basis of measurement. This FRS specifies which measurement basis a micro-entity shall use for many types of assets, liabilities, income and expenses.

Pervasive recognition and measurement principles

- 2.20 In the absence of a requirement in this FRS that applies specifically to a transaction or other event or condition, paragraph 8.4 provides guidance for making a judgement and paragraph 8.5 requires a micro-entity to look to the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses and the pervasive principles set out in this section.

Accrual basis

- 2.21 A micro-entity shall prepare its financial statements using the **accrual basis** of accounting. On the accrual basis, items are recognised as assets, liabilities, equity, income or expenses when they satisfy the definitions and recognition criteria for those items.

Recognition in financial statements

Assets

- 2.22 A micro-entity shall recognise an asset in the statement of financial position when it is probable that the future economic benefits will flow to the micro-entity and the asset has a cost or value that can be measured reliably. An asset is not recognised in the statement of financial position when expenditure has been incurred for which it is considered not probable that economic benefits will flow to the micro-entity beyond the current reporting period. Instead such a transaction results in the recognition of an expense in the income statement.
- 2.23 A micro-entity shall not recognise a **contingent asset** as an asset. When the flow of future economic benefits to the micro-entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Liabilities

- 2.24 A micro-entity shall recognise a liability in the statement of financial position when:
- (a) the micro-entity has an obligation at the end of the reporting period as a result of a past event;
 - (b) it is probable that the micro-entity will be required to transfer resources embodying economic benefits in settlement; and
 - (c) the settlement amount can be measured reliably.
- 2.25 A **contingent liability** is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 2.24.

Income

- 2.26 The recognition of income results directly from the recognition and measurement of assets and liabilities. A micro-entity shall recognise income in the income statement when an increase in future economic benefits related to an increase in an asset or a decrease of a liability has arisen that can be measured reliably.

Expenses

- 2.27 The recognition of expenses results directly from the recognition and measurement of assets and liabilities. A micro-entity shall recognise expenses in the income statement when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably.

Profit or loss

- 2.28 **Profit or loss** is the arithmetical difference between income and expenses. It is not a separate element of financial statements, and a separate recognition principle is not needed for it.

- 2.29 Generally this FRS does not allow the recognition of items in the statement of financial position that do not meet the definition of assets or of liabilities regardless of whether they result from applying the notion commonly referred to as the 'matching concept' for measuring profit or loss.

Measurement at initial recognition

- 2.30 At initial recognition, a micro-entity shall measure assets and liabilities at cost.
- 2.31 Under limited circumstances this FRS requires a micro-entity to estimate the cost of an asset or liability based on its **fair value**. Where this FRS requires a micro-entity to determine the fair value of an asset or liability, it shall use the following methodology to estimate the fair value:
- (a) The best evidence of fair value is the open market price for an identical asset or liability (or similar asset or liability) in an **active market**.
 - (b) When an open market price is not available, the price of a recent transaction for an identical asset or liability (or similar asset or liability) in an arm's length transaction between knowledgeable, willing parties provides evidence of fair value. However, this price may not be a good estimate of fair value if there has been a significant change in economic circumstances or a significant period of time between the date of the binding sale agreement or the transaction, and the measurement date.
 - (c) If neither (a) nor (b) above are available, the fair value shall be estimated using another valuation technique. The objective of using a valuation technique is to estimate what the price of a recent transaction for an identical asset or liability (or similar asset or liability) would have been on the measurement date in an arm's length exchange motivated by normal business considerations.

Subsequent measurement

Financial assets and financial liabilities

- 2.32 A micro-entity measures **financial assets** and **financial liabilities** as follows:
- (a) Investments in preference shares or **ordinary shares** and investments in **subsidiaries** and **associates** and interests in **jointly controlled entities** shall be measured at cost less impairment.
 - (b) **Derivatives** are measured at cost adjusted for amounts recognised in profit or loss over the term of the instruments and any **impairment loss**.
 - (c) **Financial instruments** other than financial instruments covered by paragraphs (a) and (b) are measured at cost adjusted for the allocation of interest, the amortisation of any **transaction costs** included in the cost of the instruments and any impairment loss.

Non-financial assets

- 2.33 Property, plant and equipment, **investment property** and **biological assets** are measured at cost less accumulated depreciation and accumulated impairment losses.
- 2.34 Inventories are measured at the lower of cost and selling price less costs to complete and sell.
- 2.35 Measurement of assets at amounts lower than their initial historical cost is intended to ensure that an asset is not measured at an amount greater than the micro-entity expects to recover from the sale or use of that asset.

Liabilities other than financial liabilities

- 2.36 Most liabilities other than financial liabilities are measured at the best estimate of the amount that would be required to settle the obligation at the **reporting date**.

Offsetting

- 2.37 A micro-entity shall not offset assets and liabilities, or income and expenses, unless required or permitted by this FRS.
- (a) Measuring assets net of valuation allowances (for example, allowances for inventory obsolescence and allowances for uncollectible receivables) is not offsetting.
 - (b) If a micro-entity's normal **operating activities** do not include buying and selling **fixed assets**, including investments and operating assets, then the micro-entity reports gains and losses on disposal of such assets by deducting from the proceeds on disposal the **carrying amount** of the asset and related selling expenses.

Disclosures

- 2.38 An Irish micro-entity shall disclose information in relation to assets or income set off against amounts in respect of items representing liabilities or expenditure or vice versa in accordance with Appendix B to Section 6 *Notes to the Financial Statements*.

Section 3

Financial Statement Presentation

Scope of this section

- 3.1 This section sets out what compliance with this FRS requires and what makes up a complete set of **financial statements** for a **micro-entity**.

Presumed true and fair view

- 3.2 The financial statements of a micro-entity that comply with this FRS are presumed in law to give a true and fair view of the **financial position** and **profit or loss** of the micro-entity in accordance with the **micro-entities regime**.

Going concern

- 3.3 When preparing financial statements using this FRS, the management of a micro-entity shall make an assessment of whether the going concern basis of accounting is appropriate. The going concern basis of accounting is appropriate unless management either intends to liquidate the micro-entity or to cease trading, or has no realistic alternative but to do so. In assessing whether the going concern basis of accounting is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, 12 months from the date when the financial statements are authorised for issue.

Frequency of reporting

- 3.4 A micro-entity shall present a complete set of financial statements (including comparative information as set out in paragraph 3.7) at the end of each **reporting period**.

Consistency of presentation

- 3.5 A micro-entity shall retain the presentation and classification of items in the financial statements from one period to the next unless:
- (a) it is apparent, following a significant change in the nature of the micro-entity's operations or a review of its financial statements, that another presentation or classification would be more appropriate having regard to the criteria for the selection and application of **accounting policies** in Section 8 *Accounting Policies, Estimates and Errors*; or
 - (b) this FRS requires a change in presentation.
- 3.6 When the presentation or classification of items in the financial statements is changed, a micro-entity shall reclassify comparative amounts unless the reclassification is **impracticable**.

Comparative information

- 3.7 Except when this FRS permits or requires otherwise, a micro-entity shall present comparative information in respect of the preceding period for all amounts presented in the current period's financial statements.

Materiality

- 3.8 This FRS specifies information that is required to be included in the financial statements of a micro-entity, which includes the **notes**. A micro-entity need not provide a specific disclosure required by this FRS if the information resulting from that disclosure is not **material**, except when required by the Act² regardless of materiality.

Complete set of financial statements

- 3.9 A complete set of financial statements of a micro-entity shall include the following:
- (a) a **statement of financial position** as at the **reporting date** with notes included at the foot of the statement³; and
 - (b) an **income statement** for the reporting period.
- 3.10 Because paragraph 3.7 requires comparative amounts in respect of the previous period for all amounts presented in the financial statements, a complete set of financial statements means that a micro-entity shall present, as a minimum, two of each of the required financial statements and related notes.
- 3.11 In a complete set of financial statements, a micro-entity shall present each financial statement with equal prominence.
- 3.12 A micro-entity may use titles for the financial statements other than those used in this FRS as long as they are not misleading.

Identification of the financial statements

- 3.13 A micro-entity shall clearly identify each of the financial statements and the notes. In addition, a micro-entity shall display the following information prominently, and repeat it when necessary for an understanding of the information presented:
- (a) the name of the reporting entity and any change in its name since the end of the preceding reporting period;
 - (b) the date of the end of the reporting period and the period covered by the financial statements;
 - (c) the presentation currency; and
 - (d) the level of rounding, if any, used in presenting amounts in the financial statements.
- 3.13A In accordance with section 396(A1) of the **Act**, the financial statements of a micro-entity in the UK shall state:
- (a) the part of the United Kingdom in which the micro-entity is registered;
 - (b) the micro-entity's registered number;
 - (c) whether the micro-entity is a public or private company and whether it is limited by shares or by guarantee⁴;

² For Irish micro-entities reference to the Act shall be replaced with the Companies Act 2014.

³ Irish micro-entities are not required to include the notes to the financial statements at the foot of the statement of financial position.

⁴ Public companies are excluded from the micro-entities regime, therefore a micro-entity shall state that it is a private company. Sub-paragraph (c) does not apply to micro-entities that are LLPs.

- (d) the address of the micro-entity's registered office; and
- (e) where appropriate, the fact that the micro-entity is being wound up.

3.13B In accordance with section 291(3A) of the Companies Act 2014, the financial statements of a micro-entity in the Republic of Ireland shall state the following:

- (a) the name and legal form of the micro-entity;
- (b) the place of registration of the micro-entity and the number under which it is registered;
- (c) the address of its registered office; and
- (d) if relevant, the fact that the micro-entity is being wound up, and where appropriate, whether a receiver or a provisional liquidator has been appointed and the former name as well as the existing name of the micro-entity if the winding up of the micro entity commences within one year after the date on which it has changed its name.

Statement of compliance with the micro-entity provisions

3.14 Financial statements prepared in accordance with the **micro-entity provisions** shall contain on the statement of financial position, in a prominent position above the signature, a statement that the financial statements are prepared in accordance with the micro-entity provisions⁵.

Disclosures

3.15 An Irish micro-entity shall disclose particulars of any departure from the principles set out in company law in preparing the micro-entity's financial statements, the reasons for it and its effects on the statement of financial position and income statement in accordance with Appendix B to Section 6 *Notes to the Financial Statements*.

⁵ This is required by section 414(3) of the Act, or Regulation 12 of the *Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008* (SI 2008/1911) for micro-entities in the UK and section 324(4A) of the Companies Act 2014 for micro-entities in the Republic of Ireland.

Section 4

Statement of Financial Position

Scope of this section

- 4.1 A **micro-entity** shall present its **financial position** at the end of the **reporting period**. This section sets out the information that shall be presented in a **statement of financial position** and how to present it. The statement of financial position (which is referred to as the balance sheet in the **Act**) presents a **micro-entity's assets, liabilities** and **equity** as at the end of the reporting period.
- 4.2 A micro-entity is permitted, but not required, to present information additional to that required by this section. Paragraph 1.3 applies to any additional information presented.

Information to be presented in the statement of financial position

- 4.3 A micro-entity shall present a statement of financial position in accordance with one of the formats set out in Section C of Part 1 of Schedule 1 to the **Small Companies Regulations**⁶ or Section C of Part 1 of Schedule 1 to the **Small LLP Regulations**⁷, as illustrated below:

Format 1	CU	CU
Called up share capital not paid	X	
Fixed assets	X	
Current assets	X	
Prepayments and accrued income	X	
Creditors: amounts falling due within one year	<u>(X)</u>	
Net current assets / (liabilities)		<u>X/(X)</u>
Total assets less current liabilities		X
Creditors: amounts falling due after more than one year		(X)
Provisions for liabilities		(X)
Accruals and deferred income		<u>(X)</u>
		<u>X</u>
		<u> </u>
Capital and reserves		<u>X</u>

⁶ Irish micro-entities shall refer to Section B of Part II of Schedule 3B to the Companies Act 2014.

⁷ LLPs shall describe the items as set out in the Small LLP Regulations. In particular, 'Called up share capital not paid' shall not be used and 'Loans and other debts due to members' and 'Members' other interests' shall be used instead of 'Capital and reserves'.

Format 2	CU	CU
Assets		
Called up share capital not paid		X
Fixed assets		X
Current assets		X
Prepayments and accrued income		X
		<hr/>
		X
Capital, Reserves and Liabilities		
Capital and reserves		X
Provisions for liabilities		X
Creditors		
Amounts falling due within one year	X	
Amounts falling due after one year	X	
	<hr/>	
		X
Accruals and deferred income		X
		<hr/>
		X

Creditors: amounts falling due within one year

- 4.4 A micro-entity shall classify a creditor as due within one year when the micro-entity does not have an unconditional right, at the end of the reporting period, to defer settlement of the creditor for at least 12 months after the **reporting date**.

Disclosures

- 4.5 An Irish micro-entity shall disclose information in relation to the following items in accordance with Appendix B to Section 6 *Notes to the Financial Statements*:
- a change in the format of the statement of financial position adopted;
 - an asset or liability that relates to more than one of the items listed in the statement of financial position; and
 - any debts included under 'creditors' against which security has been given.

Section 5 Income Statement

Scope of this section

- 5.1 A **micro-entity** shall present its **profit or loss** for a period, ie its financial **performance** for the period. This section sets out the information that shall be presented in the **income statement** (which is referred to as the profit and loss account in the **Act**) and how to present it.
- 5.2 A micro-entity is permitted, but not required, to present information additional to that required by this section. Paragraph 1.3 applies to any additional information presented.

Presentation of profit or loss

- 5.3 A micro-entity shall present its profit or loss for a period in an income statement in accordance with Section C of Part 1 of Schedule 1 to the **Small Companies Regulations**⁸ or Section C of Part 1 of Schedule 1 to the **Small LLP Regulations**, as illustrated below:

	CU
Turnover	X
Other income	X
Cost of raw materials and consumables	(X)
Staff costs	(X)
Depreciation and other amounts written off assets	(X)
Other charges	(X)
Tax	(X)
Profit or loss ⁹	<u>X / (X)</u>

- 5.4 An entity shall recognise all items of **income** and **expense** in a period in profit or loss unless an FRS requires or permits otherwise, or unless prohibited by the Act. For example, under this FRS, the effects of corrections of **material errors** and changes in **accounting policies** are presented as retrospective adjustments of prior periods rather than as part of profit or loss in the period in which they arise (see Section 8 *Accounting Policies, Estimates and Errors*).

⁸ Irish micro-entities shall refer to Section B of Part II of Schedule 3B to the Companies Act 2014.

⁹ LLPs shall describe this item as 'Profit or loss for the financial year before members' remuneration and profit shares'.

Section 6

Notes to the Financial Statements

Scope of this section

- 6.1 This section sets out the information that shall be disclosed in the **notes** to the **financial statements** and where. A **micro-entity** is permitted, but not required, to disclose information additional to that required by this section. Paragraph 1.3 applies to any additional information disclosed.

Structure and content of the notes

- 6.2 The notes to the financial statements of a micro-entity in the UK shall be presented at the foot of the **statement of financial position** and shall include information about:
- (a) off-balance sheet arrangements as required by section 410A of the **Act** (see paragraph 6A.1 of Appendix A to this section);
 - (b) employee numbers as required by section 411 of the Act (see paragraph 6A.2 of Appendix A to this section);
 - (c) advances, credit and guarantees granted to directors as required by section 413 of the Act (see paragraph 6A.3 of Appendix A to this section); and
 - (d) financial commitments, guarantees and contingencies required by regulation 5A of, and paragraph 57 of Part 3 of Schedule 1 to, the **Small Companies Regulations** (see paragraphs 6A.4 and 6A.5 of Appendix A to this section).
- 6.3 The notes to the financial statements of an **LLP** which qualifies as a micro-entity shall be presented at the foot of the statement of financial position and shall include information about:
- (a) off-balance sheet arrangements as required by Regulation 11 of *The Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008* (SI2008/1911) (see paragraph 6A.1 of Appendix A to this section);
 - (b) employee numbers as required by Regulation 11 of *The Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008* (SI2008/1911) (see paragraph 6A.2 of Appendix A to this section);
 - (c) financial commitments, guarantees and contingencies as required by paragraph 55 of Part 3 of Schedule 1 to the **Small LLP Regulations** (see paragraphs 6A.4 and 6A.5 in the Appendix A to this section).
- 6.4 Appendix B to this section sets out the disclosure requirements applicable to micro-entities in the Republic of Ireland.

Appendix A to Section 6

Company law disclosure requirements for micro-entities in the UK

This appendix is an integral part of Section 6.

This appendix sets out the company law disclosure requirements referred to in paragraph 6.2 for micro-entities in the UK. Other than substituting company law terminology with the equivalent terminology used in this FRS (see Appendix II Table of equivalence for company law terminology), the drafting is as close as possible to that set out in company law.

When this FRS contains a disclosure requirement related to a company law requirement, this has been indicated.

- 6A.1 *If in any reporting period a micro-entity is or has been party to arrangements that are not reflected in its statement of financial position and at the reporting date the risks or benefits arising from those arrangements are material, the nature and business purpose of the arrangements must be given in the notes to the financial statements to the extent necessary for enabling the financial position of the micro-entity to be assessed. (Section 410A of the Act)*
- 6A.2 *The notes to a micro-entity's financial statements must disclose the average number of persons employed by the micro-entity in the financial year. (Section 411 of the Act)*
- 6A.3 *Details of advances and credits granted by a micro-entity to its directors and guarantees of any kind entered into by a micro-entity on behalf of its directors must be shown in the notes to the financial statements.*

The details required of an advance or credit are:

- (a) its amount;*
- (b) an indication of the interest rate;*
- (c) its main conditions;*
- (d) any amounts repaid;*
- (e) any amounts written off; and*
- (f) any amounts waived.*

There must also be stated in the notes to the financial statements the totals of amounts stated under (a), (d), (e) and (f).

The details required of a guarantee are:

- (a) its main terms;*
- (b) the amount of the maximum liability that may be incurred by a micro-entity;*
- (c) any amount paid and any liability incurred by a micro-entity for the purpose of fulfilling the guarantee (including any loss incurred by reason of enforcement of the guarantee).*

There must also be stated in the notes to the financial statements the totals of amounts stated under (b) and (c). (Section 413 of the Act)

- 6A.4 *The total amount of any financial commitments, guarantees and contingencies that are not included in the statement of financial position must be stated. (paragraph 57(1) of*

Schedule 1 to the Small Companies Regulations or paragraph 55(1) of Schedule 1 to the Small LLP Regulations)

The total amount of any commitments concerning pensions must be separately disclosed. (paragraph 57(3) of Schedule 1 to the Small Companies Regulations or paragraph 55(3) of Schedule 1 to the Small LLP Regulations)

The total amount of any commitments which are undertaken on behalf of or for the benefit of:

(a) any parent, fellow subsidiary or any subsidiary of a micro-entity; or

(b) any undertaking in which a micro-entity has a participating interest,

must be separately stated and those within (a) must also be stated separately from those within (b). (paragraph 57(4) of Schedule 1 to the Small Companies Regulations or paragraph 55(4) of Schedule 1 to the Small LLP Regulations)

Paragraphs 9.28(a), 11.9, 12.28(a), 13.17(a), 14.3, 15.17, 15.33, 16.19, 23.22 and 27.5(a) address these disclosure requirements within the context of specific transactions.

6A.5 *An indication of the nature and form of any valuable security given by the micro-entity in respect of commitments, guarantees and contingencies within paragraph 6A.2. must be given. (paragraph 57(2) of Schedule 1 to the Small Companies Regulations or paragraph 55(2) of Schedule 1 to the Small LLP Regulations)*

Paragraphs 9.28(b), 10.22, 12.28(b), 13.17(b) and 27.5(b) address these disclosure requirements within the context of specific transactions.

Appendix B to Section 6

Company law disclosure requirements for micro-entities in the Republic of Ireland

This appendix is an integral part of Section 6.

This appendix sets out the company law disclosure requirements referred to in paragraph 6.4 for micro-entities in the Republic of Ireland. The drafting is as close as possible to that set out in company law, other than, for example, substituting company law terminology with the equivalent terminology used in this FRS (see Appendix II Table of equivalence for company law terminology). References in this appendix to sections of the Companies Act 2014 are to the sections of that Act as amended by the Companies (Accounting) Act 2017 and references to Schedule 3B are to Schedule 3B to the Companies Act 2014.

When this FRS contains a disclosure requirement related to a company law requirement this has been indicated.

6B.1 *These notes shall be presented in the order in which, where relevant, the items to which they relate are presented in the statement of financial position and in the income statement. (Schedule 3B, paragraph 31(2))*

Basis of preparation

6B.2 *A micro-entity shall ensure that its financial statements include a statement as to whether they have been prepared in accordance with this FRS and for any material departure from this FRS, the effect of the departure and the reasons for it are noted in the financial statements. (Section 291(7) of the Companies Act 2014)*

Accounting policies

6B.3 *A micro-entity shall disclose in the notes to its financial statements the accounting policies adopted by the micro-entity in determining:*

- (a) the items and amounts to be included in its statement of financial position; and*
- (b) the items and amounts to be included in its income statement. (Section 321(1) of the Companies Act 2014)*

6B.4 *In any case where any goodwill acquired by a micro-entity is shown or included as an asset in the micro-entity's statement of financial position, the period chosen for writing off the consideration for that goodwill and the reasons for choosing that period shall be disclosed in a note to the financial statements. (Schedule 3B, paragraph 25(4))*

See paragraph 14.4.

Changes in presentation and accounting policies and correcting prior period errors

6B.5 *Where any change is made in the format adopted in preparing a statement of financial position of a micro-entity, the reasons for the change, together with full particulars of the change, shall be given in a note to the financial statements in which the new format is first adopted. (Schedule 3B, paragraph 3(2))*

See paragraph 4.5(a).

6B.6 *Where a micro-entity changes an accounting policy and has disclosed such change in the notes to the financial statements, the notes to those financial statements shall also disclose:*

- (a) the reason for the change in accounting policy; and*
- (b) to the extent practicable, the impact of the change in accounting policy on the financial statements for the current reporting period and on the financial statements of preceding periods. (Section 321(3) of the Companies Act 2014)*

See paragraph 8.10A.

6B.7 *Where the corresponding amount for the immediately preceding reporting period is not comparable with the amount to be shown for the item in question in respect of the reporting period to which the statement of financial position or income statement relates, the former amount may be adjusted, and particulars of the adjustment and the reasons therefor shall be given in a note to the financial statements. (Schedule 3B, paragraph 5)*

This is likely to be relevant when there has either been a change in accounting policy or the correction of a material prior period error. See Section 8 *Accounting Policies, Estimates and Errors*.

Departure from principles in company law

6B.8 *If it appears to the micro-entity that there are special reasons for departing from any of the principles set out in company law in preparing the micro-entity's financial statements in respect of any reporting period, it may do so, in which case particulars of the departure, the reasons for it, and its effects on the statement of financial position and income statement must be given in the notes to the financial statements. (Schedule 3B, paragraph 19)*

This is only expected to occur in special circumstances. See Section 3 *Financial Statement Presentation*.

Notes supporting the statement of financial position

6B.9 *Where an asset or liability relates to more than one of the items listed in the statement of financial position, its relationship to other items shall be disclosed either under the item where it is shown or in the notes to the financial statements. (Schedule 3B, paragraph 4(4))*

See paragraph 4.5(b).

Impairment of assets

6B.10 *Value adjustments for impairment of fixed assets (including fixed asset investments) must be disclosed (either separately or in aggregate) in a note to the financial statements if not shown separately in the income statement. (Schedule 3B, paragraphs 23(1) and (2))*

6B.11 *Any value adjustments for impairment of fixed assets (including fixed asset investments) that are reversed because the reasons for which they were made have ceased to apply must be disclosed (either separately or in aggregate) in a note to the financial statements if not shown separately in the income statement. (Schedule 3B, paragraph 23(3))*

See paragraph 22.22.

Indebtedness, guarantees and financial commitments

6B.12 *In respect of 'creditors' shown in the micro-entity's statement of financial position there shall be stated:*

- (a) the aggregate amount of any debts included under that item in respect of which any security has been given; and*
- (b) an indication of the nature of the securities so given. (Schedule 3B, paragraph 34)*

See paragraph 4.5(c).

6B.13 *Particulars shall be given of any charge on the assets of the micro-entity to secure the liabilities of any other person, including, where practicable, the amount secured. (Schedule 3B, paragraph 35(1))*

6B.14 *Particulars and the total amount or estimated total amount shall be given with respect to any other financial commitment, guarantee or contingency not provided for in the statement of financial position. (Schedule 3B, paragraph 35(2))*

See paragraphs 9.28(a), 11.9, 12.128(a), 13.17(a), 14.3, 15.17, 15.33, 16.19 and 27.5(a).

The aggregate amount of any such commitments, guarantees or contingencies which are undertaken on behalf of or for the benefit of:

- (a) any parent or fellow subsidiary of the micro-entity;*
- (b) any subsidiary of the micro-entity; or*
- (c) any undertaking in which the micro-entity has a participating interest,*

shall be separately stated and those within each of clauses (a), (b) and (c) shall also be stated separately from those within any other of those clauses. (Schedule 3B, paragraph 35(6))

6B.15 *An indication of the nature and form of any valuable security given by the micro-entity in connection with its commitments, guarantees and contingencies not provided for in the statement of financial position must be given. (Schedule 3B, paragraph 35(3))*

See paragraphs 9.28(b), 10.22, 12.28(b), 13.17(b) and 27.5(b).

6B.16 *The total amount of any commitments not provided for in the statement of financial position concerning retirement benefits shall be disclosed separately. (Schedule 3B, paragraph 35(4))*

See paragraph 23.22.

6B.17 *Particulars shall be given of retirement benefit commitments which are included in the statement of financial position. (Schedule 3B, paragraph 35(5))*

See paragraph 23.23.

Appropriation of profit or loss

6B.18 *The income statement, statement of financial position or notes to the financial statements of a micro-entity for a reporting period shall show:*

- (a) *the aggregate amount of dividends paid in the reporting period (other than dividends for which a liability existed at the immediately preceding reporting date);*
- (b) *the aggregate amount of dividends the micro-entity is liable to pay at the reporting date (other than dividends for which a liability existed at the immediately preceding reporting date);*
- (c) *separately, any transfer between the retained earnings and other reserves;*
- (d) *any other increase or reduction in the balance on retained earnings since the immediately preceding reporting date;*
- (e) *the profit or loss brought forward at the beginning of the reporting period; and*
- (f) *the profit or loss carried forward at the end of the reporting period. (Schedule 3B, paragraph 33)*

See paragraph 17.16 in relation to sub-paragraphs (a) and (b).

Related party disclosures

Transactions with directors (Sections 307 and 308 of the Companies Act 2014)

6B.19 *The financial statements of a micro-entity shall disclose, both for the current and the preceding reporting period, in the notes to the financial statements the particulars of the following arrangements (see paragraphs 6B.20 to 6B.23).*

Loans, quasi-loans and credit transactions^{10 11}

6B.20 *The particulars required in respect of loans, quasi-loans and credit transactions entered into by the micro-entity with or for persons who at any time during the reporting period, were directors of the company or of its parent or persons connected with such directors, separately for each director or other person, are:*

- (a) *the name of the person for whom the arrangements were made and where that person is or was connected with a director of the micro-entity or its parent, the name of the director;*
- (b) *the value of the arrangements at the beginning and end of the reporting period;*
- (c) *advances made under the arrangements during the reporting period;*
- (d) *amounts repaid under the arrangements during the reporting period;*
- (e) *the amounts of any allowance made during the reporting period in respect of any failure or anticipated failure by the borrower to repay the whole or part of the outstanding amount;*
- (f) *amounts outstanding under the arrangements waived during the reporting period;*

¹⁰ Other arrangements: Similar disclosures must be given where a micro-entity has been assigned or has assumed any right or obligation or liability which, if it had itself undertaken that right or obligation or liability, would have fallen under these disclosures. (Sections 307(1)(e) and 307(7) of the Companies Act 2014).

¹¹ Exemption: The disclosure requirements in paragraphs 6B.20 to 6B.23 do not apply in relation to an individual director and persons connected with him/her if the aggregate value of all agreements, transactions and arrangements did not, at any time during the reporting period, exceed €7,500 for that director and those persons. Section 308(6) states that references to 'director' are also to be read as references to an 'officer who is not a director' as applicable. (Sections 308(3), 308(5) and 308(6) of the Companies Act 2014).

- (g) *an indication of the interest rate; and*
- (h) *the arrangements' other main conditions. (Section 307(3) of the Companies Act 2014)*

Additionally, a separate total of the amounts stated for the purposes of each of paragraphs (b) to (f) above, and the amounts stated for the purposes of paragraph (b) expressed as a percentage of the net assets of the micro-entity at the beginning and end of the reporting period shall be disclosed. (Section 307(8)(a) and (c) of the Companies Act 2014) These additional requirements are extended to persons who are officers (but not directors) of the micro-entity or its parent, and separate disclosure in respect of these officers is required on an aggregate basis, as well as the number of officers for whom such arrangements were made. (Section 307(9) of the Companies Act 2014)

- 6B.21 *The particulars required in respect of an agreement to enter into loans, quasi-loans or credit transactions by the micro-entity with or for persons who at any time during the reporting period, were directors of the company or directors of its parent or persons connected with such directors, are those of subparagraphs (a), (g) and (h) of paragraph 6B.20, and additionally the value of the arrangements agreed to. (Section 307(4) of the Companies Act 2014)*

All the above disclosures shall be made separately for each director or other person.

Guarantees and security provided by the micro-entity^{12 13}

- 6B.22 *The particulars required for guarantees entered into and security provided by the micro-entity on behalf of persons who at any time during the reporting period were directors of the micro-entity or of its parent or persons connected with such directors in connection with a loan, quasi-loan or credit transaction entered into with or for those directors or other persons, separately for each director or other person, are:*

- (a) *the name of the person for whom the arrangements were made and where that person is or was connected with a director of the micro-entity or its parent, the name of the director;*
- (b) *the amount of the maximum liability that may be incurred by the micro-entity;*
- (c) *any amount paid and any liability incurred by the micro-entity for the purpose of fulfilling the guarantee or on foot of the provision of security (including any loss incurred by reason of enforcement of the guarantee or loss of the security); and*
- (d) *the arrangements' main terms. (Section 307(5) of the Companies Act 2014)*

Additionally, a separate total of the amounts stated for the purposes of each of paragraphs (b) and (c) above is required. (Section 307(8)(b) of the Companies Act 2014) This requirement is extended to persons who are officers (but not directors) of the micro-entity or its parent and separate disclosure in respect of these officers is required on an aggregate basis, as well as the number of officers for whom such arrangements were made. (Section 307(9) of the Companies Act 2014)

¹² Other arrangements: Similar disclosures must be given where a micro-entity has been assigned or has assumed any right or obligation or liability which, if it had itself undertaken that right or obligation or liability, would have fallen under these disclosures. (Sections 307(1)(e) and 307(7) of the Companies Act 2014).

¹³ Exemption: The disclosure requirements in paragraphs 6B.20 to 6B.23 do not apply in relation to an individual director and persons connected with him/her if the aggregate value of all agreements, transactions and arrangements did not, at any time during the reporting period, exceed €7,500 for that director and those persons. Section 308(6) states that references to 'director' are also to be read as references to an 'officer who is not a director' as applicable. (Sections 308(3), 308(5) and 308(6) of the Companies Act 2014).

6B.23 *The particulars required in respect of agreements by the micro-entity to enter into guarantees or provide security on behalf of persons who at any time during the reporting period were directors of the micro-entity or of its parent or persons connected with such directors in connection with a loan, quasi-loan or credit transaction entered into with or for those directors or other persons, are those of subparagraphs (a), (b) and (d) of paragraph 6B.22. (Section 307(6) of the Companies Act 2014)*

The disclosures shall be made separately for each director or other person.

Additional requirements

6B.24 *Where at any time during the reporting period the aggregate of the amounts of:*

- (a) the amount outstanding under arrangements waived comprising loans, quasi-loans and credit transactions; and*
- (b) the amount of the maximum liability that may be incurred by the micro-entity in respect of arrangements comprising guarantees entered into or security provided in connection with a loan, quasi-loan or credit transaction amount to more than 10 per cent of the net assets of the micro-entity, the aggregate amount shall be stated and the percentage of net assets that the total represents. (Section 307(10) of the Companies Act 2014)*

6B.25 *A micro-entity that is a parent shall provide the information required by paragraphs 6B.19 to 6B.24 in its financial statements in relation to both the micro-entity and its subsidiaries. (Section 308(4) of the Companies Act 2014)*

The micro-entities regime is not available if consolidated financial statements are prepared.

Other related party disclosures

6B.26 *Where a micro-entity, or a nominee of the micro-entity or a person acting in that person's own name but on behalf of the micro-entity, holds shares in the micro-entity or an interest in such shares, the notes to the financial statements shall give separately:*

- (a) the number and aggregate nominal value of those shares and, where shares of more than one class have been acquired, the number and aggregate nominal value of each class of such shares, at the beginning and end of the reporting period together with the consideration paid for such shares;*
- (b) a reconciliation of the number and nominal value of each class of such shares from the beginning of the reporting period to the end of the reporting period showing all changes during the reporting period, including further acquisitions, disposals and cancellations, in each case showing the value of the consideration paid or received, if any;*
- (c) the reasons for any acquisitions made during the reporting period;*
- (d) the proportion of called-up share capital held at the beginning and end of the reporting period; and*
- (e) particulars of any restriction on profits available for distribution by virtue of the application of Section 320. (Section 320 of the Companies Act 2014)*

Other

6B.27 *Amounts in respect of items representing assets or income may be set off against amounts in respect of items representing liabilities or expenditure or vice versa in accordance with applicable accounting standards, provided that the gross amounts are disclosed in a note to the financial statements. (Schedule 3B, paragraph 7)*

See Section 2 *Concepts and Pervasive Principles*.

6B.28 *In accordance with Sections 325(1A)(b) and 328 of the Companies Act 2014 a micro-entity that chooses not to prepare a directors' report shall provide the information required by Section 328 of the Companies Act 2014 in respect of acquisitions or disposals of own shares. (Section 325(1A)(b) of the Companies Act 2014)*

Section 7

Subsidiaries, Associates, Jointly Controlled Entities and Intermediate Payment Arrangements

Scope of this section

- 7.1 This section applies to investments in **subsidiaries** and **associates**, interests in **jointly controlled entities** and intermediate payment arrangements.

Investments in subsidiaries, associates and interests in jointly controlled entities

- 7.2 A **micro-entity** shall account for any investments in subsidiaries and associates and any interests in jointly controlled entities in accordance with Section 9 *Financial Instruments*.

Consolidated financial statements

- 7.3 An entity that is required or chooses to present **consolidated financial statements** is excluded from the **micro-entities regime** (sections 384A(8) and 384B(2) of the **Act**¹⁴) and shall not apply this FRS.

Intermediate payment arrangements (eg ESOPs)

- 7.4 Intermediate payment arrangements may take a variety of forms:
- (a) The intermediary is usually established by the micro-entity and constituted as a trust, although other arrangements are possible.
 - (b) The relationship between the micro-entity and the intermediary may take different forms. For example, when the intermediary is constituted as a trust, the micro-entity will not have a right to direct the intermediary's activities. However, in these and other cases the micro-entity may give advice to the intermediary or may be relied on by the intermediary to provide the information it needs to carry out its activities. Sometimes, the way the intermediary has been set up gives it little discretion in the broad nature of its activities.
 - (c) The arrangements are most commonly used to pay employees, although they are sometimes used to compensate suppliers of goods and services other than employee services. Sometimes the micro-entity's employees and other suppliers are not the only beneficiaries of the arrangement. Other beneficiaries may include past employees and their dependants, and the intermediary may be entitled to make charitable donations.
 - (d) The precise identity of the persons or entities that will receive payments from the intermediary, and the amounts that they will receive, are not usually agreed at the outset.
 - (e) The micro-entity often has the right to appoint or veto the appointment of the intermediary's trustees (or its directors or the equivalent).
 - (f) The payments made to the intermediary and the payments made by the intermediary are often cash payments but may involve other transfers of value.

¹⁴ Or, when relevant, Regulation 5A of the *Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008* (SI 2008/1911). Irish micro-entities shall refer to section 280D of the Companies Act 2014.

Examples of intermediate payment arrangements are employee share ownership plans (ESOPs) and employee benefit trusts that are used to facilitate employee shareholdings under remuneration schemes. In a typical employee benefit trust arrangement for **share-based payment transactions**, a micro-entity makes payments to a trust or guarantees borrowing by the trust, and the trust uses its funds to accumulate **assets** to pay the micro-entity's employees for services the employees have rendered to the micro-entity.

Although the trustees of an intermediary must act at all times in accordance with the interests of the beneficiaries of the intermediary, most intermediaries (particularly those established as a means of remunerating employees) are specifically designed so as to serve the purposes of the micro-entity, and to ensure that there will be minimal risk of any conflict arising between the duties of the trustees of the intermediary and the interest of the micro-entity, such that there is nothing to encumber implementation of the wishes of the micro-entity in practice. Where this is the case, the micro-entity has de facto **control**.

- 7.4A It is possible for an entity to be owned by a trust established for the benefit of employees without the entity controlling the trust. An example is when the entity is a co-operative, owned by its employees, and all of the shares are held in a trust for the benefit of the employees but the shares never **vest** in individual employees with dividends from the company being distributed to employees solely in accordance with the provisions of the trust deed.

Accounting for intermediate payment arrangements

- 7.5 When a micro-entity makes payments (or transfers assets) to an intermediary, there is a rebuttable presumption that the entity has exchanged one asset for another and that the payment itself does not represent an immediate **expense**. To rebut this presumption at the time the payment is made to the intermediary, the micro-entity must demonstrate:
- (a) it will not obtain future economic benefit from the amounts transferred; or
 - (b) it does not have control of the right or other access to the future economic benefit it is expected to receive.
- 7.6 Where a payment to an intermediary is an exchange by the micro-entity of one asset for another, any assets that the intermediary acquires in a subsequent exchange transaction will also be under the control of the micro-entity. Accordingly, assets and **liabilities** of the intermediary shall be accounted for by the micro-entity as an extension of its own business and recognised in its **financial statements**. An asset will cease to be recognised as an asset of the micro-entity when, for example, the asset of the intermediary vests unconditionally with identified beneficiaries.
- 7.7 A micro-entity may distribute its own equity instruments, or other equity instruments, to an intermediary in order to facilitate employee shareholdings under a remuneration scheme. Where this is the case and the micro-entity has control, or de facto control, of the assets and liabilities of the intermediary, the commercial effect is that the micro-entity is, for all practical purposes, in the same position as if it had purchased the shares directly.
- 7.8 Where an intermediary holds the micro-entity's equity instruments, the micro-entity shall account for the equity instruments as if it had purchased them directly. The micro-entity shall account for the assets and liabilities of the intermediary in its financial statements as follows:

- (a) The consideration paid for the equity instruments of the sponsoring entity shall be deducted from **equity** until such time that the equity instruments vest unconditionally with employees.
- (b) Other assets and liabilities of the intermediary shall be recognised as assets and liabilities of the micro-entity.
- (c) No **gain** or loss shall be recognised in **profit or loss** on the purchase, sale, issue or cancellation of the micro-entity's own equity instruments.
- (d) Finance costs and any administration expenses shall be recognised on an **accrual basis** rather than as funding payments are made to the intermediary.
- (e) Any dividend income arising on the micro-entity's own equity instruments shall be excluded from profit or loss and deducted from the aggregate of dividends paid.

Section 8

Accounting Policies, Estimates and Errors

Scope of this section

- 8.1 This section sets out requirements for:
- (a) selecting and applying the **accounting policies** used in preparing **financial statements**;
 - (b) accounting for **changes in accounting estimates**; and
 - (c) accounting for corrections of **errors** in prior period financial statements.

Selection and application of accounting policies

- 8.2 Accounting policies are the specific principles, bases, conventions, rules and practices applied by a **micro-entity** in preparing and presenting financial statements.
- 8.3 If this FRS specifically addresses a transaction, other event or condition, a micro-entity shall apply this FRS. However, the micro-entity need not follow a requirement in this FRS if the effect of doing so would not be **material**.
- 8.4 If this FRS does not specifically address a transaction, other event or condition, a micro-entity's management shall use its judgement in developing and applying an accounting policy that results in information that:
- (a) represents faithfully the transactions, other events or conditions;
 - (b) reflects the economic substance of the transactions, other events and conditions, and not merely the legal form;
 - (c) is neutral, ie free from bias; and
 - (d) is **prudent**.
- 8.5 In making the judgement described in paragraph 8.4, management shall refer to and consider the definitions, **recognition** criteria and **measurement** concepts for **assets, liabilities, income** and **expenses** and the pervasive principles in Section 2 *Concepts and Pervasive Principles*. A micro-entity is not required to provide any disclosures other than those required by Section 6 *Notes to the Financial Statements* in respect of these transactions or events.

Consistency of accounting policies

- 8.6 A micro-entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions.

Changes in accounting policies

- 8.7 A micro-entity shall change an accounting policy only if the change:
- (a) is required by this FRS; or
 - (b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the micro-entity's **financial position** and financial **performance**.

- 8.8 The following are not changes in accounting policies:
- (a) the application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring; and
 - (b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were not material.

Applying changes in accounting policies

- 8.9 A micro-entity shall account for changes in accounting policy as follows:
- (a) a micro-entity shall account for a change in accounting policy resulting from a change in the requirements of this FRS in accordance with the transitional provisions, if any, specified in that amendment; and
 - (b) a micro-entity shall account for all other changes in accounting policy retrospectively (see paragraph 8.10).

Retrospective application

- 8.10 When a change in accounting policy is applied retrospectively in accordance with paragraph 8.9, the micro-entity shall apply the new accounting policy to comparative information for prior periods to the earliest date for which it is practicable, as if the new accounting policy had always been applied. When it is **impracticable** to determine the individual period effects of a change in accounting policy on comparative information for one or more prior periods presented, the micro-entity shall apply the new accounting policy to the **carrying amounts** of assets and liabilities as at the beginning of the earliest period for which **retrospective application** is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of **equity** for that period.

Disclosures

- 8.10A An Irish micro-entity shall disclose information in relation to changes to accounting policies and corrections of material prior period errors in accordance with Appendix B to Section 6 *Notes to the Financial Statements*.

Changes in accounting estimates

- 8.11 A **change in accounting estimate** is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.
- 8.12 A micro-entity shall recognise the effect of a change in an accounting estimate, other than a change to which paragraph 8.13 applies, **prospectively** by including it in **profit or loss** in:
- (a) the period of the change, if the change affects that period only; or
 - (b) the period of the change and future periods, if the change affects both.

- 8.13 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, the micro-entity shall recognise it by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

Corrections of prior period errors

- 8.14 Prior period errors are omissions from, and misstatements in, a micro-entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:
- (a) was available when financial statements for those periods were authorised for issue; and
 - (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
- 8.15 Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.
- 8.16 To the extent practicable, a micro-entity shall correct a material prior period error retrospectively in the first financial statements authorised for issue after its discovery by:
- (a) restating the comparative amounts for the prior period(s) presented in which the error occurred; or
 - (b) if the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.
- 8.17 When it is impracticable to determine the period-specific effects of a material error on comparative information for one or more prior periods presented, the micro-entity shall restate the opening balances of assets, liabilities and equity for the earliest period for which retrospective restatement is practicable (which may be the current period).

Section 9

Financial Instruments

Scope of this section

- 9.1 This section sets out the requirements for the **recognition, derecognition, measurement** and disclosure of **financial instruments (financial assets and financial liabilities)**.
- 9.2 All financial instruments are accounted for in accordance with this section, unless they are excluded by paragraph 9.3. Examples of financial instruments in the scope of this section include:
- (a) cash;
 - (b) accounts receivable and payable (trade debtors and creditors);
 - (c) commercial paper and commercial bills held;
 - (d) demand and fixed-term deposits with banks or similar institutions;
 - (e) bonds, loans and similar instruments;
 - (f) investments;
 - (g) **derivatives**, eg options, warrants, futures contracts, forward contracts and interest rate swaps.
- 9.3 This section does not apply to the following financial instruments:
- (a) Financial instruments that meet the definition of a **micro-entity's own equity**, and the equity component of **compound financial instruments** issued by the reporting micro-entity that contain both a **liability** and an equity component (see Section 17 *Liabilities and Equity*).
 - (b) **Leases**, to which Section 15 *Leases* applies. However, the **derecognition** requirements in paragraphs 9.21 to 9.23 and impairment accounting requirements in paragraphs 9.16 to 9.19 apply to derecognition and impairment of receivables recognised by a lessor and the derecognition requirements in paragraphs 9.25 and 9.26 apply to payables recognised by a lessee arising under a **finance lease**.
 - (c) Employers' rights and obligations under employee benefit plans, to which Section 23 *Employee Benefits* applies.
 - (d) Financial instruments, contracts and obligations to which Section 21 *Share-based Payment* applies.
 - (e) Reimbursement assets and **financial guarantee contracts** accounted for in accordance with Section 16 *Provisions and Contingencies*.
 - (f) Contracts for contingent consideration in a **business combination** (see Section 14 *Business Combinations and Goodwill*). This exemption applies only to the acquirer.

Initial recognition of financial assets and liabilities

- 9.4 A micro-entity shall recognise a financial asset or a financial liability only when the micro-entity becomes a party to the contractual provisions of the instrument.

Initial measurement

- 9.5 A financial asset or financial liability is recognised initially at its cost. The cost is measured at the transaction price.

Examples – Transaction price of a financial asset or liability	
1	For a loan the transaction price is the amount borrowed or loaned.
2	For trade receivables or payables (trade debtors or trade creditors) the transaction price equals the invoice price unless payment is deferred beyond normal credit terms (see paragraph 9.6).
3	For an investment the transaction price is the consideration given (eg cash paid to acquire the investment).
4	For an option the transaction price is the premium paid to purchase the option.

- 9.6 When a micro-entity purchases **inventory, property, plant and equipment, investment property** or sells goods or services with settlement deferred beyond normal credit terms, the transaction price is the cash price available on the date of the transaction (see Sections 10 *Inventories*, 12 *Property, Plant and Equipment and Investment Property* and 18 *Revenue* respectively).

Example – Transaction price when payment is deferred	
A micro-entity sells goods to a customer for CU100. Customers are usually required to pay within 14 days of the invoice date, but the micro-entity agrees with the customer that payment will be deferred for one year. The micro-entity sells the same item for CU90, if payment is received within the usual credit terms.	
The cash price for the goods and thereby the transaction price is CU90.	

- 9.7 **Transaction costs** shall be added to the cost of a financial asset or shall be deducted from the cost of a financial liability, unless they are not **material** in which case they are recognised immediately as an **expense** in **profit or loss**.

Examples – Transaction costs	
1	A micro-entity receives a bank loan of CU500. The bank charges CU5 in arrangement fees. The micro-entity determines that the transaction costs are immaterial and recognises them immediately in profit or loss as an expense. The cost of the loan is CU500.
2	A micro-entity is making an investment and buys shares in another entity for CU1,000. The micro-entity incurs legal fees and other transaction costs totalling CU100. The micro-entity determines that the transaction costs are material and includes them in the cost of the investment. The total cost of the investment is CU1,100.
3	A micro-entity takes out a forward foreign currency exchange contract and is charged a fee of CU30. The micro-entity determines that the transaction costs are material. The total cost of the forward foreign currency exchange contract is CU30.

Subsequent measurement

- 9.8 At the end of each **reporting period**, a micro-entity shall measure financial instruments as follows, without any deduction for transaction costs the micro-entity may incur on sale or other disposal:
- (a) Investments in preference shares or **ordinary shares** and investments in **subsidiaries, associates** and interests in **jointly controlled entities** shall be measured at cost less impairment.
 - (b) Derivatives shall be measured as set out in paragraph 9.10.
 - (c) Financial instruments other than those covered by paragraphs (a) and (b) shall be measured as set out in paragraphs 9.12 to 9.15.

All financial assets must be assessed for impairment or uncollectability. See paragraphs 9.16 to 9.19.

Derivatives

- 9.9 Derivatives include forward foreign currency exchange contracts and interest rate swaps. More examples are given in paragraph 9.2(g).
- 9.10 The transaction price of a financial instrument that is a derivative plus any transaction costs not immediately recognised in profit or loss (see paragraph 9.7) less any **impairment losses** recognised to date, is allocated to profit or loss over the term of the contract on a straight-line basis, unless another systematic basis of allocation is more appropriate.

Contractual payments

- 9.11 Under a derivative contract a micro-entity may be required to make or may be entitled to receive payments. A micro-entity shall recognise amounts payable or receivable as they accrue.

Financial instruments measured in accordance with paragraph 9.8(c)

- 9.12 Financial instruments other than those covered in paragraphs 9.8(a) and 9.8(b) are measured as follows:
- (a) the transaction price (see paragraph 9.5);
 - (b) plus, in the case of a financial asset, or minus in the case of a financial liability, transaction costs not yet recognised in profit or loss (see paragraph 9.15);
 - (c) plus the cumulative interest income or expense recognised in profit or loss to date (see paragraphs 9.13 and 9.14);
 - (d) minus all repayments of principal and all interest payments or receipts to date;
 - (e) minus, in the case of a financial asset, any reduction (directly or through the use of an allowance account) for impairment or uncollectability (see paragraphs 9.16 to 9.19).

Allocation of interest income or expense

- 9.13 Total interest income or expense is the difference between the initial transaction price and the total amount of the subsequent contractual receipts or payments, excluding transaction costs.

9.14 A micro-entity shall allocate total interest income or expense over the term of the contract as follows:

- (a) For transactions where settlement is deferred beyond normal credit terms (see paragraph 9.6), total interest income or expense shall be allocated on a straight-line basis over the term of the contract.
- (b) In all other cases, interest income or expense is allocated at a constant rate on the financial asset's or financial liability's **carrying amount** excluding transaction costs not yet recognised in profit or loss (see paragraph 9.12(b)). The applicable rate will normally be the contractual rate of interest and may be a variable or a fixed rate.

Transaction costs

9.15 Transaction costs not immediately recognised in profit or loss in accordance with paragraph 9.7, are recognised in profit or loss on a straight-line basis over the term of the contract.

Example 1: Measurement of a loan liability						
A micro-entity receives a loan of CU1,000 on 1 January 20X0. The micro-entity pays loan arrangement fees of CU50. The contractual interest rate is five per cent payable annually in arrears on 31 December. The loan is repayable after two years. The micro-entity's annual reporting period ends on 31 December.						
The micro-entity determines that the loan arrangement fees (transaction costs) are material and on 1 January 20X0 recognises the loan at its transaction price of CU1,000 less the transaction costs of CU50. The transactions costs of CU50 are recognised in the profit and loss account on a straight-line basis over two years, ie CU25 each year.						
The carrying value of the loan is as follows:						
Year	Carrying amount at 1 Jan	Interest at 5%	Transaction costs in profit or loss	Cash payments	Carrying amount at 31 Dec	
	CU	CU	CU	CU	CU	
20X0	(950)	(50)	(25)	50	(975)	
20X1	(975)	(50)	(25)	1,050	0	

Example 2: Measurement of a loan asset

A micro-entity makes an interest-free loan of CU900 on 1 January 20X0. The loan is repayable after two years. In 20X1 the micro-entity agrees that the borrower only needs to repay CU450 which is paid on 31 December 20X1. The micro-entity's annual reporting period ends on 31 December.

The loan is recognised at its transaction price of CU900 on 1 January 20X0. In 20X1 an impairment loss for the uncollectability of CU450 is recognised. The carrying amount of the loan is as follows:

Year	Carrying amount at 1 Jan	Impairment	Cash receipts	Carrying amount at 31 Dec
	CU	CU	CU	CU
20X0	900	–	–	900
20X1	900	(450)	(450)	

Impairment of financial assets

Recognition and measurement

- 9.16 At the end of each reporting period, a micro-entity shall assess whether there is evidence of impairment of any financial asset.
- 9.17 Evidence that a financial asset could be impaired includes the following events:
- (a) significant financial difficulty of the debtor;
 - (b) a breach of contract, such as a default or delinquency in interest or principal payments;
 - (c) the creditor, for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the creditor would not otherwise consider;
 - (d) it has become **probable** that the debtor will enter bankruptcy or other financial reorganisation;
 - (e) declining market values of the **asset** or similar assets;
 - (f) significant changes with an adverse effect on the asset that have taken place in the technological, market, economic or legal environment; and
 - (g) the contract has become an **onerous contract**.
- 9.18 A micro-entity shall measure an impairment loss for financial assets as set out below. An impairment loss is immediately recognised in profit or loss.
- (a) An investment in preference shares or ordinary shares and an investment in subsidiaries and associates and an interest in jointly controlled entities is impaired and an impairment loss shall be recognised if the asset's carrying amount exceeds the best estimate of the asset's selling price as at the **reporting date**.
 - (b) An asset that is a derivative is impaired and an impairment loss shall be recognised if the asset's carrying value exceeds the asset's **fair value less costs to sell**.
 - (c) An asset measured in accordance with paragraph 9.8(c), is impaired and an impairment loss shall be recognised, if the asset's carrying amount exceeds the total of estimated net cash flows that can be generated from the asset. When the

effect of the time value of money is material, the amount of the net cash flows shall be the **present value** of the estimated net cash flows. The discount rate shall be the asset's current contractual interest rate.

Reversal

- 9.19 A micro-entity shall reverse a previously recognised impairment loss if in a subsequent period the amount of an impairment loss decreases and the decrease can be related to an event occurring after the impairment was recognised (eg an improvement in the debtor's credit rating). The micro-entity shall recognise the amount of the reversal in profit or loss immediately.

Onerous contracts

- 9.20 At each reporting date a micro-entity shall assess whether a derivative constitutes an onerous contract. A derivative is an onerous contract when the expected unavoidable payments exceed the economic benefits expected to be received from the derivative. A derivative which does not mitigate a specific risk or risks of a micro-entity is an onerous contract when the expected payments exceed the expected cash receipts under the contract. The present obligation arising from an onerous contract shall be measured in accordance with Section 16.

Example: Assessment of whether a derivative is onerous
<p>A micro-entity takes out a loan with a variable rate of interest. In order to mitigate the risk of fluctuating interest payments, the micro-entity enters into an interest rate swap. Through the interest rate swap the micro-entity pays a fixed rate of interest and receives a variable rate of interest equal to the interest on the loan.</p> <p>Scenario 1:</p> <p>Interest rates are going down and as a result the payments made by the micro-entity under the interest rate swap are higher than the receipts. The interest rate swap is not an onerous contract because the micro-entity continues to benefit from the interest rate swap by effectively paying a fixed rate of interest on the loan.</p> <p>Scenario 2:</p> <p>The micro-entity repays the loan early, but the interest rate swap cannot be terminated. The micro-entity expects that the payments due under the interest rate swap exceed the receipts. The interest rate swap is an onerous contract because the micro-entity no longer derives a benefit from it.</p>

Derecognition of a financial asset

- 9.21 A micro-entity shall derecognise a financial asset only when:
- (a) the contractual rights to the cash flows from the financial asset expire or are settled;
 - (b) the micro-entity transfers to another party substantially all of the risks (eg slow or non-payment risk) and rewards of ownership (eg future cash flows from a debtor); or
 - (c) when no future economic benefits are expected from holding it or its disposal.
- 9.22 A micro-entity shall recognise any **gain** or loss on the derecognition of a financial asset in profit or loss when the item is derecognised.

- 9.23 If a micro-entity received any proceeds from the transfer of a financial asset, but the conditions in paragraph 9.21 are not met, a micro-entity shall continue to recognise the asset in its entirety and shall recognise a financial liability for the consideration received. The asset and liability shall not be offset. In subsequent periods, the micro-entity shall recognise any **income** on the transferred asset and any expense incurred on the financial liability.

Example 1: Debt factoring arrangement that qualifies for derecognition

A micro-entity sells a group of its accounts receivable to a bank at less than their carrying amount. The micro-entity is obliged to remit promptly to the bank all amounts collected, but it has no obligation to the bank for slow payment or non-payment by the debtors.

In this case, the micro-entity has transferred to the bank substantially all of the risks and rewards of ownership of the receivables. Accordingly, it removes the receivables from its statement of financial position (ie derecognises them), and it shows no liability in respect of the proceeds received from the bank. The micro-entity recognises a loss calculated as the difference between the carrying amount of the receivables at the time of sale and the proceeds received from the bank. The micro-entity recognises a liability to the extent that it has collected funds from the debtors but has not yet remitted them to the bank.

Example 2: Debt factoring arrangement that does not qualify for derecognition

The facts are the same as in the preceding example except that the micro-entity has agreed to buy back from the bank any receivables for which the debtor is in arrears as to principal or interest for more than 120 days.

In this case, the micro-entity has retained the risk of slow payment or non-payment by the debtors – a significant risk with respect to receivables. Accordingly, the micro-entity does not treat the receivables as having been sold to the bank, and it does not derecognise them. Instead, it treats the proceeds from the bank as a loan. The micro-entity continues to recognise the receivables as an asset until they are collected or written off as uncollectible.

Transfers of non-cash collateral

- 9.24 When a micro-entity participates in arrangements where it provides or receives financial assets other than cash as collateral (eg a micro-entity pledges commercial papers as security against a loan), the micro-entity shall apply the requirements of paragraphs 11.35(b) to 11.35(d) of **FRS 102**.

Derecognition of a financial liability

- 9.25 A micro-entity shall derecognise a financial liability (or a part of a financial liability) only when it is extinguished – ie when the obligation specified in the contract is discharged, is cancelled or expires.
- 9.26 A micro-entity shall recognise any gain or loss on the derecognition of a financial liability (or a part of a financial liability) in profit or loss when the item is derecognised.

Presentation

- 9.27 A financial asset and a financial liability shall be offset and the net amount presented in the **statement of financial position** when, and only when, a micro-entity:
- (a) currently has a legally enforceable right to set off the recognised amounts; and
 - (b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Disclosures

- 9.28 A micro-entity shall disclose information in relation to the following items in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*:
- (a) financial commitments, guarantees and contingencies not recognised in the statement of financial position arising from financial instruments; and
 - (b) financial assets given as security in respect of its commitments, guarantees and contingencies.

Section 10 Inventories

Scope of this section

10.1 [Deleted]

10.2 This section applies to **inventories**, except:

- (a) work in progress arising under **construction contracts**, including directly related service contracts (see Section 18 *Revenue*); and
- (b) **biological assets** related to **agricultural activity** and **agricultural produce** at the point of harvest (see Section 27 *Specialised Activities*).

Measurement of inventories

10.3 A **micro-entity** shall measure inventories at the lower of cost and estimated selling price less costs to complete and sell.

Cost of inventories

10.4 A micro-entity shall include in the cost of inventories all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

10.5 Where inventories are acquired through a **non-exchange transaction**, their cost shall be measured at their **fair value** at the date of acquisition.

Costs of purchase

10.6 The costs of purchase of inventories comprise the purchase price, import duties and other taxes (other than those subsequently recoverable by the micro-entity from the taxing authorities), and transport, handling and other costs directly attributable to the acquisition of finished goods, materials and services. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase.

10.7 If payment is deferred beyond normal credit terms, the purchase price is the cash price available at the date of purchase. Any excess of the deferred payment amount over the cash price available at the date of purchase is recognised as interest and accounted for in accordance with paragraph 9.14(a).

Costs of conversion

10.8 The costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Fixed production overheads are those indirect costs of production that remain relatively constant regardless of the volume of production, such as **depreciation** and maintenance of factory buildings and equipment, and the cost of factory management and administration. Variable production overheads are those indirect costs of production that vary directly, or nearly directly, with the volume of production, such as indirect materials and indirect labour.

- 10.9 Production overheads include the costs for obligations (recognised and measured in accordance with Section 16 *Provisions and Contingencies*) for dismantling, removing and restoring a site on which an item of **property, plant and equipment** is located that are incurred during the **reporting period** as a consequence of having used that item of property, plant and equipment to produce inventory during that period.

Allocation of production overheads

- 10.10 A micro-entity shall allocate fixed production overheads to the costs of conversion on the basis of the normal capacity of the production facilities. Normal capacity is the production expected to be achieved on average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance. The actual level of production may be used if it approximates normal capacity. The amount of fixed overhead allocated to each unit of production is not increased as a consequence of low production or idle plant. Unallocated overheads are recognised as an **expense** in the period in which they are incurred. In periods of abnormally high production, the amount of fixed overhead allocated to each unit of production is decreased so that inventories are not measured above cost. Variable production overheads are allocated to each unit of production on the basis of the actual use of the production facilities.

Other costs included in inventories

- 10.11 A micro-entity shall include other costs in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

Costs excluded from inventories

- 10.12 Examples of costs excluded from the cost of inventories and recognised as expenses in the period in which they are incurred are:
- (a) abnormal amounts of wasted materials, labour or other production costs;
 - (b) storage costs, unless those costs are necessary during the production process before a further production stage;
 - (c) administrative overheads that do not contribute to bringing inventories to their present location and condition; and
 - (d) selling costs.

Cost of inventories of a service provider

- 10.13 To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel, and attributable overheads. Labour and other costs relating to sales and general administrative personnel are not included but are recognised as expenses in the period in which they are incurred. The cost of inventories of a service provider does not include profit margins or non-attributable overheads that are often factored into prices charged by service providers.

Cost of agricultural produce harvested from biological assets

- 10.14 Section 27 requires that inventories comprising agricultural produce that a micro-entity has harvested from its biological assets should be measured on initial **recognition**, at the point of harvest, at the lower of cost and estimated selling price less costs to

complete and sell. This becomes the cost of the inventories at that date for application of this section.

Techniques for measuring cost, such as standard costing, retail method and most recent purchase price

10.15 A micro-entity may use techniques such as the standard cost method, the retail method or most recent purchase price for measuring the cost of inventories if the result approximates cost. Standard costs take into account normal levels of materials and supplies, labour, efficiency and capacity utilisation. They are regularly reviewed and, if necessary, revised in the light of current conditions. The retail method measures cost by reducing the sales value of the inventory by the appropriate percentage gross margin.

Cost formulas

10.16 A micro-entity shall measure the cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects by using specific identification of their individual costs.

10.17 A micro-entity shall measure the cost of inventories, other than those dealt with in paragraph 10.16, by using the first-in, first-out (FIFO) or weighted average cost formula. A micro-entity shall use the same cost formula for all inventories having a similar nature and use to the micro-entity. For inventories with a different nature or use, different cost formulas may be justified. The last-in, first-out method (LIFO) is not permitted by this FRS.

Impairment of inventories

10.18 Implicit in the requirement for a micro-entity to measure inventories at the lower of cost and estimated selling price less costs to complete, is a requirement that a micro-entity shall assess at the end of each reporting period whether any inventories are impaired, ie the **carrying amount** is not fully recoverable (eg because of damage, obsolescence or declining selling prices). If an item (or group of items) of inventory is impaired, the micro-entity shall recognise an **impairment loss**.

10.19 When the circumstances that previously caused inventories to be impaired no longer exist or when there is clear evidence of an increase in selling price less costs to complete and sell because of changed economic circumstances, the micro-entity shall reverse the amount of the impairment (ie the reversal is limited to the amount of the original impairment loss).

Recognition as an expense

10.20 When inventories are sold, the micro-entity shall recognise the carrying amount of those inventories as an expense in the period in which the related **revenue** is recognised.

10.21 Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another **asset** in this way are accounted for subsequently in accordance with the section of this FRS relevant to that type of asset.

Disclosures

- 10.22 A micro-entity shall disclose information in relation to any items of inventory given as security in respect of its commitments, guarantees and contingencies in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*.

Section 11

Investments in Joint Ventures

Scope of this section

- 11.1 This section applies to investments in **joint ventures** that are jointly controlled operations and jointly controlled assets.
- 11.2 A **micro-entity** shall refer to Section 7 *Subsidiaries, Associates, Jointly Controlled Entities and Intermediate Payment Arrangements* which applies to investments in joint ventures that are **jointly controlled entities**.

Joint ventures defined

- 11.3 **Joint control** is the contractually agreed sharing of **control** over an economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the **venturers**).
- 11.4 A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. Joint ventures can take the form of jointly controlled operations, jointly controlled assets, or jointly controlled entities.

Jointly controlled operations

- 11.5 The operation of some joint ventures involves the use of the **assets** and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own **property, plant and equipment** and carries its own **inventories**. It also incurs its own **expenses** and **liabilities** and raises its own finance, which represent its own obligations. The joint venture activities may be carried out by the venturer's employees alongside the venturer's similar activities. The joint venture agreement usually provides a means by which the **revenue** from the sale of the joint product and any expenses incurred in common are shared among the venturers.
- 11.6 In respect of its interests in jointly controlled operations, a venturer shall recognise in its **financial statements**:
- (a) the assets that it controls and the liabilities that it incurs; and
 - (b) the expenses that it incurs and its share of the **income** that it earns from the sale of goods or services by the joint venture.

Jointly controlled assets

- 11.7 Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture.
- 11.8 In respect of its interest in a jointly controlled asset, a venturer shall recognise in its financial statements:
- (a) its share of the jointly controlled assets, classified in accordance with the format adopted set out in Section 4 *Statement of Financial Position*;
 - (b) any liabilities that it has incurred;

- (c) its share of any liabilities incurred jointly with the other venturers in relation to the joint venture;
- (d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and
- (e) any expenses that it has incurred in respect of its interest in the joint venture.

Disclosures

- 11.9 A micro-entity shall disclose information in relation to financial commitments, guarantees and contingencies not recognised in the **statement of financial position** arising from its jointly controlled operations and jointly controlled assets in accordance with the relevant appendix in Section 6 *Notes to the Financial Statements*.

Section 12

Property, Plant and Equipment and Investment Property

Scope of this section

- 12.1 This section applies to **property, plant and equipment** and **investment property**.
- 12.2 Property, plant and equipment does not include **biological assets** related to **agricultural activity** (see Section 27 *Specialised Activities*).

Recognition

- 12.3 A **micro-entity** shall recognise the cost of an item of property, plant and equipment or investment property as an **asset** if, and only if:
- (a) it is **probable** that future economic benefits associated with the item will flow to the micro-entity; and
 - (b) the cost of the item can be measured reliably.
- 12.4 Items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this section when they meet the definition of property, plant and equipment. Otherwise, such items are classified as **inventory**.
- 12.5 Parts of some items of property, plant and equipment or investment property may require replacement at regular intervals (eg the roof of a building). A micro-entity shall add to the **carrying amount** of an item of property, plant and equipment or investment property the cost of replacing part of such an item when that cost is incurred if the replacement part is expected to provide incremental future benefits to the micro-entity. The carrying amount of those parts that are replaced is derecognised in accordance with paragraphs 12.26 and 12.27 regardless of whether the replaced parts had been depreciated separately. If it is **impracticable** for an entity to identify the carrying amount of the replaced part, it may be estimated using the current cost of the replacement part as a proxy for the original cost of the replaced part and adjusting it for **depreciation** and impairments.
- 12.6 A condition of continuing to operate an item of property, plant and equipment (eg a bus) or investment property may be performing regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant and equipment or investment property as a replacement if the **recognition** criteria are satisfied. Any remaining carrying amount of the cost of the previous major inspection (as distinct from physical parts) is derecognised. This is done regardless of whether the cost of the previous major inspection was identified in the transaction in which the item was acquired or constructed. If necessary, the estimated cost of a future similar inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed.
- 12.7 Land and buildings are separable assets, and a micro-entity shall account for them separately, even when they are acquired together.

Initial measurement

- 12.8 A micro-entity shall measure an item of property, plant and equipment or investment property at initial recognition at its cost.

Elements of cost

- 12.9 The cost of an item of property, plant and equipment or investment property comprises all of the following:
- (a) Its purchase price, including legal and brokerage fees, import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
 - (b) Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These can include the costs of site preparation, initial delivery and handling, installation and assembly, and testing of functionality.
 - (c) The initial estimate of the costs, recognised and measured in accordance with Section 16 *Provisions and Contingencies*, of dismantling and removing the item and restoring the site on which it is located, the obligation for which a micro-entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.
- 12.10 The following costs are not costs of an item of property, plant and equipment or investment property, and a micro-entity shall recognise them as an **expense** when they are incurred:
- (a) costs of opening a new facility;
 - (b) costs of introducing a new product or service (including costs of advertising and promotional activities);
 - (c) costs of conducting business in a new location or with a new class of customer (including costs of staff training); and
 - (d) administration and other general overhead costs.
- 12.11 The **income** and related expenses of incidental operations during construction or development of an item of property, plant and equipment or investment property are recognised in **profit or loss** if those operations are not necessary to bring the item to its intended location and operating condition.

Measurement of cost

- 12.12 The cost of an item of property, plant and equipment or investment property is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the cost is the cash price available at the recognition date. Any excess of the deferred payment amount over the cash price available at the recognition date is recognised as interest and accounted for in accordance with paragraph 9.14(a).

Exchanges of assets

- 12.13 An item of property, plant or equipment or investment property may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. A micro-entity shall measure the cost of the acquired asset at **fair value** unless:
- (a) the exchange transaction lacks commercial substance; or
 - (b) the fair value of neither the asset received nor the asset given up is reliably measurable. In that case, the asset's cost is measured at the carrying amount of the asset given up.

Subsequent measurement

- 12.14 A micro-entity shall measure all items of property, plant and equipment and investment property after initial recognition at cost less any accumulated depreciation and any accumulated **impairment losses**. A micro-entity shall recognise the costs of day-to-day servicing of an item of property, plant and equipment or investment property in profit or loss in the period in which the costs are incurred.

Depreciation

- 12.15 If the major components of an item of property, plant and equipment or investment property have significantly different patterns of consumption of economic benefits, a micro-entity shall allocate the initial cost of the asset to its major components and depreciate each such component separately over its **useful life**. Other assets shall be depreciated over their useful lives as a single asset. There are some exceptions, such as land which generally has an unlimited useful life and therefore is not usually depreciated.
- 12.16 The depreciation charge for each period shall be recognised in profit or loss unless another section of this FRS requires the cost to be recognised as part of the cost of an asset. For example, the depreciation of manufacturing property, plant and equipment is included in the costs of inventories (see Section 10 *Inventories*).

Depreciable amount and depreciation period

- 12.17 A micro-entity shall allocate the **depreciable amount** of an asset on a systematic basis over its useful life.
- 12.18 Factors may indicate that the **residual value** or useful life of an asset has changed since the most recent annual **reporting date**. If such indicators are present, a micro-entity shall review its previous estimates and, if current expectations differ, amend the residual value, depreciation method or useful life. The micro-entity shall account for the change in residual value, depreciation method or useful life as a change in an accounting estimate in accordance with paragraphs 8.11 to 8.13.
- 12.19 Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases when the asset is derecognised. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.
- 12.20 A micro-entity shall consider all the following factors in determining the useful life of an asset:
- (a) The expected usage of the asset. Usage is assessed by reference to the asset's expected capacity or physical output.
 - (b) Expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle.
 - (c) Technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset.
 - (d) Legal or similar limits on the use of the asset, such as the expiry dates of related **leases**.

Depreciation method

- 12.21 A micro-entity shall select a depreciation method that reflects the pattern in which it expects to consume the asset's future economic benefits. The possible depreciation methods include the straight-line method, the diminishing balance method and a method based on usage such as the units of production method.
- 12.22 If there is an indication that there has been a significant change since the last annual reporting date in the pattern by which a micro-entity expects to consume an asset's future economic benefits, the micro-entity shall review its present depreciation method and, if current expectations differ, change the depreciation method to reflect the new pattern. The micro-entity shall account for the change as a change in an accounting estimate in accordance with paragraphs 8.11 to 8.13.

Impairment

Recognition and measurement of impairment

- 12.23 At each reporting date, a micro-entity shall apply Section 22 *Impairment of Assets* to determine whether an item or group of items of property, plant and equipment or investment property is impaired and, if so, how to recognise and measure the impairment loss. That section explains when and how a micro-entity reviews the carrying amount of its assets, how it determines the **recoverable amount** of an asset, and when it recognises or reverses an impairment loss.

Compensation for impairment

- 12.24 An entity shall include in profit or loss, compensation from third parties for items of property, plant and equipment or investment property that were impaired, lost or given up only when the compensation is virtually certain.

Property, plant and equipment or investment property held for sale

- 12.25 Paragraph 22.7(f) states that a plan to dispose of an asset before the previously expected date is an indicator of impairment that triggers the calculation of the asset's recoverable amount for the purpose of determining whether the asset is impaired.

Derecognition

- 12.26 A micro-entity shall **derecognise** an item of property, plant and equipment or investment property:
- (a) on disposal; or
 - (b) when no future economic benefits are expected from its use or disposal.
- 12.27 A micro-entity shall recognise the **gain** or loss on the **derecognition** of an item of property, plant and equipment or investment property in profit or loss when the item is derecognised (unless Section 15 *Leases* requires otherwise on a sale and leaseback). The micro-entity shall not classify such gains as **turnover** in the **income statement**.

Disclosures

- 12.28 A micro-entity shall disclose information in relation to the following items in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*:
- (a) financial commitments not recognised in the **statement of financial position** for the acquisition of property, plant and equipment or investment property; and
 - (b) items of property, plant and equipment or investment property given as security in respect of its commitments, guarantees and contingencies.

Section 13

Intangible Assets other than Goodwill

Scope of this section

- 13.1 This section applies to separately acquired **intangible assets** and internally generated intangible assets. This section does not apply to intangible assets held by a **micro-entity** for sale in the ordinary course of business (see Section 10 *Inventories* and Section 18 *Revenue*).
- 13.2 For the accounting of intangible assets acquired as part of a **business combination** including **goodwill** see Section 14 *Business Combinations and Goodwill*.

Recognition

- 13.3 A micro-entity shall recognise all separately acquired intangible assets.
- 13.4 An internally generated intangible shall not be recognised as an **asset**. All expenditure incurred shall be recognised as an **expense** immediately in **profit or loss**.
- 13.5 A micro-entity shall recognise the expenditure on the following items as an expense and shall not recognise such expenditure as intangible assets (the list is not exhaustive):
- (a) Expenditure on **research** and **development** activities.
 - (b) Internally generated brands, logos, publishing titles, customer lists and items similar in substance.
 - (c) Start-up activities (ie start-up costs), which include establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or **business** (ie pre-opening costs) and expenditure for starting new operations or launching new products or processes (ie pre-operating costs).
 - (d) Training activities.
 - (e) Advertising and promotional activities.
 - (f) Relocating or reorganising part or all of a micro-entity.
 - (g) Internally generated goodwill.

Initial measurement

- 13.6 A micro-entity shall measure a separately acquired intangible asset initially at cost which comprises:
- (a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
 - (b) any directly attributable cost of preparing the asset for its intended use.

Exchanges of assets

- 13.7 An intangible asset may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. A micro-entity shall measure the cost of such an intangible asset at **fair value** unless:
- (a) the exchange transaction lacks commercial substance; or

- (b) the fair value of neither the asset received nor the asset given up is reliably measurable. In that case, the asset's cost is measured at the **carrying amount** of the asset given up.

Subsequent measurement

- 13.8 A micro-entity shall measure a separately acquired intangible asset after initial **recognition** at cost less any accumulated **amortisation** and any accumulated **impairment losses**. The requirements for amortisation are set out in paragraphs 13.9 to 13.14.

Amortisation over useful life

- 13.9 Intangible assets shall be considered to have a finite **useful life**. The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the micro-entity expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the micro-entity without significant cost.
- 13.10 If, in exceptional cases, a micro-entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall not exceed ten years.

Amortisation period and amortisation method

- 13.11 A micro-entity shall allocate the **depreciable amount** of an intangible asset on a systematic basis over its useful life. The amortisation charge for each period shall be recognised in profit or loss, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset. For example, the amortisation of an intangible asset may be included in the costs of **inventories** or **property, plant and equipment**.
- 13.12 Amortisation begins when the intangible asset is available for use, ie when it is in the location and condition necessary for it to be usable in the manner intended by management. Amortisation ceases when the asset is derecognised. The micro-entity shall choose an amortisation method that reflects the pattern in which it expects to consume the asset's future economic benefits. If the micro-entity cannot determine that pattern reliably, it shall use the straight-line method.

Residual value

- 13.13 A micro-entity shall assume that the **residual value** of an intangible asset is zero unless:
- (a) there is a commitment by a third party to purchase the asset at the end of its useful life; or
 - (b) there is an **active market** for the asset and:
 - (i) residual value can be determined by reference to that market; and
 - (ii) it is **probable** that such a market will exist at the end of the asset's useful life.

Review of amortisation period and amortisation method

- 13.14 Factors may indicate that the residual value or useful life of an intangible asset has changed since the most recent annual **reporting date**. If such indicators are present, a

micro-entity shall review its previous estimates and, if current expectations differ, amend the residual value, amortisation method or useful life. The micro-entity shall account for the change in residual value, amortisation method or useful life as a change in an accounting estimate in accordance with paragraphs 8.11 to 8.13.

Recoverability of the carrying amount—impairment losses

13.15 To determine whether a separately acquired intangible asset is impaired, a micro-entity shall apply Section 22 *Impairment of Assets*. That section explains when and how a micro-entity reviews the carrying amount of its assets, how it determines the **recoverable amount** of an asset, and when it recognises or reverses an impairment loss.

Retirements and disposals

13.16 A micro-entity shall derecognise a separately acquired intangible asset, and shall recognise a **gain** or loss in profit or loss:

- (a) on disposal; or
- (b) when no future economic benefits are expected from its use or disposal.

Disclosures

13.17 A micro-entity shall disclose information in relation to the following items in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*:

- (a) financial commitments, guarantees and contingencies not recognised in the **statement of financial position** for the acquisition of separately acquired intangible assets; and
- (b) intangible assets given as security in respect of its commitments, guarantees and contingencies.

Section 14

Business Combinations and Goodwill

Accounting for a trade and asset acquisition

- 14.1 When a **micro-entity** effects a **business combination** by acquiring the trade and **assets** of another **business**, it shall apply Section 19 *Business Combinations and Goodwill* of **FRS 102**, except for the following:
- (a) a micro-entity shall not separately identify and recognise **intangible assets**;
 - (b) a micro-entity shall not recognise a **deferred tax asset** or **liability**;
 - (c) a micro-entity shall not apply paragraph 19.23 of FRS 102, but instead apply paragraph 14.2 of this FRS;
 - (d) a micro-entity shall not recognise and measure a **share-based payment transaction** in accordance with Section 26 *Share-based Payment* of FRS 102, but instead apply Section 21 *Share-based Payment* of this FRS;
 - (e) a micro-entity shall not recognise and measure a liability (or asset, if any) related to the acquired business's **employee benefits** arrangements in accordance with Section 28 *Employee Benefit* of FRS 102, but instead apply Section 23 *Employee Benefits* of this FRS; and
 - (f) a micro-entity is not required to provide any of the disclosures.

Goodwill arising on a trade and asset acquisition

- 14.2 Where a micro-entity has recognised **goodwill** acquired in a trade and asset acquisition (in accordance with paragraph 19.22 of FRS 102), the micro-entity shall measure that goodwill at cost less accumulated **amortisation** and accumulated **impairment losses**:
- (a) A micro-entity shall follow the principles in paragraphs 13.9 to 13.14 of this FRS for amortisation of goodwill. Goodwill shall be considered to have a finite **useful life**, and shall be amortised on a systematic basis over its life. If, in exceptional cases, a micro-entity is unable to make a reliable estimate of the useful life of goodwill, the life shall not exceed 10 years.
 - (b) A micro-entity shall follow Section 22 *Impairment of Assets* of this FRS for recognising and measuring the impairment of goodwill.

Disclosures

- 14.3 A micro-entity shall disclose information in relation to financial commitments, guarantees and contingencies not recognised in the **statement of financial position** for trade and asset acquisitions in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*.
- 14.4 An Irish micro-entity shall disclose information in relation to goodwill acquired in accordance with Appendix B to Section 6.

Section 15

Leases

Scope of this section

- 15.1 This section applies to **leases** except for licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights (see Section 13 *Intangible Assets other than Goodwill*).
- 15.2 This section applies to agreements that transfer the right to use **assets** even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. This section does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.
- 15.3 Some arrangements do not take the legal form of a lease but convey rights to use assets in return for payments. Examples of such arrangements may include outsourcing arrangements, telecommunication contracts that provide rights to capacity and take-or-pay contracts.
- 15.4 Determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement.

Classification of leases

- 15.5 A lease is classified as a **finance lease** if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an **operating lease** if it does not transfer substantially all the risks and rewards incidental to ownership.
- 15.6 Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:
- (a) the lease transfers ownership of the asset to the lessee by the end of the **lease term**;
 - (b) the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the **fair value** at the date the option becomes exercisable for it to be reasonably certain, at the **inception of the lease**, that the option will be exercised;
 - (c) the lease term is for the major part of the economic life of the asset even if title is not transferred;
 - (d) at the inception of the lease the **present value** of the **minimum lease payments** amounts to at least substantially all of the fair value of the leased asset; and
 - (e) the leased assets are of such a specialised nature that only the lessee can use them without major modifications.
- 15.7 Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease are:
- (a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;

- (b) **gains** or losses from the fluctuation in the **residual value** of the leased asset accrue to the lessee (eg in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and
 - (c) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.
- 15.8 The examples and indicators in paragraphs 15.6 and 15.7 are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. For example, this may be the case if ownership of the asset is transferred to the lessee at the end of the lease for a variable payment equal to the asset's then fair value, or if there are **contingent rents**, as a result of which the lessee does not have substantially all risks and rewards incidental to ownership.
- 15.9 Lease classification is made at the inception of the lease and is not changed during the term of the lease unless the lessee and the lessor agree to change the provisions of the lease (other than simply by renewing the lease), in which case the lease classification shall be re-evaluated.

Financial statements of lessees: finance leases

Initial recognition and measurement

- 15.10 At the **commencement of the lease term**, a lessee shall recognise its rights of use and obligations under finance leases as assets and **liabilities** in its **statement of financial position** at amounts equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments, determined at the inception of the lease. Any initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognised as an asset.
- 15.11 The present value of the minimum lease payments shall be calculated using the **interest rate implicit in the lease**. If this cannot be determined, the **lessee's incremental borrowing rate** shall be used.

Subsequent measurement

- 15.12 A lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability. The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. A lessee shall charge contingent rents as **expenses** in the periods in which they are incurred.
- 15.13 A lessee shall depreciate an asset leased under a finance lease in accordance with Section 12 *Property, Plant and Equipment and Investment Property* and Section 13 *Intangible Assets other than Goodwill*. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its **useful life**. A lessee shall also assess at each **reporting date** whether an asset leased under a finance lease is impaired (see Section 22 *Impairment of Assets*).

Financial statements of lessees: operating leases

Recognition and measurement

- 15.14 A lessee shall recognise lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense over the lease term on a

straight-line basis unless another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis.

- 15.15 A lessee shall recognise the aggregate benefit of **lease incentives** as a reduction to the expense recognised in accordance with paragraph 15.14 over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern of the lessee's benefit from the use of the leased asset. Any costs incurred by the lessee (for example, costs for termination of a pre-existing lease, relocation or leasehold improvements) shall be accounted for in accordance with the applicable section.
- 15.16 Where an operating lease becomes an **onerous contract** a **micro-entity** shall also apply Section 16 *Provisions and Contingencies*.

Disclosures

- 15.17 A micro-entity shall disclose information in relation to financial commitments, guarantees and contingencies not recognised in the statement of financial position arising from operating leases in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*.

Financial statements of lessors: finance leases

Initial recognition and measurement

- 15.18 A lessor shall recognise assets held under a finance lease in its statement of financial position and present them as a receivable at an amount equal to the **net investment in the lease**. The net investment in a lease is the lessor's **gross investment in the lease** discounted at the interest rate implicit in the lease. The gross investment in the lease is the aggregate of:
- (a) the minimum lease payments receivable by the lessor under a finance lease; and
 - (b) any unguaranteed residual value accruing to the lessor.
- 15.19 For finance leases other than those involving manufacturer or dealer lessors, initial direct costs (costs that are incremental and directly attributable to negotiating and arranging a lease) are included in the initial measurement of the finance lease receivable and reduce the amount of **income** recognised over the lease term.

Subsequent measurement

- 15.20 The **recognition** of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease. Lease payments relating to the period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance income. If there is an indication that the estimated unguaranteed residual value used in computing the lessor's gross investment in the lease has changed significantly, the income allocation over the lease term is revised, and any reduction in respect of amounts accrued is recognised immediately in **profit or loss**.

Manufacturer or dealer lessors

- 15.21 Manufacturers or dealers often offer to customers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:

- (a) profit or loss equivalent to the profit or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and
- (b) finance income over the lease term.

15.22 The sales **revenue** recognised at the commencement of the lease term by a manufacturer or dealer lessor is the fair value of the asset or, if lower, the present value of the minimum lease payments accruing to the lessor, computed at a market rate of interest. The cost of sale recognised at the commencement of the lease term is the cost, or **carrying amount** if different, of the leased asset less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the selling profit, which is recognised in accordance with the micro-entity's policy for outright sales.

15.23 If artificially low rates of interest are quoted, selling profit shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognised as an expense when the selling profit is recognised.

Financial statements of lessors: operating leases

Recognition and measurement

15.24 A lessor shall recognise lease income from operating leases (excluding amounts for services such as insurance and maintenance) in profit or loss on a straight-line basis over the lease term unless another systematic basis is representative of the time pattern of the lessee's benefit from the leased asset, even if the receipt of payments is not on that basis.

15.25 A lessor shall recognise the aggregate cost of lease incentives as a reduction to the income recognised in accordance with paragraph 15.24 over the lease term on a straight-line basis, unless another systematic basis is representative of the time pattern over which the lessor's benefit from the leased asset is diminished.

15.26 A lessor shall recognise as an expense, costs, including **depreciation**, incurred in earning the lease income. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets.

15.27 A lessor shall add to the carrying amount of the leased asset any initial direct costs it incurs in negotiating and arranging an operating lease and shall recognise such costs as an expense over the lease term on the same basis as the lease income.

15.28 To determine whether a leased asset has become impaired, a lessor shall apply Section 22.

15.29 A manufacturer or dealer lessor does not recognise any selling profit on entering into an operating lease because it is not the equivalent of a sale.

Sale and leaseback transactions

15.30 A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends on the type of lease.

Sale and leaseback transaction results in a finance lease

- 15.31 If a sale and leaseback transaction results in a finance lease, the seller-lessee shall not recognise immediately, as income, any excess of sales proceeds over the carrying amount. Instead, the seller-lessee shall defer such excess and amortise it over the lease term.

Sale and leaseback transaction results in an operating lease

- 15.32 If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, the seller-lessee shall recognise any profit or loss immediately. If the sale price is below fair value, the seller-lessee shall recognise any profit or loss immediately unless the loss is compensated for by future lease payments at below market price. In that case the seller-lessee shall defer and amortise such loss in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the seller-lessee shall defer the excess over fair value and amortise it over the period for which the asset is expected to be used.

Disclosures

- 15.33 A micro-entity shall disclose information in relation to financial commitments, guarantees and contingencies not recognised in the statement of financial position arising from a sale and lease back transaction in accordance with the relevant appendix to Section 6.

Section 16

Provisions and Contingencies

Scope of this section

- 16.1 This section applies to **provisions, contingent liabilities** and **contingent assets** except for provisions covered by other sections of this FRS. Where those other sections contain no specific requirements to deal with contracts that have become onerous, this section applies to those contracts.
- 16.2 This section does not apply to **financial instruments** that are within the scope of Section 9 *Financial Instruments* unless the contracts are **onerous contracts** or **financial guarantee contracts**.
- 16.3 The requirements in this section do not apply to executory contracts unless they are onerous contracts. Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.
- 16.4 The word 'provision' is sometimes used in the context of such items as **depreciation**, impairment of **assets**, and uncollectible receivables. Those are adjustments of the **carrying amounts** of assets, rather than **recognition of liabilities**, and therefore are not covered by this section.

Initial recognition

- 16.5 A **micro-entity** shall recognise a provision only when:
- (a) the micro-entity has an obligation at the **reporting date** as a result of a past event;
 - (b) it is **probable** (ie more likely than not) that the micro-entity will be required to transfer economic benefits in settlement; and
 - (c) the amount of the obligation can be estimated reliably.
- 16.6 The micro-entity shall recognise the provision as a liability in the **statement of financial position** and shall recognise the amount of the provision as an **expense**, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset such as **inventories** or **property, plant and equipment**.
- 16.7 The condition in paragraph 16.5(a) means that the micro-entity has no realistic alternative to settling the obligation. This can happen when the micro-entity has a legal obligation that can be enforced by law or when the micro-entity has a **constructive obligation** because the past event (which may be an action of the micro-entity) has created valid expectations in other parties that the micro-entity will discharge the obligation. Obligations that will arise from the micro-entity's future actions (ie the future conduct of its **business**) do not satisfy the condition in paragraph 16.5(a), no matter how likely they are to occur and even if they are contractual. To illustrate, because of commercial pressures or legal requirements, a micro-entity may intend or need to carry out expenditure to operate in a particular way in the future (for example, by fitting smoke filters in a particular type of factory). Because the micro-entity can avoid the future expenditure by its future actions, for example, by changing its method of operation or selling the factory, it has no present obligation for that future expenditure and no provision is recognised.

Initial measurement

- 16.8 A micro-entity shall measure a provision at the best estimate of the amount required to settle the obligation at the reporting date. The best estimate is the amount a micro-entity would rationally pay to settle the obligation at the end of the **reporting period** or to transfer it to a third party at that time.
- (a) When the provision involves a large population of items, the estimate of the amount reflects the weighting of all possible outcomes by their associated probabilities. Where there is a continuous range of possible outcomes, and each point in that range is as likely as any other, the mid-point of the range is used.
 - (b) When the provision arises from a single obligation, the individual most likely outcome may be the best estimate of the amount required to settle the obligation. However, even in such a case, the micro-entity considers other possible outcomes. When other possible outcomes are either mostly higher or mostly lower than the most likely outcome, the best estimate will be a higher or lower amount.

When the effect of the time value of money is **material**, the amount of a provision shall be the **present value** of the amount expected to be required to settle the obligation. The discount rate (or rates) shall be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and risks specific to the liability. The risks specific to the liability shall be reflected either in the discount rate or in the estimation of the amounts required to settle the obligation, but not both.

- 16.9 A micro-entity shall exclude **gains** from the expected disposal of assets from the **measurement** of a provision.
- 16.10 When some or all of the amount required to settle a provision may be reimbursed by another party (eg through an insurance claim), the micro-entity shall recognise the reimbursement as a separate asset only when it is virtually certain that the micro-entity will receive the reimbursement on settlement of the obligation. The amount recognised for the reimbursement shall not exceed the amount of the provision. The reimbursement receivable shall be presented in the statement of financial position as an asset and shall not be offset against the provision. In the **income statement** the expense relating to a provision may be presented net of the amount recognised for a reimbursement.

Subsequent measurement

- 16.11 A micro-entity shall charge against a provision only those expenditures for which the provision was originally recognised.
- 16.12 A micro-entity shall review provisions at each reporting date and adjust them to reflect the current best estimate of the amount that would be required to settle the obligation at that reporting date. Any adjustments to the amounts previously recognised shall be recognised in **profit or loss** unless the provision was originally recognised as part of the cost of an asset (see paragraph 16.6). When a provision is measured at the present value of the amount expected to be required to settle the obligation, the unwinding of the discount shall be recognised as interest expense in profit or loss in the period it arises.

Onerous contracts

- 16.13 If a micro-entity has an onerous contract, the present obligation under the contract shall be recognised and measured as a provision (see Example 2 of the appendix to this section).

Future operating losses

- 16.14 Provisions shall not be recognised for future operating losses (see Example 1 of the appendix to this section).

Restructuring

- 16.15 A **restructuring** gives rise to a constructive obligation only when a micro-entity:
- (a) has a detailed formal plan for the restructuring identifying at least:
 - (i) the business or part of a business concerned;
 - (ii) the principal locations affected;
 - (iii) the location, function, and approximate number of employees who will be compensated for terminating their services;
 - (iv) the expenditures that will be undertaken; and
 - (v) when the plan will be implemented; and
 - (b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.
- 16.16 A micro-entity recognises a provision for restructuring costs only when it has a legal or constructive obligation at the reporting date to carry out the restructuring.

Contingent liabilities

- 16.17 A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 16.5. A micro-entity shall not recognise a contingent liability as a liability, except for provisions for contingent liabilities of an acquiree in a trade and asset acquisition (see Section 14 *Business Combinations and Goodwill*). Paragraph 16.19 sets out the disclosure requirements for a contingent liability. When a micro-entity is jointly and severally liable for an obligation, the part of the obligation that is expected to be met by other parties is treated as a contingent liability.

Contingent assets

- 16.18 A micro-entity shall not recognise a contingent asset as an asset. However, when the flow of future economic benefits to the micro-entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Disclosures

- 16.19 A micro-entity shall disclose information in relation to financial commitments, guarantees and contingencies not recognised in the statement of financial position in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*. A micro-entity is not required to disclose the amount of a contingent liability when the possibility of an outflow of resources is remote.

Appendix to Section 16

Examples of recognising and measuring provisions

This appendix accompanies, but is not part of, Section 16. It provides guidance for applying the requirements of Section 16 in recognising and measuring provisions.

All of the micro-entities in the examples in this appendix have 31 December as their reporting date. In all cases, it is assumed that a reliable estimate can be made of any outflows expected. In some examples the circumstances described may have resulted in impairment of the assets; this aspect is not dealt with in the examples. References to 'best estimate' are to the present value amount, when the effect of the time value of money is material.

Example 1 Future operating losses

16A.1 A micro-entity determines that it is probable that it will incur future operating losses for several years.

Present obligation as a result of a past obligating event: There is no past event that obliges the micro-entity to pay out resources.

Conclusion: The micro-entity does not recognise a provision for future operating losses. Expected future losses do not meet the definition of a liability. The expectation of future operating losses may be an indicator that one or more assets are impaired (see Section 22 *Impairment of Assets* of this FRS).

Example 2 Onerous contracts

16A.2 An onerous contract is one in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. For example, a micro-entity may be contractually required under an operating lease to make payments to lease an asset for which it no longer has any use.

Present obligation as a result of a past obligating event: The micro-entity is contractually required to pay out resources for which it will not receive commensurate benefits.

Conclusion: If a micro-entity has a contract that is onerous, the micro-entity recognises and measures the present obligation under the contract as a provision.

Example 3 Warranties

16A.3 A manufacturer gives warranties at the time of sale to purchasers of its product. Under the terms of the contract for sale, the manufacturer undertakes to make good, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale. On the basis of experience, it is probable (ie more likely than not) that there will be some claims under the warranties.

Present obligation as a result of a past obligating event: The obligating event is the sale of the product with a warranty, which gives rise to a legal obligation.

An outflow of resources embodying economic benefits in settlement: Probable for the warranties as a whole.

Conclusion: The micro-entity recognises a provision for the best estimate of the costs of making good under the warranty products sold before the reporting date.

Illustration of calculations:

In 20X0, goods are sold for CU100,000. Experience indicates that 90 per cent of products sold require no warranty repairs; 6 per cent of products sold require minor repairs costing 30 per cent of the sale price; and 4 per cent of products sold require major repairs or replacement costing 70 per cent of sale price. Therefore estimated warranty costs are:

CU100,000 × 90% × 0 =	CU0
CU100,000 × 6% × 30% =	CU1,800
CU100,000 × 4% × 70% =	CU2,800
Total	CU4,600

The expenditures for warranty repairs and replacements for products sold in 20X0 are expected to be made 60 per cent in 20X1, 30 per cent in 20X2, and 10 per cent in 20X3, in each case at the end of the period. Because the estimated cash flows already reflect the probabilities of the cash outflows, and assuming there are no other risks or uncertainties that must be reflected, to determine the present value of those cash flows the micro-entity uses a 'risk-free' discount rate based on government bonds with the same term as the expected cash outflows (6 per cent for one-year bonds and 7 per cent for two-year and three-year bonds). Calculation of the present value, at the end of 20X0, of the estimated cash flows related to the warranties for products sold in 20X0 is as follows:

Year		Expected cash payments (CU)	Discount rate	Discount factor	Present value (CU)
1	60% × CU4,600	2,760	6%	0.9434 (at 6% for 1 year)	2,604
2	30% × CU4,600	1,380	7%	0.8734 (at 7% for 2 years)	1,205
3	10% × CU4,600	460	7%	0.8163 (at 7% for 3 years)	375
Total					4,184

The micro-entity will recognise a warranty obligation of CU4,184 at the end of 20X0 for products sold in 20X0.

Example 4 Refunds policy

16A.4 A retail store has a policy of refunding purchases by dissatisfied customers, even though it is under no legal obligation to do so. Its policy of making refunds is generally known.

Present obligation as a result of a past obligating event: The obligating event is the sale of the product, which gives rise to a constructive obligation because the conduct of the

store has created a valid expectation on the part of its customers that the store will refund purchases.

An outflow of resources embodying economic benefits in settlement: Probable that a proportion of goods will be returned for refund.

Conclusion: The micro-entity recognises a provision for the best estimate of the amount required to settle the refunds.

Example 5 Closure of a division: no implementation before end of reporting period

16A.5 On 12 December 20X0 the board of a micro-entity decided to close down a division. Before the end of the reporting period (31 December 20X0) the decision was not communicated to any of those affected and no other steps were taken to implement the decision.

Present obligation as a result of a past obligating event: There has been no obligating event, and so there is no obligation.

Conclusion: The micro-entity does not recognise a provision.

Example 6 Closure of a division: communication and implementation before end of reporting period

16A.6 On 12 December 20X0 the board of a micro-entity decided to close a division making a particular product. On 20 December 20X0 a detailed plan for closing the division was agreed by the board, letters were sent to customers warning them to seek an alternative source of supply, and redundancy notices were sent to the staff of the division.

Present obligation as a result of a past obligating event: The obligating event is the communication of the decision to the customers and employees, which gives rise to a constructive obligation from that date, because it creates a valid expectation that the division will be closed.

An outflow of resources embodying economic benefits in settlement: Probable.

Conclusion: The micro-entity recognises a provision at 31 December 20X0 for the best estimate of the costs that would be incurred to close the division at the reporting date.

Example 7 Staff retraining as a result of changes in the income tax system

16A.7 The government introduces changes to the income tax system. As a result of those changes, a micro-entity will need to retrain a large proportion of its administrative and sales workforce in order to ensure continued compliance with tax regulations. At the end of the reporting period, no retraining of staff has taken place.

Present obligation as a result of a past obligating event: The tax law change does not impose an obligation on a micro-entity to do any retraining. An obligating event for recognising a provision (the retraining itself) has not taken place.

Conclusion: The micro-entity does not recognise a provision.

Example 8 A court case

16A.8 A customer has sued Micro-entity X, seeking damages for injury the customer allegedly sustained from using a product sold by Micro-entity X. Micro-entity X disputes liability on grounds that the customer did not follow directions in using the product. Up to the

date the financial statements for the year to 31 December 20X1 were authorised for issue, the micro-entity's lawyers advise that it is probable that the micro-entity will not be found liable. However, when the micro-entity prepares the financial statements for the year to 31 December 20X2, its lawyers advise that, owing to developments in the case, it is now probable that the micro-entity will be found liable.

(a) At 31 December 20X1

Present obligation as a result of a past obligating event: On the basis of the evidence available when the financial statements were approved, there is no obligation as a result of past events.

Conclusion: No provision is recognised, but the micro-entity shall make the disclosures required by paragraph 16.19.

(b) At 31 December 20X2

Present obligation as a result of a past obligating event: On the basis of the evidence available, there is a present obligation. The obligating event is the sale of the product to the customer.

An outflow of resources embodying economic benefits in settlement: Probable.

Conclusion: A provision is recognised at the best estimate of the amount to settle the obligation at 31 December 20X2, and the expense is recognised in profit or loss. It is not a correction of an error in 20X1 because, on the basis of the evidence available when the 20X1 financial statements were approved, a provision should not have been recognised at that time.

Section 17

Liabilities and Equity

Scope of this section

- 17.1 This section sets out the requirements for:
- (a) classifying **financial instruments** as either **liabilities** or **equity**;
 - (b) the accounting for **compound financial instruments**, such as convertible debt; and
 - (c) the issue of equity instruments, distributions to individuals or other parties acting in their capacity as investors in equity instruments (ie in their capacity as **owners**) and the accounting for purchases of own equity.
- 17.2 This section applies to financial instruments except:
- (a) Investments in **subsidiaries** and **associates** and interests in **jointly controlled entities** (see Section 7 *Subsidiaries, Associates, Jointly Controlled Entities and Intermediate Payment Arrangements*).
 - (b) Employers' rights and obligations under employee benefit plans (see Section 23 *Employee Benefits*).
 - (c) Financial instruments, contracts and obligations under **share-based payment transactions** (see Section 21 *Share-based Payment*), except that paragraph 17.14 shall be applied to **treasury shares** issued, purchased, sold, transferred or cancelled in connection with employee share option plans, employee share purchase plans, and all other **share-based payment arrangements**.
 - (d) **Financial guarantee contracts** (see Section 16 *Provisions and Contingencies*).

Classification of an instrument as liability or equity

- 17.3 Equity is the residual interest in the **assets** of a **micro-entity** after deducting all its liabilities. Equity includes investments by the owners of the micro-entity, plus additions to those investments earned through profitable operations and retained for use in the micro-entity's operations, minus reductions to owners' investments as a result of unprofitable operations and distributions to owners.
- 17.4 A financial instrument is classified as equity where the issuer can be required to settle an obligation in cash or by delivery of another **financial asset** (or otherwise to settle it in such a way that it would be a **financial liability**) only in the event of the liquidation of the issuer.
- 17.5 A financial instrument is a financial liability of the issuer where the issuer does not have an unconditional right to avoid settling an obligation in cash or by delivery of another financial asset (or otherwise to settle it in such a way that it would be a financial liability), other than for the reason described in paragraph 17.4.
- 17.6 Examples of instruments and their classification as equity or liabilities are set out below:
- (a) An instrument is classified as equity if the only payment holders of the instruments are entitled to receive is a pro rata share of the net assets of the micro-entity on liquidation.
 - (b) An instrument is classified as a liability if it obliges the micro-entity to make payments to the holder before liquidation, such as a mandatory dividend.

- (c) A preference share that provides for mandatory redemption by the issuer for a fixed or determinable amount at a fixed or determinable future date, or gives the holder the right to require the issuer to redeem the instrument at or after a particular date for a fixed or determinable amount, is a financial liability.

Original issue of shares or other equity instruments

- 17.7 A micro-entity shall recognise the issue of shares or other equity instruments as equity when it issues those instruments and another party is obliged to provide cash or other resources to the micro-entity in exchange for the instruments.
- (a) If the micro-entity receives the cash or other resources before the equity instruments are issued, and the micro-entity cannot be required to repay the cash or other resources received, the micro-entity shall recognise the corresponding increase in equity to the extent of consideration received.
 - (b) To the extent that the equity instruments have been subscribed for but not issued (or called up), and the micro-entity has not yet received the cash or other resources, the micro-entity shall not recognise an increase in equity.
- 17.8 A micro-entity shall measure equity instruments at the **fair value** of the cash or other resources received or receivable, net of **transaction costs**.
- 17.8A A micro-entity shall not apply paragraph 17.8 to transactions in which a financial liability is extinguished (partially or in full) by the issue of equity instruments if:
- (a) the creditor is also a direct or indirect shareholder and is acting in its capacity as a direct or indirect existing shareholder;
 - (b) the creditor and the entity are controlled by the same party or parties before and after the transaction and the substance of the transaction includes an equity distribution by, or contribution to, the entity; or
 - (c) the extinguishment is in accordance with the original terms of the financial liability.

In these circumstances, there is no **gain** or loss recognised in **profit or loss** as the result of such a transaction.

- 17.9 A micro-entity shall account for the transaction costs of an equity transaction as a deduction from equity. **Income tax** related to transaction costs shall be accounted for in accordance with Section 24 *Income Tax*.

Exercise of options, rights and warrants

- 17.10 A micro-entity shall apply the principles in paragraphs 17.7 to 17.9 to equity issued by means of exercise of options, rights, warrants and similar equity instruments.

Convertible debt and similar compound financial instruments

- 17.11 On issuing convertible debt, or a similar compound financial instrument, a micro-entity shall allocate the proceeds between the liability component and the equity component of the instrument. To make the allocation, the micro-entity shall first determine the amount of the liability component as the fair value of a similar liability that does not have a conversion feature or similar associated equity component. The micro-entity shall allocate the residual amount as the equity component. Transaction costs shall be allocated between the debt component and the equity component on the basis of their relative fair values.

- 17.12 The micro-entity shall not revise the allocation in a subsequent period.
- 17.13 In periods after the instruments were issued, the micro-entity shall account for the liability component as a financial instrument in accordance with Section 9. The example shown in the Appendix to Section 22 *Liabilities and Equity* of **FRS 102** illustrates the accounting for convertible debt by an issuer.

Treasury shares

- 17.14 Treasury shares are the equity instruments of a micro-entity that have been issued and subsequently reacquired by the micro-entity. A micro-entity shall deduct from equity the fair value of the consideration given for the treasury shares. The micro-entity shall not recognise a gain or loss in profit or loss on the purchase, sale, transfer or cancellation of treasury shares.

Distributions to owners

- 17.15 A micro-entity shall reduce its equity reserves for the amount of distributions to its owners (holders of its equity instruments).

Disclosures

- 17.16 An Irish micro-entity shall disclose information in relation to dividends paid or payable in accordance with Appendix B to Section 6 *Notes to the Financial Statements*.

Section 18

Revenue

Scope of this section

- 18.1 This section applies to **revenue** arising from:
- (a) the sale of goods (whether produced by the **micro-entity** for the purpose of sale or purchased for resale);
 - (b) the rendering of services;
 - (c) **construction contracts** in which the micro-entity is the contractor; and
 - (d) the use by others of micro-entity **assets** yielding interest, royalties or dividends.
- 18.2 This section does not apply to revenue or other **income** arising from **lease** agreements (see Section 15 *Leases*).

Measurement of revenue

- 18.3 A micro-entity shall measure revenue at the amount receivable, taking into account any trade discounts, prompt settlement discounts and volume rebates allowed by the micro-entity.
- 18.4 A micro-entity shall include in revenue only the gross inflows of economic benefits received and receivable by the micro-entity on its own account. A micro-entity shall exclude from revenue all amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes. In an agency relationship, a micro-entity (the **agent**) shall include in revenue only the amount of its commission. The amounts collected on behalf of the **principal** are not revenue of the micro-entity.

Deferred payment

- 18.5 If payment is deferred beyond normal credit terms, the amount of revenue recognised is equal to the cash price available on the transaction date. Any excess of the deferred payment amount over the cash price available on the transaction date is recognised as interest and accounted for in accordance with paragraph 9.14(a).

Exchanges of goods or services

- 18.6 A micro-entity shall not recognise revenue:
- (a) when goods or services are exchanged for goods or services that are of a similar nature and value; or
 - (b) when goods or services are exchanged for dissimilar goods or services but the transaction lacks commercial substance.
- 18.7 A micro-entity shall recognise revenue when goods are sold or services are exchanged for dissimilar goods or services in a transaction that has commercial substance. In that case, the micro-entity shall measure the transaction:
- (a) at the **fair value** of the goods or services received, adjusted by the amount of any cash transferred;
 - (b) if the amount under (a) cannot be measured reliably, then at the fair value of the goods or services given up adjusted by the amount of any cash transferred; or

- (c) if the fair value of neither the goods or services received nor the goods or services given up can be measured reliably, then at the **carrying amount** of the goods or services given up adjusted by the amount of any cash transferred.

Identification of the revenue transaction

- 18.8 A micro-entity shall apply the **recognition** criteria to the separately identifiable components of a single transaction when necessary to reflect the substance of the transaction. For example, a micro-entity applies the recognition criteria to the separately identifiable components of a single transaction when the selling price of a product includes an identifiable amount for subsequent servicing. Conversely, a micro-entity applies the recognition criteria to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole.

Sale of goods

- 18.9 A micro-entity shall recognise revenue from the sale of goods when all the following conditions are satisfied:
- (a) the micro-entity has transferred to the buyer the significant risks and rewards of ownership of the goods;
 - (b) the micro-entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
 - (c) the amount of revenue can be measured reliably;
 - (d) it is **probable** that the economic benefits associated with the transaction will flow to the micro-entity; and
 - (e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.
- 18.10 The assessment of when a micro-entity has transferred the significant risks and rewards of ownership to the buyer requires an examination of the circumstances of the transaction. In most cases, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the buyer. This is the case for most retail sales. In other cases, the transfer of risks and rewards of ownership occurs at a time different from the transfer of legal title or the passing of possession.
- 18.11 A micro-entity does not recognise revenue if it retains significant risks and rewards of ownership. Examples of situations in which the micro-entity may retain the significant risks and rewards of ownership are:
- (a) when the micro-entity retains an obligation for unsatisfactory performance not covered by normal warranties;
 - (b) when the receipt of the revenue from a particular sale is contingent on the buyer selling the goods;
 - (c) when the goods are shipped subject to installation and the installation is a significant part of the contract that has not yet been completed; and
 - (d) when the buyer has the right to rescind the purchase for a reason specified in the sales contract, or at the buyer's sole discretion without any reason, and the micro-entity is uncertain about the probability of return.
- 18.12 If an entity retains only an insignificant risk of ownership, the transaction is a sale and the entity recognises the revenue. For example, a seller recognises revenue when it retains the legal title to the goods solely to protect the collectability of the amount due.

Similarly, an entity recognises revenue when it offers a refund if the customer finds the goods faulty or is not satisfied for other reasons, and the entity can estimate the returns reliably. In such cases, the entity recognises a **provision** for returns in accordance with Section 16 *Provisions and Contingencies*.

Rendering of services

18.13 When the outcome of a transaction involving the rendering of services can be estimated reliably, a micro-entity shall recognise revenue associated with the transaction by reference to the stage of completion of the transaction at the end of the **reporting period** (sometimes referred to as the percentage of completion method). The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

- (a) the amount of revenue can be measured reliably;
- (b) it is probable that the economic benefits associated with the transaction will flow to the micro-entity;
- (c) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and
- (d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

Paragraphs 18.18 to 18.24 provide guidance for applying the percentage of completion method.

18.14 When services are performed by an indeterminate number of acts over a specified period of time, a micro-entity recognises revenue on a straight-line basis over the specified period unless there is evidence that some other method better represents the stage of completion. When a specific act is much more significant than any other act, the micro-entity postpones recognition of revenue until the significant act is executed.

18.15 When the outcome of the transaction involving the rendering of services cannot be estimated reliably, a micro-entity shall recognise revenue only to the extent of the **expenses** recognised that it is probable will be recovered.

Construction contracts

18.16 When the outcome of a construction contract can be estimated reliably, a micro-entity shall recognise contract revenue and contract costs associated with the construction contract as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period (often referred to as the percentage of completion method). Reliable estimation of the outcome requires reliable estimates of the stage of completion, future costs and collectability of billings. Paragraphs 18.18 to 18.24 provide guidance for applying the percentage of completion method.

18.16A Costs that relate directly to a contract and are incurred in securing the contract are also included as part of the contract costs if they can be separately identified and measured reliably and it is probable that the contract will be obtained. When costs incurred in securing a contract are recognised as an expense in the period in which they are incurred, they are not included in contract costs when the contract is obtained in a subsequent period.

18.17 The requirements of this section are usually applied separately to each construction contract. However, in some circumstances, it is necessary to apply this section to the

separately identifiable components of a single contract or to a group of contracts together in order to reflect the substance of a contract or a group of contracts.

Percentage of completion method

- 18.18 This method is used to recognise revenue from rendering services (see paragraphs 18.13 to 18.15) and from construction contracts (see paragraphs 18.16 and 18.17). A micro-entity shall review and, when necessary, revise the estimates of revenue and costs as the service transaction or construction contract progresses.
- 18.19 A micro-entity shall determine the stage of completion of a transaction or contract using the method that measures most reliably the work performed. Possible methods include:
- (a) the proportion that costs incurred for work performed to date bear to the estimated total costs. Costs incurred for work performed to date do not include costs relating to future activity, such as for materials or prepayments;
 - (b) surveys of work performed; and
 - (c) completion of a physical proportion of the contract work or the completion of a proportion of the service contract.

Progress payments and advances received from customers often do not reflect the work performed.

- 18.20 A micro-entity shall recognise costs that relate to future activity on the transaction or contract, such as for materials or prepayments, as an asset if it is probable that the costs will be recovered.
- 18.21 A micro-entity shall recognise as an expense immediately any costs whose recovery is not probable.
- 18.22 When the outcome of a construction contract cannot be estimated reliably:
- (a) a micro-entity shall recognise revenue only to the extent of contract costs incurred that it is probable will be recoverable; and
 - (b) the micro-entity shall recognise contract costs as an expense in the period in which they are incurred.
- 18.23 When it is probable that total contract costs will exceed total contract revenue on a construction contract, the expected loss shall be recognised as an expense immediately, with a corresponding provision for an **onerous contract** (see Section 16 *Provisions and Contingencies*).
- 18.24 If the collectability of an amount already recognised as contract revenue is no longer probable, the micro-entity shall recognise the uncollectible amount as an expense rather than as an adjustment of the amount of contract revenue.

Interest, royalties and dividends

- 18.25 A micro-entity shall recognise revenue arising from the use by others of micro-entity assets yielding interest, royalties and dividends on the bases set out in paragraph 18.26 when:
- (a) it is probable that the economic benefits associated with the transaction will flow to the micro-entity; and
 - (b) the amount of the revenue can be measured reliably.

18.26 A micro-entity shall recognise revenue on the following bases:

- (a) Interest income shall be recognised in accordance with Section 9 *Financial Instruments*.
- (b) Royalties shall be recognised on an **accrual basis** in accordance with the substance of the relevant agreement.
- (c) Dividends shall be recognised when the shareholder's right to receive payment is established.

Appendix to Section 18

Examples of revenue recognition under the principles in Section 18

This appendix accompanies, but is not part of, Section 18. It provides guidance for applying the requirements of Section 18 in recognising revenue.

18A.1 The following examples focus on particular aspects of a transaction and are not a comprehensive discussion of all the relevant factors that might influence the recognition of revenue. The examples generally assume that the amount of revenue can be measured reliably, it is probable that the economic benefits will flow to the micro-entity and the costs incurred or to be incurred can be measured reliably.

Sale of goods

18A.2 The law in different countries may cause the recognition criteria in Section 18 to be met at different times. In particular, the law may determine the point in time at which the micro-entity transfers the significant risks and rewards of ownership. Therefore, the examples in this appendix need to be read in the context of the laws relating to the sale of goods in the country in which the transaction takes place.

Example 1 'Bill and hold' sales, in which delivery is delayed at the buyer's request but the buyer takes title and accepts billing

18A.3 The seller recognises revenue when the buyer takes title, provided:

- (a) it is probable that delivery will be made;
- (b) the item is on hand, identified and ready for delivery to the buyer at the time the sale is recognised;
- (c) the buyer specifically acknowledges the deferred delivery instructions; and
- (d) the usual payment terms apply.

Revenue is not recognised when there is simply an intention to acquire or manufacture the goods in time for delivery.

Example 2 Goods shipped subject to conditions: installation and inspection

18A.4 The seller normally recognises revenue when the buyer accepts delivery, and installation and inspection are complete. However, revenue is recognised immediately upon the buyer's acceptance of delivery when:

- (a) the installation process is simple, for example the installation of a factory-tested television receiver that requires only unpacking and connection of power and antennae; or
- (b) the inspection is performed only for the purposes of final determination of contract prices, for example, shipments of iron ore, sugar or soya beans.

Example 3 Goods shipped subject to conditions: on approval when the buyer has negotiated a limited right of return

18A.5 If there is uncertainty about the possibility of return, the seller recognises revenue when the shipment has been formally accepted by the buyer or the goods have been delivered and the time period for rejection has elapsed.

Example 4 Goods shipped subject to conditions: consignment sales under which the recipient (buyer) undertakes to sell the goods on behalf of the shipper (seller)

18A.6 The shipper recognises revenue when the goods are sold by the recipient to a third party.

Example 5 Goods shipped subject to conditions: cash on delivery sales

18A.7 The seller recognises revenue when delivery is made and cash is received by the seller or its agent.

Example 6 Layaway sales under which the goods are delivered only when the buyer makes the final payment in a series of instalments

18A.8 The seller recognises revenue from such sales when the goods are delivered. However, when experience indicates that most such sales are consummated, revenue may be recognised when a significant deposit is received, provided the goods are on hand, identified and ready for delivery to the buyer.

Example 7 Orders when payment (or partial payment) is received in advance of delivery for goods not currently held in inventory, for example, the goods are still to be manufactured or will be delivered direct to the buyer from a third party

18A.9 The seller recognises revenue when the goods are delivered to the buyer.

Example 8 Sale and repurchase agreements (other than swap transactions) under which the seller concurrently agrees to repurchase the same goods at a later date, or when the seller has a call option to repurchase, or the buyer has a put option to require the repurchase, by the seller, of the goods

18A.10 For a sale and repurchase agreement on an asset other than a financial asset, the seller must analyse the terms of the agreement to ascertain whether, in substance, the risks and rewards of ownership have been transferred to the buyer. If they have been transferred, the seller recognises revenue. When the seller has retained the risks and rewards of ownership, even though legal title has been transferred, the transaction is a financing arrangement and does not give rise to revenue. For a sale and repurchase agreement on a financial asset, the derecognition provisions of Section 9 apply.

Example 9 Sales to intermediate parties, such as distributors, dealers or others for resale

18A.11 The seller generally recognises revenue from such sales when the risks and rewards of ownership have been transferred. However, when the buyer is acting, in substance, as an agent, the sale is treated as a consignment sale.

Example 10 Subscriptions to publications and similar items

18A.12 When the items involved are of similar value in each time period, the seller recognises revenue on a straight-line basis over the period in which the items are dispatched. When the items vary in value from period to period, the seller recognises revenue on the basis of the sales value of the item dispatched in relation to the total estimated sales value of all items covered by the subscription.

Example 11 Instalment sales, under which the consideration is receivable in instalments

18A.13 The seller recognises revenue based on the cash price a customer would pay at the date of sale. If the total amount paid through instalments is greater than the cash price payable at the date of sale, any excess is recognised as interest and accounted for in accordance with paragraph 9.14(a).

Example 12 Agreements for the construction of real estate

18A.14 A micro-entity that undertakes the construction of real estate, directly or through subcontractors, and enters into an agreement with one or more buyers before construction is complete, shall account for the agreement using the percentage of completion method, only if:

- (a) the buyer is able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not); or
- (b) the buyer acquires and supplies construction materials and the micro-entity provides only construction services.

18A.15 If the micro-entity is required to provide services together with construction materials in order to perform its contractual obligation to deliver real estate to the buyer, the agreement shall be accounted for as the sale of goods. In this case, the buyer does not obtain control or the significant risks and rewards of ownership of the work in progress in its current state as construction progresses. Rather, the transfer occurs only on delivery of the completed real estate to the buyer.

Example 13 Sale with customer loyalty award

18A.16 A micro-entity sells product A for CU100. Purchasers of product A get an award credit enabling them to buy product B for CU10. The normal selling price of product B is CU18. The micro-entity estimates that 40 per cent of the purchasers of product A will use their award to buy product B at CU10. The normal selling price of product A, after taking into account discounts that are usually offered but that are not available during this promotion, is CU95.

18A.17 The fair value of the award credit is $40 \text{ per cent} \times [\text{CU}18 - \text{CU}10] = \text{CU}3.20$. The micro-entity allocates the total revenue of CU100 between product A and the award credit by reference to their relative fair values of CU95 and CU3.20 respectively. Therefore:

- (a) Revenue for product A is $\text{CU}100 \times [\text{CU}95 / (\text{CU}95 + \text{CU}3.20)] = \text{CU}96.74$
- (b) Revenue for product B is $\text{CU}100 \times [\text{CU}3.20 / (\text{CU}95 + \text{CU}3.20)] = \text{CU}3.26$

Rendering of services

Example 14 Installation fees

18A.18 The seller recognises installation fees as revenue by reference to the stage of completion of the installation, unless they are incidental to the sale of a product, in which case they are recognised when the goods are sold.

Example 15 Servicing fees included in the price of the product

18A.19 When the selling price of a product includes an identifiable amount for subsequent servicing (eg after sales support and product enhancement on the sale of software), the seller defers that amount and recognises it as revenue over the period during which the

service is performed. The amount deferred is that which will cover the expected costs of the services under the agreement, together with a reasonable profit on those services.

Example 16 Advertising commissions

18A.20 Media commissions are recognised when the related advertisement or commercial appears before the public. Production commissions are recognised by reference to the stage of completion of the project.

Example 17 Admission fees

18A.21 The seller recognises revenue from artistic performances, banquets and other special events when the event takes place. When a subscription to a number of events is sold, the seller allocates the fee to each event on a basis that reflects the extent to which services are performed at each event.

Example 18 Tuition fees

18A.22 The seller recognises revenue over the period of instruction.

Example 19 Initiation, entrance and membership fees

18A.23 Revenue recognition depends on the nature of the services provided. If the fee permits only membership, and all other services or products are paid for separately, or if there is a separate annual subscription, the fee is recognised as revenue when no significant uncertainty about its collectability exists. If the fee entitles the member to services or publications to be provided during the membership period, or to purchase goods or services at prices lower than those charged to non-members, it is recognised on a basis that reflects the timing, nature and value of the benefits provided.

Franchise fees

18A.24 Franchise fees may cover the supply of initial and subsequent services, equipment and other tangible assets, and know-how. Accordingly, franchise fees are recognised as revenue on a basis that reflects the purpose for which the fees were charged. The following methods of franchise fee recognition are appropriate.

Example 20 Franchise fees: Supplies of equipment and other tangible assets

18A.25 The franchisor recognises the fair value of the assets sold as revenue when the items are delivered or title passes.

Example 21 Franchise fees: Supplies of initial and subsequent services

18A.26 The franchisor recognises fees for the provision of continuing services, whether part of the initial fee or a separate fee, as revenue as the services are rendered. When the separate fee does not cover the cost of continuing services together with a reasonable profit, part of the initial fee, sufficient to cover the costs of continuing services and to provide a reasonable profit on those services, is deferred and recognised as revenue as the services are rendered.

18A.27 The franchise agreement may provide for the franchisor to supply equipment, inventories, or other tangible assets at a price lower than that charged to others or a price that does not provide a reasonable profit on those sales. In these circumstances, part of the initial fee, sufficient to cover estimated costs in excess of that price and to provide a reasonable profit on those sales, is deferred and recognised over the period

the goods are likely to be sold to the franchisee. The balance of an initial fee is recognised as revenue when performance of all the initial services and other obligations required of the franchisor (such as assistance with site selection, staff training, financing and advertising) has been substantially accomplished.

18A.28 The initial services and other obligations under an area franchise agreement may depend on the number of individual outlets established in the area. In this case, the fees attributable to the initial services are recognised as revenue in proportion to the number of outlets for which the initial services have been substantially completed.

18A.29 If the initial fee is collectible over an extended period and there is a significant uncertainty that it will be collected in full, the fee is recognised as cash instalments are received.

Example 22 Franchise fees: Continuing franchise fees

18A.30 Fees charged for the use of continuing rights granted by the agreement, or for other services provided during the period of the agreement, are recognised as revenue as the services are provided or the rights used.

Example 23 Franchise fees: Agency transactions

18A.31 Transactions may take place between the franchisor and the franchisee that, in substance, involve the franchisor acting as agent for the franchisee. For example, the franchisor may order supplies and arrange for their delivery to the franchisee at no profit. Such transactions do not give rise to revenue.

Example 24 Fees from the development of customised software

18A.32 The software developer recognises fees from the development of customised software as revenue by reference to the stage of completion of the development, including completion of services provided for post-delivery service support.

Interest, royalties and dividends

Example 25 Licence fees and royalties

18A.33 The licensor recognises fees and royalties paid for the use of its assets (such as trademarks, patents, software, music copyright, record masters and motion picture films) in accordance with the substance of the agreement. As a practical matter, this may be on a straight-line basis over the life of the agreement, for example, when a licensee has the right to use specified technology for a specified period of time.

18A.34 An assignment of rights for a fixed fee or non-refundable guarantee under a non-cancellable contract that permits the licensee to exploit those rights freely and the licensor has no remaining obligations to perform is, in substance, a sale. An example is a licensing agreement for the use of software when the licensor has no obligations after delivery. Another example is the granting of rights to exhibit a motion picture film in markets in which the licensor has no control over the distributor and expects to receive no further revenues from the box office receipts. In such cases, revenue is recognised at the time of sale.

18A.35 In some cases, whether or not a licence fee or royalty will be received is contingent on the occurrence of a future event. In such cases, revenue is recognised only when it is probable that the fee or royalty will be received, which is normally when the event has occurred.

Determining whether a micro-entity is acting as a principal or as an agent

18A.36 Determining whether a micro-entity is acting as a principal or as an agent requires judgement and consideration of all relevant facts and circumstances.

18A.37 A micro-entity is acting as a principal when it has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. Features that indicate that a micro-entity is acting as principal include:

- (a) the micro-entity has the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer;
- (b) the micro-entity has inventory risk before or after the customer order, during shipping or on return;
- (c) the micro-entity has latitude in establishing prices, either directly or indirectly, for example by providing additional goods or services; and
- (d) the micro-entity bears the customer's credit risk for the amount receivable from the customer.

18A.38 A micro-entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that a micro-entity is acting as agent is that the amount the micro-entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer.

18A.39 When a micro-entity has entered into a contract as an undisclosed agent, it is normally acting as principal.

18A.40 The amounts collected by an agent on behalf of a principal are not revenue. Instead, revenue is the amount of commission.

Section 19

Government Grants

Scope of this section

- 19.1 This section applies to **government grants**.
- 19.2 Government grants exclude those forms of government assistance that cannot reasonably have a value placed upon them and transactions with government that cannot be distinguished from the normal trading transactions of the **micro-entity**.

Recognition and measurement

- 19.3 Government grants, including non-monetary grants, shall not be recognised until there is reasonable assurance that:
- (a) the micro-entity will comply with the conditions attaching to them; and
 - (b) the grants will be received.
- 19.4 A micro-entity shall measure grants at the **fair value** of the **asset** received or receivable.
- 19.5 Where a grant becomes repayable it shall be recognised as a **liability** when the repayment meets the definition of a liability.
- 19.6 A micro-entity shall classify government grants either as a grant relating to **revenue** or a grant relating to assets.
- 19.7 Government grants relating to revenue shall be recognised in **income** on a systematic basis over the periods in which the micro-entity recognises the related costs for which the grant is intended to compensate.
- 19.8 A government grant that becomes receivable as compensation for **expenses** or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised as income in **profit or loss** in the period in which it becomes receivable.
- 19.9 Government grants relating to assets shall be recognised in income on a systematic basis over the expected **useful life** of the asset.
- 19.10 Where part of a government grant relating to an asset is deferred it shall be recognised as deferred income and not deducted from the **carrying amount** of the asset.

Section 20

Borrowing Costs

Scope of this section

- 20.1 This section applies to **borrowing costs**. Borrowing costs include:
- (a) interest expense recognised in accordance with Section 9 *Financial Instruments*;
 - (b) finance charges in respect of **finance leases** recognised in accordance with Section 15 *Leases*; and
 - (c) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

Recognition

- 20.2 A **micro-entity** shall recognise all borrowing costs as an **expense** in **profit or loss** in the period in which they are incurred.

Section 21

Share-based Payment

Scope of this section

- 21.1 This section applies to **share-based payment transactions** including:
- (a) **equity-settled share-based payment transactions**;
 - (b) **cash-settled share-based payment transactions**; and
 - (c) transactions in which the **micro-entity** receives or acquires goods or services and the terms of the arrangement provide either the micro-entity or the supplier of those goods or services with a choice of whether the micro-entity settles the transaction in cash (or other **assets**) or by issuing equity instruments.

In the absence of specifically identifiable goods or services, other circumstances may indicate that goods or services have been (or will be) received, in which case this section applies.

Equity-settled share-based payment transactions

- 21.2 A micro-entity shall not account for equity-settled share-based payments transactions until shares are issued, at which point the micro-entity shall apply the requirements of Section 17 *Liabilities and Equity*.

Cash-settled share-based payment transactions

- 21.3 A micro-entity shall recognise the goods or services received or acquired in a cash-settled share-based payment transaction when it obtains the goods or as the services are received and recognise a corresponding **liability**.
- 21.4 If the cash-settled share-based payments granted **vest** immediately, the counterparty is not required to complete a specified period of service before becoming unconditionally entitled to those cash-settled share-based payments. In the absence of evidence to the contrary, the micro-entity shall presume that services rendered by the counterparty as consideration for the share-based payments have been received. In this case, on **grant date** the micro-entity shall recognise the services received in full, with a corresponding liability.
- 21.5 If the cash-settled share-based payments do not vest until the counterparty completes a specified period of service, the micro-entity shall presume that the services to be rendered by the counterparty as consideration for those cash-settled share-based payments will be received in the future, during the vesting period. The micro-entity shall account for those services as they are rendered by the counterparty during the vesting period, with a corresponding increase in the liability.
- 21.6 When the goods or services received or acquired in a cash-settled share-based payment transaction do not qualify for **recognition** as assets, the micro-entity shall recognise them as **expenses**.
- 21.7 A micro-entity shall measure the goods and services acquired and the liability incurred in accordance with the **measurement** requirements for a **provision** in Section 16 *Provisions and Contingencies*.

Share-based payment transactions with cash alternatives

- 21.8 Some share-based payment transactions give either the micro-entity or the counterparty a choice of settling the transaction in cash (or other assets) or by the transfer of equity instruments.
- 21.9 When the micro-entity has a choice of settlement of the transaction in cash (or other assets) or by the transfer of equity instruments, the micro-entity shall account for the whole transaction as set out in paragraph 21.2 unless:
- (a) the choice of settlement in equity instruments has no commercial substance (eg because the micro-entity is legally prohibited from issuing shares); or
 - (b) the micro-entity has a past practice or a stated policy of settling in cash, or generally settles in cash whenever the counterparty asks for cash settlement.

In circumstances (a) and (b) the micro-entity shall account for the transaction as a wholly cash-settled transaction in accordance with paragraphs 21.3 to 21.7.

- 21.10 Except as set out in paragraph 21.11, when the counterparty has a choice of settlement of the transaction in cash (or other assets) or by the transfer of equity instruments, the micro-entity shall account for the transaction as a wholly cash-settled share-based payment transaction in accordance with paragraphs 21.3 to 21.7
- 21.11 If the choice of settlement in cash (or other assets) has no commercial substance because the cash settlement amount (or value of the other assets) bears no relationship to, and is likely to be lower in value than, the **fair value** of the equity instruments, the entity shall account for the whole transaction as set out in paragraph 21.2.

Section 22

Impairment of Assets

Scope of this section

- 22.1 This section applies to the impairment of **assets** (including **goodwill**), except in relation to:
- (a) assets arising from **construction contracts** (see Section 18 *Revenue*);
 - (b) **financial assets** within the scope of Section 9 *Financial Instruments*; and
 - (c) **inventories** (see Section 10 *Inventories*).

Impairment of assets

General principles

- 22.2 If, and only if, the **recoverable amount** of an asset is less than its **carrying amount**, the **micro-entity** shall reduce the carrying amount of the asset to its recoverable amount.
- 22.3 If it is not possible to estimate the recoverable amount of the individual asset, a micro-entity shall estimate the recoverable amount of the **cash-generating unit** to which the asset belongs. This may be the case because measuring the recoverable amount requires forecasting cash flows, and sometimes individual assets do not generate cash flows by themselves. An **impairment loss** for a cash-generating unit shall be recognised and measured in accordance with the relevant requirements of Section 27 *Impairment of Assets* of **FRS 102**.
- 22.4 A micro-entity that has goodwill acquired in a **business combination** shall apply the additional impairment requirements applicable to goodwill in paragraphs 27.24 to 27.27 of FRS 102.
- 22.5 A micro-entity shall recognise an impairment loss immediately in **profit or loss**.

Indicators of impairment

- 22.6 A micro-entity shall assess at each **reporting date** whether there is any indication that an asset may be impaired. If any such indication exists, the micro-entity shall estimate the recoverable amount of the asset. If there is no indication of impairment, it is not necessary to estimate the recoverable amount.
- 22.7 In assessing whether there is any indication that an asset may be impaired, a micro-entity shall consider, as a minimum, the following indications:

External sources of information

- (a) During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.
- (b) Significant changes with an adverse effect on the micro-entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the micro-entity operates or in the market to which an asset is dedicated.
- (c) Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect materially the

discount rate used in calculating an asset's **value in use** and decrease the asset's **fair value less costs to sell**.

- (d) The carrying amount of the net assets of the micro-entity is more than the estimated **fair value** of the micro-entity as a whole (such an estimate may have been made, for example, in relation to the potential sale of part or all of the micro-entity).

Internal sources of information

- (e) Evidence is available of obsolescence or physical damage of an asset.
- (f) Significant changes with an adverse effect on the micro-entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the **useful life** of an asset as finite rather than indefinite.
- (g) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected. In this context economic performance includes operating results and cash flows.

- 22.8 If there is an indication that an asset may be impaired, this may indicate that the micro-entity should review the remaining useful life, the **depreciation (amortisation)** method or the **residual value** for the asset and adjust it in accordance with the section of this FRS applicable to the asset (eg Section 12 *Property, Plant and Equipment and Investment Property* and Section 13 *Intangible Assets other than Goodwill*), even if no impairment loss is recognised for the asset.

Measuring recoverable amount

- 22.9 The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.
- 22.10 It is not always necessary to determine both an asset's fair value less costs to sell and its value in use. If either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.
- 22.11 If there is no reason to believe that an asset's value in use materially exceeds its fair value less costs to sell, the asset's fair value less costs to sell may be used as its recoverable amount. This will often be the case for an asset that is held for disposal.

Fair value less costs to sell

- 22.12 Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. The best evidence of the fair value less costs to sell of an asset is a price in a binding sale agreement in an arm's length transaction or a open market price in an **active market**. If there is no binding sale agreement or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that a micro-entity could obtain, at the reporting date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, a micro-entity considers the outcome of recent transactions for similar assets within the same industry. Paragraph 2.31 provides further guidance on determining fair value.

- 22.13 When determining an asset's fair value less costs to sell, consideration shall be given to any restrictions imposed on that asset. Costs to sell shall also include the cost of obtaining relaxation of a restriction where necessary in order to enable the asset to be sold. If a restriction would also apply to any potential purchaser of an asset, the fair value of the asset may be lower than that of an asset whose use is not restricted.

Value in use

- 22.14 Value in use is the **present value** of the future cash flows expected to be derived from an asset. This present value calculation involves the following steps:
- (a) estimating the future cash inflows and outflows to be derived from the continuing use of the asset and from its ultimate disposal; and
 - (b) applying the appropriate discount rate to those future cash flows.
- 22.15 In measuring value in use, estimates of future cash flows shall include:
- (a) projections of cash inflows from the continuing use of the asset;
 - (b) projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and
 - (c) net cash flows, if any, expected to be received (or paid) for the disposal of the asset at the end of its useful life in an arm's length transaction between knowledgeable, willing parties.

The micro-entity may wish to use any recent financial budgets or forecasts to estimate the cash flows, if available, and extrapolate the projections using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified.

- 22.16 Estimates of future cash flows shall not include:
- (a) cash inflows or outflows from **financing activities**; or
 - (b) **income tax** receipts or payments.
- 22.17 Future cash flows shall be estimated for the asset in its current condition. Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:
- (a) a future **restructuring** to which a micro-entity is not yet committed; or
 - (b) improving or enhancing the asset's performance.
- 22.18 The discount rate(s) used in the present value calculation shall be a pre-tax rate(s) that reflect(s) current market assessments of:
- (a) the time value of money; and
 - (b) the risks specific to the asset for which the future cash flow estimates have not been adjusted.

The discount rate(s) used to measure an asset's value in use shall not reflect risks for which the future cash flow estimates have been adjusted, to avoid double-counting.

Reversal of an impairment loss

- 22.19 An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

22.20 For all assets other than goodwill, if and only if, the reasons for the impairment loss have ceased to apply, an impairment loss shall be reversed in a subsequent period. A micro-entity shall assess at each reporting date whether there is any indication that an impairment loss recognised in prior periods may no longer exist or may have decreased. Indications that an impairment loss may have decreased or may no longer exist are generally the opposite of those set out in paragraph 22.7. If any such indication exists, the micro-entity shall determine whether all or part of the prior impairment loss should be reversed.

Reversal where recoverable amount was estimated for an individual impaired asset

22.21 When the prior impairment loss was based on the recoverable amount of the individual impaired asset, the following requirements apply:

- (a) The micro-entity shall estimate the recoverable amount of the asset at the current reporting date.
- (b) If the estimated recoverable amount of the asset exceeds its carrying amount, the micro-entity shall increase the carrying amount to recoverable amount, subject to the limitation described in paragraph (c) below. That increase is a reversal of an impairment loss. The micro-entity shall recognise the reversal immediately in profit or loss.
- (c) The reversal of an impairment loss shall not increase the carrying amount of the asset above the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.
- (d) After a reversal of an impairment loss is recognised, the micro-entity shall adjust the depreciation (amortisation) charge for the asset in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Disclosures

22.22 An Irish micro-entity shall disclose information in relation to impairment losses recognised and reversed in accordance with Appendix B to Section 6 *Notes to the Financial Statements*.

Section 23

Employee Benefits

Scope of this section

- 23.1 This section applies to **employee benefits**, except for **share-based payment transactions** (see Section 21 *Share-based Payment*). Employee benefits include:
- (a) short-term employee benefits, which are employee benefits (other than **termination benefits**) that are expected to be settled wholly before 12 months after the end of the **reporting period** in which the employees render the related service;
 - (b) **post-employment benefits**, which are employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment;
 - (c) other long-term employee benefits, which are all employee benefits, other than short-term employee benefits, post-employment benefits and termination benefits; or
 - (d) termination benefits, which are employee benefits provided in exchange for the termination of an employee's employment as a result of either:
 - (i) a micro-entity's decision to terminate an employee's employment before the normal retirement date; or
 - (ii) an employee's decision to accept voluntary redundancy in exchange for those benefits.

General recognition principle for all employee benefits

- 23.2 A micro-entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the micro-entity during the reporting period:
- (a) As a **liability**, after deducting amounts that have been paid directly to the employees or as a contribution to an employee benefit fund¹⁵. If the amount paid exceeds the obligation arising from service before the **reporting date**, a micro-entity shall recognise that excess as an **asset** to the extent that the prepayment will lead to a reduction in future payments or a cash refund.
 - (b) As an **expense**, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset such as **inventories** (for example in accordance with paragraph 10.8) or **property, plant and equipment** (in accordance with paragraph 12.9).

¹⁵ Contributions to an employee benefit fund that is an intermediate payment arrangement shall be accounted for in accordance with Section 7 *Subsidiaries, Associates, Jointly Controlled Entities and Intermediate Payment Arrangements*, and as a result if the employer is a sponsoring micro-entity the assets and liabilities of the intermediary will be accounted for by the sponsoring micro-entity as an extension of its own business. In which case the payment to the employee benefit fund does not extinguish the liability of the employer.

Short-term employee benefits

Examples

- 23.3 Short-term employee benefits include items such as the following, if expected to be settled wholly before 12 months after the end of the annual reporting period in which the employees render the related service:
- (a) wages, salaries and social security contributions;
 - (b) paid annual leave and paid sick leave;
 - (c) profit-sharing and bonuses; and
 - (d) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.

Measurement of short-term benefits generally

- 23.4 When an employee has rendered service to a micro-entity during the reporting period, the micro-entity shall measure the amounts recognised in accordance with paragraph 23.2 at the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

Recognition and measurement: Short-term compensated absences

- 23.5 A micro-entity may compensate employees for absence for various reasons including annual leave and sick leave. Some short-term compensated absences accumulate - they can be carried forward and used in future periods if the employee does not use the current period's entitlement in full. Examples include annual leave and sick leave. A micro-entity shall recognise the expected cost of **accumulating compensated absences** when the employees render service that increases their entitlement to future compensated absences. The micro-entity shall measure the expected cost of accumulating compensated absences at the undiscounted additional amount that the micro-entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The micro-entity shall present this amount as falling due within one year at the reporting date.
- 23.6 A micro-entity shall recognise the cost of other (non-accumulating) compensated absences when the absences occur. The micro-entity shall measure the cost of non-accumulating compensated absences at the undiscounted amount of salaries and wages paid or payable for the period of absence.

Recognition: Profit-sharing and bonus plans

- 23.7 A micro-entity shall recognise the expected cost of profit-sharing and bonus payments only when:
- (a) the micro-entity has a present legal or **constructive obligation** to make such payments as a result of past events (this means that the micro-entity has no realistic alternative but to make the payments); and
 - (b) a reliable estimate of the obligation can be made.

Post-employment benefits: Distinction between defined contribution plans and defined benefit plans

- 23.8 Post-employment benefits include, for example:
- (a) retirement benefits, such as pensions; and

- (b) other post-employment benefits, such as post-employment life insurance and post-employment medical care.

Arrangements whereby a micro-entity provides post-employment benefits are **post-employment benefit plans**. A micro-entity shall apply this section to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits. In some cases, these arrangements are imposed by law rather than by action of the micro-entity. In some cases, these arrangements arise from actions of the micro-entity even in the absence of a formal, documented plan.

- 23.9 Post-employment benefit plans are classified as either **defined contribution plans** or **defined benefit plans**, depending on their principal terms and conditions:
- (a) Defined contribution plans are post-employment benefit plans under which a micro-entity pays fixed contributions into a separate entity (a fund) and has no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. The amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by a micro-entity (and perhaps also the employee) to a post-employment benefit plan or to an insurer, together with investment returns arising from the contributions.
 - (b) Defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans, the micro-entity's obligation is to provide the agreed benefits to current and former employees, and actuarial risk (that benefits will cost more or less than expected) and investment risk (that returns on assets set aside to fund the benefits will differ from expectations) are borne, in substance, by the micro-entity. If actuarial or investment experience is worse than expected, the micro-entity's obligation may be increased, and vice versa if actuarial or investment experience is better than expected.

Post-employment benefit plans

Recognition and measurement – requirements applicable to all plans

- 23.10 When contributions to a defined contribution or defined benefit plan are not expected to be settled wholly within 12 months after the end of the reporting period in which the employees render the related service, the liability recognised in accordance with paragraph 23.2(a) shall be measured at the **present value** of the contributions payable using the methodology for selecting a discount rate specified in paragraph 23.11. The unwinding of the discount shall be recognised as interest expense in **profit or loss** in the period in which it arises.
- 23.11 A micro-entity shall determine the rate used to discount the future payments by reference to market yields at the reporting date on high quality corporate bonds. In countries with no deep market in such bonds, the micro-entity shall use the market yields (at the reporting date) on government bonds. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated period of the future payments.

Recognition and measurement – requirements applicable to defined benefit plans

- 23.12 When a micro-entity participates in a defined benefit plan (which may include a **multi-employer plan** or **state plan**) and has entered into an agreement with the plan that determines how the micro-entity will fund a deficit (such as a schedule of

contributions), the micro-entity shall recognise a liability for the contributions payable that arise from the agreement (to the extent that they relate to the deficit) and the resulting expense in profit or loss in accordance with paragraphs 23.2 and 23.10.

- 23.13 Where a micro-entity participates in a defined benefit plan that shares risks between entities under common control it shall recognise a cost equal to its contribution payable for the period. If a micro-entity is legally responsible for the plan and has entered into an agreement with the plan that determines how a deficit will be funded, the micro-entity shall recognise a liability for the contributions payable that arise from the agreement (to the extent that they relate to the deficit) and the resulting expense in profit or loss in accordance with paragraphs 23.2 and 23.10.

Other long-term employee benefits

- 23.14 Other long-term employee benefits include items such as the following, if not expected to be settled wholly before 12 months after the end of the annual reporting period in which the employees render the related service:

- (a) long-term paid absences such as long-service or sabbatical leave;
- (b) other long-service benefits;
- (c) long-term disability benefits;
- (d) profit-sharing and bonuses; and
- (e) deferred remuneration.

- 23.15 A micro-entity shall recognise a liability for other long-term employee benefits measured at the present value of the benefit obligation at the reporting date calculated using the methodology for selecting a discount rate in paragraph 23.11. The unwinding of the discount shall be recognised as interest expense in profit or loss in the period in which it arises.

Termination benefits

- 23.16 A micro-entity may be committed, by legislation, by contractual or other agreements with employees or their representatives or by a constructive obligation based on business practice, custom or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits.

Recognition

- 23.17 Because termination benefits do not provide a micro-entity with future economic benefits, a micro-entity shall recognise them as an expense in profit or loss immediately.
- 23.18 A micro-entity shall recognise termination benefits as a liability and an expense only when the micro-entity is demonstrably committed either:
- (a) to terminate the employment of an employee or group of employees before the normal retirement date; or
 - (b) to provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

- 23.19 A micro-entity is demonstrably committed to a termination only when the micro-entity has a detailed formal plan for the termination¹⁶ and is without realistic possibility of withdrawal from the plan.

Measurement

- 23.20 A micro-entity shall measure termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the reporting date. In the case of an offer made to encourage voluntary redundancy, the **measurement** of termination benefits shall be based on the number of employees expected to accept the offer.
- 23.21 When termination benefits are due more than 12 months after the end of the reporting period, they shall be measured at their discounted present value using the methodology for selecting a discount rate specified in paragraph 23.11.

Disclosures

- 23.22 A micro-entity shall disclose any commitment not recognised in the **statement of financial position** concerning pensions separately from other financial commitments, guarantees and contingencies in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*.
- 23.23 An Irish micro-entity shall disclose particulars of retirement benefit commitments included in the statement of financial position in accordance with Appendix B to Section 6.

¹⁶ An example of the features of a detailed formal plan for restructuring, which may include termination benefits, is given in paragraph 16.15.

Section 24

Income Tax

Scope of this section

24.1 [Deleted]

24.2 This section applies to:

- (a) **income tax** comprising only of **current tax**; and
- (b) value added tax (VAT) and other similar sales taxes, which are not income taxes.

This section prohibits the **recognition** of **deferred tax** which represents the future tax consequences of transactions and events recognised in the **financial statements** of the current and previous periods.

24.3 [Moved to 24.2(b)]

Current tax

24.4 A **micro-entity** shall recognise a current tax liability for tax payable on **taxable profit** for the current and past periods. If the amount of tax paid for the current and past periods exceeds the amount of tax payable for those periods, the micro-entity shall recognise the excess as a current tax **asset**.

24.4A A micro-entity shall measure current tax at the tax rate applicable to undistributed profits until the micro-entity recognises a **liability** to pay a dividend. When the micro-entity recognises a liability to pay a dividend, it shall recognise the resulting current tax liability (asset), and the related **tax expense** (income).

24.4B As an exception, when:

- (a) a micro-entity is wholly-owned by one or more charitable¹⁷ entities;
- (b) it is **probable** that a gift aid payment will be made to a member of the same charitable group, or charitable **venturer**, within nine months of the **reporting date**; and
- (c) that payment will qualify to be set against profits for tax purposes,

the income tax effects of that gift aid payment shall be recognised at the reporting date. The income tax effects shall be measured consistently with the tax treatment planned to be used in the entity's income tax filings.

24.5 A micro-entity shall recognise a current tax asset for the benefit of a tax loss that can be carried back to recover tax paid in a previous period.

24.6 A micro-entity shall measure a current tax liability (asset) at the amount of tax it expects to pay (recover) using the tax rates and laws that have been enacted or **substantively enacted** by the reporting date.

¹⁷ In this context charitable refers to an entity that has been recognised by HMRC as being eligible for certain tax reliefs because of its charitable purposes.

Deferred tax

24.7 A micro-entity shall not recognise deferred tax.

Measurement of current tax

24.8 A micro-entity shall not discount current tax assets and liabilities.

Withholding tax on dividends

24.9 When a micro-entity pays dividends to its shareholders, it may be required to pay a portion of the dividends to taxation authorities on behalf of shareholders. Outgoing dividends and similar amounts payable shall be recognised at an amount that includes any withholding tax but excludes other taxes, such as attributable tax credits.

24.10 Incoming dividends and similar **income** receivable shall be recognised at an amount that includes any withholding tax but excludes other taxes, such as attributable tax credits. Any withholding tax suffered shall be shown as part of the tax charge.

Value Added Tax and other similar sales taxes

24.11 **Turnover** included in **profit or loss** shall exclude VAT and other similar sales taxes on taxable outputs and VAT imputed under the flat rate VAT scheme. **Expenses** shall exclude recoverable VAT and other similar recoverable sales taxes. Irrecoverable VAT allocable to **fixed assets** and to other items separately recognised shall be included in their cost where practicable and **material**.

Presentation

Allocation in profit or loss

24.12 A micro-entity shall present changes in a current tax liability (asset) as tax expense (income).

Offsetting

24.13 A micro-entity shall offset current tax assets and current tax liabilities, if, and only if, it has a legally enforceable right to set off the amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Section 25

Foreign Currency Translation

Scope of this section

- 25.1 This section applies to foreign currency transactions. When a micro-entity has a foreign branch, the micro-entity should refer to the requirements of Section 30 *Foreign Currency Translation* of **FRS 102** to determine if the foreign branch has a different functional currency, and if so, should apply the requirements of Section 30 of FRS 102 to those transactions undertaken by the foreign branch.

Reporting foreign currency transactions

Initial recognition

- 25.2 A foreign currency transaction is a transaction that is denominated or requires settlement in a foreign currency, including transactions arising when a micro-entity:
- (a) buys or sells goods or services whose price is denominated in a foreign currency;
 - (b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or
 - (c) otherwise acquires or disposes of **assets**, or incurs or settles **liabilities**, denominated in a foreign currency.
- 25.3 A micro-entity shall record a foreign currency transaction by applying to the foreign currency amount the spot exchange rate at the date of the transaction unless:
- (a) the transaction is to be settled at a contracted rate, in which case that rate shall be used; or
 - (b) where a trading transaction is covered by a related or matching forward contract, in which case the rate of exchange specified in that contract shall be used.
- 25.4 The date of a transaction is the date on which the transaction first qualifies for **recognition** in accordance with this FRS. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used, for example, an average rate for a week or a month might be used for all transactions in each foreign currency occurring during that period. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.

Reporting at the end of the subsequent reporting periods

- 25.5 At the end of each **reporting period**, unless it is applying a contracted rate in accordance with paragraph 25.3 a micro-entity shall:
- (a) translate foreign currency **monetary items** using the **closing rate**; and
 - (b) translate non-monetary items that are measured in terms of historical cost in a foreign currency using the exchange rate at the date of the transaction.
- 25.6 A micro-entity shall recognise, in **profit or loss** in the period in which they arise, exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous periods.

Section 26

Events after the End of the Reporting Period

Scope of this section

26.1 This section applies to the **recognition, measurement** and disclosure of events after the end of the **reporting period**.

Events after the end of the reporting period defined

26.2 Events after the end of the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the **financial statements** are authorised for issue. There are two types of events:

- (a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the end of the reporting period); and
- (b) those that are indicative of conditions that arose after the end of the reporting period (non-adjusting events after the end of the reporting period).

26.3 Events after the end of the reporting period include all events up to the date when the financial statements are authorised for issue, even if those events occur after the public announcement of **profit or loss** or other selected financial information.

Recognition and measurement

Adjusting events after the end of the reporting period

26.4 A **micro-entity** shall adjust the amounts recognised in its financial statements to reflect adjusting events after the end of the reporting period.

26.5 The following are examples of adjusting events after the end of the reporting period that require a micro-entity to adjust the amounts recognised in its financial statements, or to recognise items that were not previously recognised:

- (a) The settlement after the end of the reporting period of a court case that confirms that the micro-entity had a present obligation at the end of the reporting period. The micro-entity adjusts any previously recognised **provision** related to this court case in accordance with Section 16 *Provisions and Contingencies* or recognises a new provision. The micro-entity does not merely disclose a **contingent liability**. Rather, the settlement provides additional evidence to be considered in determining the provision that should be recognised at the end of the reporting period in accordance with Section 16.
- (b) The receipt of information after the end of the reporting period indicating that an **asset** was impaired at the end of the reporting period, or that the amount of a previously recognised **impairment loss** for that asset needs to be adjusted. For example:
 - (i) the bankruptcy of a customer that occurs after the end of the reporting period usually confirms that a loss existed at the end of the reporting period on a trade receivable and that the micro-entity needs to adjust the **carrying amount** of the trade receivable; and
 - (ii) the sale of **inventories** after the end of the reporting period may give evidence about their selling price at the end of the reporting period for the purpose of assessing impairment at that date.

- (c) The determination after the end of the reporting period of the cost of assets purchased, or the proceeds from assets sold, before the end of the reporting period.
- (d) The determination after the end of the reporting period of the amount of profit-sharing or bonus payments, if the micro-entity had a legal or **constructive obligation** at the end of the reporting period to make such payments as a result of events before that date (see Section 23 *Employee Benefits*).
- (e) The discovery of fraud or **errors** that show that the financial statements are incorrect.

Non-adjusting events after the end of the reporting period

- 26.6 A micro-entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the end of the reporting period.
- 26.7 Examples of non-adjusting events after the end of the reporting period include:
- (a) A decline in 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, a micro-entity does not adjust the amounts recognised in its financial statements for the investments.
 - (b) 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 (see paragraph 16.18). 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.

Going concern

- 26.8 A micro-entity shall not prepare its financial statements on a going concern basis if management determines after the end of the reporting period that it either intends to liquidate the micro-entity or to cease trading, or that it has no realistic alternative but to do so.
- 26.9 Deterioration in operating results and **financial position** after the reporting period may lead management to determine that they intend to liquidate the micro-entity or to cease trading or that they have no realistic alternative but to do so. If the going concern basis of accounting is no longer appropriate, the effect is so pervasive that this section requires a fundamental change in the basis of accounting.

Dividends

- 26.10 If a micro-entity declares dividends to holders of its equity instruments after the end of the reporting period, the micro-entity shall not recognise those dividends as a **liability** at the end of the reporting period because no obligation exists at that time.

Section 27

Specialised Activities

Scope of this section

27.1 This section applies to a **micro-entity** involved in agriculture.

Agriculture

Recognition

- 27.2 A micro-entity that is engaged in **agricultural activity** shall recognise a **biological asset** or an item of **agricultural produce** when, and only when:
- (a) the micro-entity controls the **asset** as a result of past events;
 - (b) it is **probable** that future economic benefits associated with the asset will flow to the micro-entity; and
 - (c) the cost of the asset can be measured reliably.

Measurement

- 27.3 A micro-entity shall measure biological assets at cost less any accumulated **depreciation** and any accumulated **impairment losses**.
- 27.4 Agricultural produce harvested from a micro-entity's biological assets shall be measured at the point of harvest at the lower of cost and estimated selling price less costs to complete and sell.

Such **measurement** is the cost at that date when applying Section 10 *Inventories* or another applicable section of this FRS.

Disclosures

- 27.5 A micro-entity shall disclose information in relation to the following items in accordance with the relevant appendix to Section 6 *Notes to the Financial Statements*:
- (a) financial commitments, guarantees and contingencies not recognised in the **statement of financial position** for the acquisition of a biological asset; and
 - (b) a biological asset or item of agricultural produce given as security in respect of its commitments, guarantees and contingencies.

Section 28

Transition to this FRS

Scope of this section

- 28.1 This section applies to a **first-time adopter of this FRS**, regardless of its previous financial reporting framework.
- 28.2 Notwithstanding the requirements in paragraphs 28.3 and 28.4, a **micro-entity** that has applied this FRS in a previous **reporting period**, but whose most recent previous annual **financial statements** were prepared in accordance with a different financial reporting framework, must either apply this section or else apply this FRS retrospectively in accordance with Section 8 *Accounting Policies, Changes in Estimates and Errors* as if the micro-entity had never stopped applying this FRS.

First-time adoption

- 28.3 A first-time adopter of this FRS shall apply this section in its first financial statements that conform to this FRS.
- 28.4 A micro-entity's first financial statements that conform to this FRS are the first financial statements prepared in accordance with this FRS if, for example, the micro-entity:
- (a) did not present financial statements for previous periods; or
 - (b) presented its most recent previous financial statements under previous UK and Republic of Ireland requirements or **FRS 102** and that are not consistent with this FRS in all respects.
- 28.5 Paragraph 3.9 defines a complete set of financial statements for a micro-entity.
- 28.6 Paragraph 3.10 requires a micro-entity to disclose, in a complete set of financial statements, comparative information in respect of the preceding period for all amounts presented in the financial statements. Therefore, a micro-entity's **date of transition** to this FRS is the beginning of the earliest period for which the micro-entity presents full comparative information in accordance with this FRS in its first financial statements that comply with this FRS.

Procedures for preparing financial statements at the date of transition

- 28.7 Except as provided in paragraphs 28.9 to 28.11, a micro-entity shall, in its opening **statement of financial position** as of its date of transition to this FRS (ie the beginning of the earliest period presented):
- (a) recognise all **assets** and **liabilities** whose **recognition** is required by this FRS;
 - (b) not recognise items as assets or liabilities if this FRS does not permit such recognition;
 - (c) reclassify items that it recognised under its previous financial reporting framework as one type of asset, liability or component of **equity**, but are a different type of asset, liability or component of equity under this FRS; and
 - (d) apply this FRS in **measuring** all recognised assets and liabilities.

This section does not require the opening statement of financial position to be presented.

28.8 The **accounting policies** that a micro-entity uses in its opening statement of financial position under this FRS may differ from those that it used for the same date using its previous financial reporting framework. The resulting adjustments arise from transactions, other events or conditions before the date of transition to this FRS. Therefore, a micro-entity shall recognise those adjustments directly in equity reserves at the date of transition to this FRS.

28.9 On first-time adoption of this FRS, a micro-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 **financial liabilities** derecognised under a micro-entity's previous financial reporting 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 a micro-entity's previous financial reporting framework, a micro-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) *Accounting estimates.*

28.10 A micro-entity may use one or more of the following exemptions in preparing its first financial statements that conform to this FRS:

(a) *Business combinations and goodwill*

A first-time adopter is not required to apply Section 14 *Business Combinations and Goodwill* to **business combinations** that were effected before the date of transition to this FRS. However, if a first-time adopter restates any business combination to comply with Section 14, it shall restate all later business combinations. If a first-time adopter does not apply Section 14 retrospectively, the first-time adopter shall recognise and measure all its assets and liabilities acquired or assumed in a past business combination at the date of transition to this FRS in accordance with paragraphs 28.7 to 28.9 or, if applicable, with paragraphs 28.10(b) to (h) except that no adjustment shall be made to the **carrying amount of goodwill**.

(b) *Share-based payment transactions*

A first-time adopter is not required to apply Section 21 *Share-based Payment* to obligations arising from **share-based payment transactions** that were settled before the date of transition to this FRS.

(c) *Investment properties*

A first-time adopter is not required to retrospectively apply paragraph 12.15 to determine the depreciated cost of each of the major components of an **investment property** at the date of transition to this FRS. If this exemption is applied, a first-time adopter shall:

- (i) Determine the total cost of the investment property including all of its components. Where no **depreciation** had been charged under the micro-entity's previous financial reporting framework, this can be calculated by reversing any revaluation **gains** or losses previously recognised in equity reserves.
- (ii) The cost of land, if any, shall be separated from buildings.
- (iii) Estimate the total depreciated cost of the investment property (excluding land) at the date of transition to this FRS, by recognising accumulated

depreciation since the date of initial acquisition calculated on the basis of the **useful life** of the most significant component of the item of investment property (eg the main structural elements of the building).

- (iv) A portion of the estimated total depreciated cost calculated in paragraph (iii) shall then be allocated to each of the other major components (ie excluding the most significant component identified above) to determine their depreciated cost. The allocation should be made on a reasonable and consistent basis. For example, a possible basis of allocation is to multiply the current cost to replace the component by the ratio of its remaining useful life to the expected useful life of a replacement component.
- (v) Any amount of the total depreciated cost not allocated under paragraph (iv) shall be allocated to the most significant component of the investment property.

(d) *Compound financial instruments*

Paragraph 17.11 requires a micro-entity to split a **compound financial instrument** into its liability and equity components at the date of issue. A first-time adopter need not separate those two components if the liability component is not outstanding at the date of transition to this FRS.

(e) *Arrangements containing a lease*

A first-time adopter may elect to determine whether an arrangement existing at the date of transition to this FRS contains a **lease** (see paragraph 15.4) on the basis of facts and circumstances existing at that date, rather than when the arrangement was entered into.

(f) *Decommissioning liabilities included in the cost of property, plant and equipment or investment property*

Paragraph 12.9(c) states that the cost of an item of **property, plant and equipment** or **investment property** includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which a micro-entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce **inventories** during that period. A first-time adopter may elect to measure this component of the cost of an item of property, plant and equipment or investment property at the date of transition to this FRS, rather than on the date(s) when the obligation initially arose.

(g) *Dormant companies*

A company within the **Act's** definition of a dormant company may elect to retain its accounting policies for reported assets, liabilities and equity at the date of transition to this FRS until there is any change to those balances or the company undertakes any new transactions.

(h) *Lease incentives*

A first-time adopter is not required to apply paragraphs 15.15 and 15.25 to **lease incentives** provided the term of the lease commenced before the date of transition to this FRS. The first-time adopter shall continue to recognise any residual benefit or cost associated with these lease incentives on the same basis as that applied at the date of transition to this FRS.

28.11 If it is **impracticable** for a micro-entity to make one or more of the adjustments required by paragraph 28.7 at the date of transition, the micro-entity shall apply paragraphs 28.7 to 28.10 for such adjustments in the earliest period for which it is practicable to do so.

28.12 Where applicable to the transactions, events or arrangements affected by applying these exemptions, a micro-entity may continue to use the exemptions that are applied

at the date of transition to this FRS when preparing subsequent financial statements, until such time when the assets and liabilities associated with those transactions, events or arrangements are derecognised.

Appendix I Glossary

This appendix is an integral part of this FRS.

accounting policies	The specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements .
accrual basis (of accounting)	The effects of transactions and other events are recognised when they occur (and not as cash or its equivalent is received or paid) and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate.
accumulating compensated absences	Compensated absences that are carried forward and can be used in future periods if the current period's entitlement is not used in full.
Act	The Companies Act 2006
active market	A market in which all the following conditions exist: (a) the items traded in the market are homogeneous; (b) willing buyers and sellers can normally be found at any time; and (c) prices are available to the public.
agent	An entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that an entity is acting as an agent is that the amount the entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer.
agricultural activity	The management by an entity of the biological transformation of biological assets for sale, into agricultural produce or into additional biological assets.
agricultural produce	The harvested product of the entity's biological assets .
amortisation	The systematic allocation of the depreciable amount of an asset over its useful life .
asset	A resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.
associate	An entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture .
biological asset	A living animal or plant.
borrowing costs	Interest and other costs incurred by an entity in connection with the borrowing of funds.

business	<p>An integrated set of activities and assets conducted and managed for the purpose of providing:</p> <p>(a) a return to investors; or</p> <p>(b) lower costs or other economic benefits directly and proportionately to policyholders or participants.</p> <p>A business generally consists of inputs, processes applied to those inputs, and resulting outputs that are, or will be, used to generate revenues. If goodwill is present in a transferred set of activities and assets, the transferred set shall be presumed to be a business.</p>
business combination	The bringing together of separate entities or businesses into one reporting entity.
carrying amount	The amount at which an asset or liability is recognised in the statement of financial position .
cash-generating unit	The smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.
cash-settled share-based payment transaction	A share-based payment transaction in which the entity acquires goods or services by incurring a liability to transfer cash or other assets to the supplier of those goods or services for amounts that are based on the price (or value) of equity instruments (including shares and share options) of the entity or another group entity.
change in accounting estimate	An adjustment of the carrying amount of an asset or a liability , or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors .
closing rate	The spot exchange rate at the end of the reporting period .
commencement of lease term	The date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial recognition of the lease (ie the recognition of the assets, liabilities, income or expenses resulting from the lease, as appropriate).
compound financial instrument	A financial instrument that, from the issuer's perspective, contains both a liability and an equity element.
consolidated financial statements	The financial statements of a parent and its subsidiaries presented as those of a single economic entity.
construction contract	A contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

constructive obligation	An obligation that derives from an entity's actions where: <ul style="list-style-type: none"> (a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and (b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities
contingent asset	A possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.
contingent liability	A contingent liability is either: <ul style="list-style-type: none"> (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or (b) a present obligation that arises from past events but is not recognised because: <ul style="list-style-type: none"> (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability.
contingent rent	That portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time (eg percentage of future sales, amount of future use, future price indices, and future market rates of interest).
control (of an entity)	The power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.
current tax	The amount of income tax payable (refundable) in respect of the taxable profit (tax loss) for the current period or past reporting periods .
date of transition	The beginning of the earliest period for which an entity presents full comparative information in a given standard in its first financial statements that comply with that standard.
deferred tax	Income tax payable (recoverable) in respect of the taxable profit (tax loss) for future reporting periods as a result of past transactions or events.
defined benefit plans	Post-employment benefit plans other than defined contribution plans .
defined contribution plans	Post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and has no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

depreciable amount	The cost of an asset , or other amount substituted for cost (in the financial statements), less its residual value .
depreciation	The systematic allocation of the depreciable amount of an asset over its useful life .
derecognition	The removal of a previously recognised asset or liability from an entity's statement of financial position .
derivative	Is a financial instrument with the following three characteristics: (a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable (sometimes called the 'underlying'), provided in the case of a non-financial variable that the variable is not specific to a party to the contract; (b) it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and (c) it is settled at a future date.
development	The application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.
employee benefits	All forms of consideration given by an entity in exchange for service rendered by employees.
equity	The residual interest in the assets of the entity after deducting all its liabilities .
equity-settled share-based payment transaction	A share-based payment transaction in which the entity: (a) receives goods or services as consideration for its own equity instruments (including shares or share options); or (b) receives goods or services but has no obligation to settle the transaction with the supplier.
errors	Omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that: (a) was available when financial statements for those periods were authorised for issue; and (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
expenses	Decreases in economic benefits during the reporting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity , other than those relating to distributions to equity investors.

fair value	The amount for which an asset could be exchanged, a liability settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction. In the absence of any specific guidance provided in the relevant section of this FRS, the guidance in paragraph 2.31 shall be used in determining fair value.
fair value less costs to sell	The amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.
finance lease	A lease that transfers substantially all the risks and rewards incidental to ownership of an asset . Title may or may not eventually be transferred. A lease that is not a finance lease is an operating lease .
financial asset	Any asset that is: <ul style="list-style-type: none"> (a) cash; (b) an equity instrument of another entity; (c) a contractual right: <ul style="list-style-type: none"> (i) to receive cash or another financial asset from another entity; or (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity; or (d) a contract that will or may be settled in the entity's own equity instruments and is: <ul style="list-style-type: none"> (i) a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or (ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.
financial guarantee contract	A contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the original or modified terms of a debt instrument.
financial instrument	A contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

financial liability	<p>Any liability that is:</p> <p>(a) a contractual obligation:</p> <p>(i) to deliver cash or another financial asset to another entity; or</p> <p>(ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity, or</p> <p>(b) a contract that will or may be settled in the entity's own equity instruments and is:</p> <p>(i) a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or</p> <p>(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.</p>
financial position	The relationship of the assets, liabilities and equity of an entity as reported in the statement of financial position .
financial statements	A structured presentation of the financial position and financial performance of an entity.
financing activities	Activities that result in changes in the size and composition of the contributed equity and borrowings of the entity.
first-time adopter of this FRS	An entity that presents its first annual financial statements that conform to this FRS, regardless of its previous financial reporting framework.
fixed assets	Assets of an entity which are intended for use on a continuing basis in the entity's activities.
FRS 102	FRS 102 <i>The Financial Reporting Standard applicable in the UK and Republic of Ireland</i>
gains	Increases in economic benefits that meet the definition of income but are not revenue .
goodwill	Future economic benefits arising from assets that are not capable of being individually identified and separately recognised.
government grant	<p>Assistance by government in the form of a transfer of resources to an entity in return for past or future compliance with specified conditions relating to the operating activities of the entity.</p> <p>Government refers to government, government agencies and similar bodies whether local, national or international.</p>

grant date	The date at which the entity and another party (including an employee) agree to a share-based payment arrangement , being when the entity and the counterparty have a shared understanding of the terms and conditions of the arrangement. At grant date the entity confers on the counterparty the right to cash, other assets , or equity instruments of the entity, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.
gross investment in a lease	The aggregate of: (a) the minimum lease payments receivable by the lessor under a finance lease ; and (b) any unguaranteed residual value accruing to the lessor.
impairment loss	The amount by which the carrying amount of an asset exceeds: in the case of inventories , its selling price less costs to complete and sell; in the case of financial assets the amounts as set out in paragraph 9.18; or in the case of any other asset, its recoverable amount .
impracticable	Applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so.
inception of the lease	The earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease .
income	Increases in economic benefits during the reporting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity , other than those relating to contributions from equity investors.
income statement	Financial statement that presents all items of income and expense recognised in a reporting period (referred to as the profit and loss account in the Act).
income tax	All domestic and foreign taxes that are based on taxable profits . Income tax also includes taxes, such as withholding taxes, that are payable by a subsidiary , associate or joint venture on distributions to the reporting entity.
intangible asset	An identifiable non-monetary asset without physical substance. Such an asset is identifiable when: (a) it is separable, ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or liability ; or (b) it arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

interest rate implicit in the lease	The discount rate that, at the inception of the lease , causes the aggregate present value of: (a) the minimum lease payments ; and (b) the unguaranteed residual value to be equal to the sum of: (i) the fair value of the leased asset ; and (ii) any initial direct costs of the lessor.
inventories	Assets: (a) held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.
investment property	Property (land or a building, or part of a building, or both) held by the owner or by the lessee under a finance lease to earn rentals or for capital appreciation or both, rather than for: (a) use in the production or supply of goods or services or for administrative purposes; or (b) sale in the ordinary course of business.
joint control	The contractually agreed sharing of control over an economic activity. It exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers).
joint venture	A contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control . Joint ventures can take the form of jointly controlled operations, jointly controlled assets, or jointly controlled entities .
jointly controlled entity	A joint venture that involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.
lease	An agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.
lease incentives	Incentives provided by the lessor to the lessee to enter into a new or renew an operating lease . Examples of such incentives include up-front cash payments to the lessee, the reimbursement or assumption by the lessor of costs of the lessee (such as relocation costs, leasehold improvements and costs associated with pre-existing lease commitments of the lessee), or initial periods of the lease provided by the lessor rent-free or at a reduced rent.
lease term	The non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

lessee's incremental borrowing rate (of interest)	The rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease , the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset .
liability	A present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.
limited liability partnership (LLP)	A limited liability partnership formed under the Limited Liability Partnerships Act 2000 or the Limited Liability Partnerships Act (Northern Ireland) 2002.
material	Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the financial statements . Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.
measurement	The process of determining the monetary amounts at which the elements of the financial statements are to be recognised and carried in the statement of financial position and income statement .
micro-entity	A micro-entity is: (a) a company meeting the definition of a micro-entity as set out in section 384A of the Act ¹⁸ , and not prevented from applying the micro-entity provisions by section 384B of the Act; (b) an LLP which qualifies as a micro-entity and is not prevented from applying the micro-entity provisions in accordance with Regulation 5A of the <i>Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008</i> (SI 2008/1911); or (c) A qualifying partnership that would meet the definition of a micro-entity as set out in section 384A of the Act, and not be prevented from applying the micro-entity provisions by section 384B of the Act, if the partnership were a company.
micro-entity minimum accounting items	The items of information required under the micro-entities regime to be contained in the financial statements of a micro-entity . These are set out in Section 3 <i>Financial Statement Presentation</i> , Section 4 <i>Statement of Financial Position</i> , Section 5 <i>Income Statement</i> and Section 6 <i>Notes to the Financial Statements</i> of this FRS.
micro-entity provisions	(a) Any provisions of Part 15, Part 16 or regulations made under Part 15 of the Act ¹⁹ ; or (b) any provisions of the Small LLP Regulations , relating specifically to the individual accounts of an entity which qualifies as a micro-entity .

¹⁸ Irish micro-entities (including partnerships that are required to comply with Part 6 of the Companies Act 2014, by virtue of the European Communities (Accounts) Regulations 1993 (as amended)) shall refer to section 280D of the Companies Act 2014.

¹⁹ Irish micro-entities shall refer to the relevant provisions of Part 6 of, and Schedule 3B to, the Companies Act 2014.

micro-entities regime	The legal requirements and exemptions relating to the preparation of the financial statements of micro-entities as set out in the Act²⁰ , the Small Companies Regulations and the Small LLP Regulations .
minimum lease payments	<p>The payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:</p> <p>(a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or</p> <p>(b) for a lessor, any residual value guaranteed to the lessor by:</p> <p>(i) the lessee;</p> <p>(ii) a party related to the lessee; or</p> <p>(iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.</p> <p>However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.</p>
monetary items	Units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.
multi-employer (benefit) plans	<p>Defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:</p> <p>(a) pool the assets contributed by various entities that are not under common control; and</p> <p>(b) use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees concerned.</p>
net investment in a lease	The gross investment in a lease discounted at the interest rate implicit in the lease .
non-exchange transaction	A transaction whereby an entity receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.
notes (to the financial statements prepared under this FRS)	Notes contain information in addition to that presented in the statement of financial position and income statement . Notes are required to be presented at the foot of the statement of financial position for micro-entities in the UK.
onerous contract	A contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

²⁰ Irish micro-entities shall refer to the Companies Act 2014.

operating activities	The principal revenue-producing activities of the entity and other activities that are not investing or financing activities .
operating lease	A lease that does not transfer substantially all the risks and rewards incidental to ownership. A lease that is not an operating lease is a finance lease .
ordinary share	An equity instrument that is subordinate to all other classes of equity instrument.
owners	Holders of instruments classified as equity .
parent	An entity that has one or more subsidiaries .
performance	The relationship of the income and expenses of a micro-entity , as reported in the income statement .
post-employment benefits	Employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment.
post-employment benefit plans	Formal or informal arrangements under which an entity provides post-employment benefits for one or more employees.
present value	A current estimate of the present discounted value of the future net cash flows in the normal course of business.
principal	An entity is acting as a principal when it has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. Features that indicate that an entity is acting as a principal include: <ul style="list-style-type: none"> (a) the entity has the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer; (b) the entity has inventory risk before or after the customer order, during shipping or on return; (c) the entity has latitude in establishing prices, either directly or indirectly, for example by providing additional goods or services; and (d) the entity bears the customer's credit risk for the amount receivable from the customer.
probable	More likely than not.
profit or loss	The total of income less expenses .
property, plant and equipment	Tangible assets that: <ul style="list-style-type: none"> (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and (b) are expected to be used during more than one period.
prospectively (applying a change in accounting policy)	Applying the new accounting policy to transactions, other events and conditions occurring after the date as at which the policy is changed.
provision	A liability of uncertain timing or amount.

prudence	The inclusion of a degree of caution in the exercise of the judgements needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.
qualifying partnership	A partnership meeting the definition of a qualifying partnership as set out in the Partnerships (Accounts) Regulations 2008 (SI 2008/569).
recognition	The process of incorporating in the statement of financial position or income statement an item that meets the definition of an asset, liability, equity, income or expense and satisfies the following criteria: (a) it is probable that any future economic benefit associated with the item will flow to or from the entity ; and (b) the item has a cost or value that can be measured with reliability.
recoverable amount	The higher of an asset's (or cash-generating unit's) fair value less costs to sell and its value in use .
reporting date	The end of the latest period covered by financial statements .
reporting period	The period covered by financial statements .
research	Original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
residual value (of an asset)	The estimated amount that an entity would currently obtain from disposal of an asset , after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life .
restructuring	A restructuring is a programme that is planned and controlled by management and materially changes either: (a) the scope of a business undertaken by an entity; or (b) the manner in which that business is conducted.
retrospective application (of an accounting policy)	Applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.
revenue	The gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increases in equity , other than increases relating to contributions from equity participants.
share-based payment arrangement	An agreement between the micro-entity (or another group entity or any shareholder of any group entity) and another party (including an employee) that entitles the other party to receive: (a) cash or other assets of the micro-entity for amounts that are based on the price (or value) of equity instruments (including shares or share options) of the micro-entity or another group entity; or (b) equity instruments (including shares or share options) of the micro-entity or another group entity, provided the specified vesting conditions, if any, are met.

share-based payment transaction	A transaction in which the entity: (a) receives goods or services from the supplier of those goods or services (including an employee) in a share-based payment arrangement ; or (b) incurs an obligation to settle the transaction with the supplier in a share-based payment arrangement when another group entity receives those goods or services.
share option	A contract that gives the holder the right, but not the obligation, to subscribe to the entity's shares at a fixed or determinable price for a specific period of time.
significant influence	Is the power to participate in the financial and operating policy decisions of the associate but is not control or joint control over those policies.
Small Companies Regulations	The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (SI 2008/409)
Small LLP Regulations	The Small Limited Liability Partnership (Accounts) Regulations 2008 (SI 2008/1912)
state (employee benefit) plan	Employee benefit plans established by legislation to cover all entities (or all entities in a particular category, for example a specific industry) and operated by national or local government or by another body (for example an autonomous agency created specifically for this purpose) which is not subject to control or influence by the reporting entity.
statement of financial position	Financial statement that presents the relationship of an entity's assets, liabilities and equity as of a specific date (referred to as the balance sheet in the Act).
subsidiary	An entity, including an unincorporated entity such as a partnership, that is controlled by another entity (known as the parent).
substantively enacted	Tax rates shall be regarded as substantively enacted when the remaining stages of the enactment process historically have not affected the outcome and are unlikely to do so. A UK tax rate shall be regarded as having been substantively enacted if it is included in either: (a) a Bill that has been passed by the House of Commons and is awaiting only passage through the House of Lords and Royal Assent; or (b) a resolution having statutory effect that has been passed under the Provisional Collection of Taxes Act 1968. (Such a resolution could be used to collect taxes at a new rate before that rate has been enacted. In practice, corporation tax rates are now set a year ahead to avoid having to invoke the Provisional Collection of Taxes Act for the quarterly payment system.) A Republic of Ireland tax rate can be regarded as having been substantively enacted if it is included in a Bill that has been passed by the Dail.
tax expense	The aggregate amount included in profit or loss or equity for the reporting period in respect of current tax .

taxable profit (tax loss)	The profit (loss) for a reporting period upon which income taxes are payable or recoverable, determined in accordance with the rules established by the taxation authorities. Taxable profit equals taxable income less amounts deductible from taxable income.
termination benefits	Employee benefits provided in exchange for the termination of an employee's employment as a result of either: (a) an entity's decision to terminate an employee's employment before the normal retirement date; or (b) an employee's decision to accept voluntary redundancy in exchange for those benefits.
transaction costs (financial instruments)	Incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability , or the issue or reacquisition of an entity's own equity instrument. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial asset or financial liability, or had not issued or reacquired its own equity instrument.
treasury shares	An entity's own equity instruments that are held by the entity.
turnover	The amounts derived from the provision of goods and services after deduction of: (a) trade discounts; (b) value added tax; and (c) any other taxes based on the amounts so derived.
useful life	The period over which an asset is expected to be available for use by an entity or the number of production or similar units expected to be obtained from the asset by an entity.
value in use	The present value of the future cash flows expected to be derived from an asset or cash-generating unit .
venturer	A party to a joint venture that has joint control over that joint venture.
vest	Become an entitlement. Under a share-based payment arrangement , a counterparty's right to receive cash, other assets or equity instruments of the entity vests when the counterparty's entitlement is no longer conditional on the satisfaction of any vesting conditions.

Appendix II

Table of equivalence for company law terminology

The following table compares company law terminology with broadly equivalent terminology used in this FRS.

Company law terminology	FRS 105 terminology
Accounting reference date	Reporting date
Accounts	Financial statements
Balance sheet	Statement of financial position
Capital and reserves	Equity
Cash at bank and in hand	Cash
Debtors	Trade receivables
Diminution in value [of assets]	Impairment
Expenses	Charges
Financial year	Reporting period
Financial year end date	Reporting date
Holding undertaking	Parent
Net realisable value [of any current asset]	Estimated selling price less costs to complete and sell
Profit and loss account	Income statement
Stocks	Inventories
Subsidiary undertaking	Subsidiary
Tangible assets	Includes: property, plant and equipment and investment property
Trade creditors	Trade payables

Appendix III

Note on legal requirements

Introduction

- A3.1 This appendix provides an overview of how the requirements of FRS 105 address UK company law requirements. It is therefore written from the perspective of a company to which *The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008* (SI 2008/409) amended by *The Small Companies (Micro-Entities' Accounts) Regulations 2013* (SI 2013/3008) and *The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015* (SI 2015/980) apply. The same provisions generally apply to limited liability partnerships (LLPs) and qualifying partnerships following amendments to legislation made in *The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016* (SI 2016/575) (see paragraph A3.6). Appendix IV discusses the Republic of Ireland legal references.
- A3.2 *The Small Companies (Micro-Entities' Accounts) Regulations 2013* were made in November 2013 and apply to the financial statements of micro-entities for accounting periods ending on or after 30 September 2013 for companies filing their accounts on or after 1 December 2013.
- A3.3 The definition of a micro-entity is contained in sections 384A and 384B of the Companies Act 2006 (the Act). The qualifying conditions are met by a company in a year in which it does not exceed two or more of the following criteria:
- | | |
|-------------------------|----------|
| (a) Turnover | £632,000 |
| (b) Balance sheet total | £316,000 |
| (c) Number of employees | 10 |
- A3.4 For any company, other than a newly incorporated company, to qualify as a micro-entity, the qualifying conditions must be met for two consecutive years. A company will cease to qualify as a micro-entity if it fails to meet the qualifying conditions for two consecutive years. However, if a company which qualified as a micro-entity in one period no longer meets the criteria for a micro-entity in the next period, the company may continue to claim the exemptions available in the next period. If that company then reverts back to being a micro-entity by meeting the criteria, the exemptions will continue uninterrupted.
- A3.5 Certain companies are excluded by section 384B of the Act from being treated as micro-entities, including those excluded from the small companies regime for reasons of public interest (as set out in section 384), certain financial institutions, charities, those voluntarily preparing group accounts and those included in group accounts. The Act should be referred to for a full list of excluded companies.
- A3.6 *The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016* (SI 2016/575) were made in May 2016 and extend the micro-entity regime to LLPs and qualifying partnerships for accounting periods beginning on or after 1 January 2016 with early application permitted for accounting periods beginning on or after 1 January 2015. LLPs and qualifying partnerships are eligible to apply the micro-entities regime, provided they meet the relevant conditions, which mirror the requirements of sections 384A and 384B of the Act for companies. Entities that are not companies, LLPs or qualifying partnerships do not meet the definition of a micro-entity.

Applicable accounting framework

A3.7 Accounts prepared in accordance with FRS 105 are classified as 'Companies Act individual accounts' for the purposes of section 395 of the Act and are therefore required to comply with the applicable provisions of Parts 15 and 16 of the Act and with the Regulations referred to in paragraph A3.1.

Fair value at initial recognition

A3.8 *The Small Companies (Micro-Entities' Accounts) Regulations 2013* state that micro-entities are not permitted to apply the Alternative Accounting Rules or the Fair Value Rules as set out in company law. Therefore, micro-entities are only permitted to apply the Historical Cost Accounting Rules.

A3.9 FRS 105 states that certain types of assets and liabilities must be measured at fair value at initial recognition, for example inventories acquired through a non-exchange transaction. This does not breach the prohibition against fair value accounting as this use of a fair value is a method of estimating cost at initial recognition.

True and fair view

A3.10 FRS 105 is an accounting standard and all accounting standards issued by the Financial Reporting Council are applicable to the preparation of financial statements that are intended to give a true and fair view. Financial statements of a micro-entity that include the minimum accounting items specified by *The Small Companies (Micro-entities' Accounts) Regulations 2013* are presumed in law to give a true and fair view.

Distributable profits

A3.11 The determination of profits available for distribution is a complex area where accounting and company law interface. In determining profits available for distribution any entity may refer to Technical Release 02/17BL *Guidance on realised and distributable profits under the Companies Act 2006* issued by the Institute of Chartered Accountants in England and Wales and the Institute of Chartered Accountants of Scotland, or any successor document, to determine profits available for distribution.

Appendix IV

Republic of Ireland legal references

Introduction

A4.1 The table below outlines the provisions in the Companies Act 2014 corresponding to the provisions of the UK Companies Act 2006 (the Act) referred to in this FRS, unless the UK legal reference in this FRS is already footnoted with an Irish reference, or written separately in an Irish context²¹. References to the Companies Act 2014 in this FRS, including in this appendix, are to the Companies Act 2014, as amended by the Companies (Accounting) Act 2017 and the Companies (Amendment) Act 2017.

Company law is structured differently in the two jurisdictions. The Companies Act 2014 consists of 26²² 'Parts' such that:

- Parts 1 to 14 (along with the relevant Schedules) apply to private companies limited by shares (LTDs);
- Parts 16 to 24 cover the other types of companies under the Companies Act 2014 – eg designated activity companies (DACs) and companies limited by guarantee (CLGs); and
- Parts 15, 25 and 26 cover Functions of the Registrar and of Regulatory and Advisory Bodies; Miscellaneous provisions; and reports on Payments to Governments, respectively.

The provisions of Parts 1 to 14 also apply to the other types of companies, unless disapplied or modified by the relevant Part (eg Part 16 for DACs). References in the text of this FRS, including in the table below, are to the primary source of requirements in Parts 1 to 14 of, and the relevant Schedules to, the Companies Act 2014 as pertaining to a private company limited by shares. For other company types, reference should be made to the relevant Part of the Companies Act 2014 as applicable.

A4.2 General references are made in this FRS to UK legislation such as the 'Companies Act 2006', 'the Act', 'the Small Companies Regulations', 'the Regulations', 'The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (SI 2008/409)', 'The Small Companies (Micro-Entities' Accounts) Regulations 2013 (SI 2013/3008)' and 'The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015 (SI 2015/980)'. In an Irish context reference should be made to the relevant sections and paragraphs of Irish company law. Such general references are not dealt with in the table below.

A4.3 There are a number of references in this FRS to Limited Liability Partnerships (LLPs) in the UK and legislation relating thereto. There is no such equivalent legislation in Ireland (and these references, therefore, are not included in the table below), however, certain Irish partnerships are required to comply with Part 6 of the Companies Act 2014 by virtue of the European Communities (Accounts) Regulations 1993 (as amended).

²¹ Similarly, corresponding Irish legal references are not provided in the table for the UK legal references in Appendix A to Section 6 *Notes to the Financial Statements*. Appendix A to Section 6 sets out the company law disclosure requirements for micro-entities in the UK, while Appendix B to Section 6 sets out the company law disclosure requirements for micro-entities in the Republic of Ireland.

²² For information, the Companies (Statutory Audits) Bill 2017 proposes the insertion of a new Part 27 to Companies Act 2014 dealing with statutory audit. This Bill is due to be enacted during 2018.

Micro companies under Irish company law

A4.4 The Companies (Accounting) Act 2017 amended the Companies Act 2014 to introduce the micro companies regime (which is similar but not identical to that in the UK) into Irish company law. Where a company qualifies as a micro company in accordance with section 280D of the Companies Act 2014, as may be appropriate, then different rules may be applied (referred to as the 'micro companies regime' in the Companies Act 2014) by the company in respect of financial statements and reports for a financial year, in relation to which that company qualifies as a micro company (section 280E of the Companies Act 2014).

The definition of a micro company is contained in section 280D of the Companies Act 2014. This section also details certain companies that cannot qualify as a micro company and are therefore excluded from the micro companies regime, as outlined below.

Subject to certain conditions and exclusions as noted in section 280D, the qualifying conditions are met by a company if, in relation to a financial year, it qualifies for the small companies regime and does not exceed two or more of the following criteria:

(a) Turnover	€700,000
(b) Balance sheet total	€350,000
(c) Average number of employees	10

A newly incorporated company must meet the qualifying conditions in relation to its first financial year to qualify as a micro company.

In relation to a subsequent financial year (referred to as a 'relevant year') the qualifying conditions must be met by a company (i) in respect of the relevant year and the financial year immediately preceding the relevant year; (ii) in respect of the relevant year and the company qualified as a micro company in relation to the financial year immediately preceding the relevant year; or (iii) in the financial year immediately preceding the relevant year and the company qualified as a micro company in relation to that preceding financial year.

Certain companies are excluded by section 280D of the Companies Act 2014 from being treated as micro companies, including those excluded from the small companies regime (as set out in sections 280A and 280B), investment undertakings, financial holding undertakings, holding companies voluntarily preparing consolidated financial statements and subsidiaries included in consolidated financial statements. The Companies Act 2014 should be referred to for a full list of excluded companies.

Applicable accounting framework

A4.5 Financial statements prepared in accordance with FRS 105 are classified as 'Companies Act entity financial statements' for the purposes of section 290 of the Companies Act 2014 and are therefore required to comply with the applicable provisions of Part 6 of, and Schedule 3B to, the Companies Act 2014.

Other notes

Fair value at initial recognition

A4.6 Under Schedule 3B to the Companies Act 2014 micro-entities are not permitted to apply the Alternative Accounting Rules or the Fair Value Rules as set out in company

law. Therefore micro-entities are only permitted to apply the Historical Cost Accounting Rules.

- A4.7 FRS 105 states that certain types of assets and liabilities must be measured at fair value at initial recognition, for example inventories acquired through a non-exchange transaction. This does not breach the prohibition against fair value accounting as this use of a fair value is a method of estimating cost at initial recognition.

True and fair view

- A4.8 In the case of a micro-entity that elects to adopt the micro-entities regime, section 291(6A) of the Companies Act 2014 provides that it shall be presumed that compliance with (a) Schedule 3B, (b) applicable accounting standards (in this case, this FRS), and (c) the other provisions of the Companies Act 2014, shall be sufficient to give a true and fair view of the assets, liabilities and financial position as at the financial year end date and of the profit or loss for the financial year.

Other

- A4.9 The following tables are intended as a reference guide to the corresponding or similar provisions in Irish law and do not purport to be complete. As such, it may be necessary to make reference to other Irish law as appropriate. It should be noted too that not all Irish legal provisions are equivalent to the corresponding UK legal provisions and reference should be made to Irish law for an understanding of the relevant requirements. It should also be noted that various sections and paragraphs referenced may have been amended by legislation subsequent to the issuing of this FRS, and reference should be made to such amended text where applicable.

Appendix I Glossary

	UK references	Rol references
Paragraph	Act (unless otherwise stated)	Companies Act 2014
'qualifying partnership'	A partnership meeting the definition of a qualifying partnership as set out in the Partnerships (Accounts) Regulations 2008 (SI 2008/569).	See Irish footnote to definition of micro-entity. Certain partnerships are required to comply with Part 6 of the Companies Act 2014 by virtue of the European Communities (Accounts) Regulations 1993 (as amended).

Appendix III Note on legal requirements

	UK references	RoI references
Paragraph	Act (unless otherwise stated)	Companies Act 2014
A3.3	Sections 384A and 384B	Refer to A4.4 in the Introduction to this Appendix.
A3.5	Sections 384B and 384	Refer to A4.4 in the Introduction to this Appendix.
A3.7	Section 395	Refer to A4.5 in the Introduction to this Appendix.
A3.7	Parts 15 and 16	Refer to A4.5 in the Introduction to this Appendix.
A3.8	<i>'The Small Companies (Micro-Entities' Accounts) Regulations 2013 state that....'</i>	Refer to A4.6 in the Introduction to this Appendix.
A3.10	<i>'Financial statements of a micro-entity that include the minimum accounting items specified by The Small Companies (Micro-Entities' Accounts) Regulations 2013 are presumed in law to give a true and fair view.'</i>	Refer to A4.8 in the Introduction to this Appendix.

Approval by the FRC

FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* was approved for issue by the Financial Reporting Council on 1 July 2015.

Amendments to FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – Limited Liability Partnerships and Qualifying Partnerships was approved for issue by the Financial Reporting Council for issue on 17 May 2016.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Triennial review 2017 – Incremental improvements and clarifications was approved for issue by the Financial Reporting Council on 6 December 2017.

Basis for Conclusions

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

This Basis for Conclusions²³ accompanies, but is not part of, FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime and summarises the main issues considered by the Financial Reporting Council (FRC) in developing FRS 105.

Feedback from a number of exposure drafts and consultation documents has been considered in the development of FRS 105 (see Table 1 at the end of this Basis for Conclusions). Unless otherwise stated, respondents to the consultations supported the proposals made; detailed feedback statements to all consultations are available on the FRC website.

The effective dates and any transitional arrangements for FRS 105, and any amendments to it, are set out in the FRS.

- 1 In November 2013, *The Small Companies (Micro-entities' Accounts) Regulations 2013* (SI 2013/3008) were made which amended *The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008* (SI 2008/409). The amendment introduced a new optional reporting framework for companies that meet the qualifying criteria of a micro-entity. Initially amendments were made to the FRSSE to accommodate the new regime and subsequently FRS 105 was developed in response to this change of UK company law.
- 2 FRS 105 is based on FRS 102, but its accounting requirements are adapted to satisfy the legal requirements applicable to micro-entities and to reflect the simpler nature and smaller size of micro-entities.
- 3 The application of the micro-entities regime is optional; however, a micro-entity that chooses to prepare its financial statements in accordance with the micro-entities regime is required to apply FRS 105. A company or LLP that qualifies for this regime, but chooses not to apply it, is required to apply another financial reporting standard (as set out in FRS 100 *Application of Financial Reporting Requirements*).

Objective

- 4 In developing financial reporting standards, the overriding objective of the FRC is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.
- 5 In achieving this objective, the FRC aims to provide succinct financial reporting standards that:
 - (a) have consistency with global accounting standards through the application of an IFRS-based solution unless an alternative clearly better meets the overriding objective;
 - (b) balance improvement, through reflecting up-to-date thinking and developments in the way businesses operate and the transactions they undertake, with stability;
 - (c) balance consistent principles for accounting by all UK and Republic of Ireland entities with proportionate and practical solutions, based on size, complexity, public interest and users' information needs;

²³ This Basis for Conclusions replaces the Accounting Council's Advice and the Corporate Reporting Council's Advice included in previous editions of FRS 105.

- (d) promote efficiency within groups; and
- (e) are cost-effective to apply.

Recognition and measurement requirements consistent with FRS 102

- 6 The reporting requirements for all entities (including small and micro-entities) are based on FRS 102 because it improves consistency across the financial reporting framework in the UK and Republic of Ireland.
- 7 To that end, FRS 105 applies the recognition and measurement requirements of FRS 102, adapted when necessary to reflect the legal requirements of the micro-entity regime and simplified further to reflect the size and nature of micro-entities.
- 8 It was noted that some of the simplifications made in FRS 105, including the omission of some of the disclosures required by FRS 102, would not have been introduced if they had not been necessary to ensure legal compliance with the micro-entities regime. For example, the FRC continues to believe that investment property should always, when practicable, be measured at fair value as this provides more relevant information to users of the financial statements of a company's financial position and performance. However, company law prohibits the revaluation of any asset by micro-entities and instead requires that fixed assets are measured at cost less depreciation and impairment.

Structure and language of FRS 105

- 9 A number of respondents to the initial consultations suggested that the accessibility of FRS 105 could be enhanced by departing from the section and paragraph numbering of FRS 102. Consequently, FRS 105 maintains consistency with the language and terminology used in FRS 102 (when possible) but uses its own unique section and paragraph numbering.

Amendments to FRS 102 to align FRS 105 with the legal requirements

Scope

- 10 FRS 105 is applicable to the preparation of the financial statements of a micro-entity which are presumed in law to give a true and fair view in accordance with the micro-entities regime.
- 11 The availability of the micro-entities regime is restricted to the smallest of companies and some types of entities are excluded. For example, charities and financial institutions are ineligible to report under this regime. For that reason, in contrast to FRS 102, FRS 105 does not contain any specific requirements that apply only to these entities.
- 12 The micro-entities regime is not available to entities that are required or choose to prepare consolidated financial statements. Therefore, FRS 105 does not contain accounting requirements that are relevant to the preparation of consolidated financial statements.
- 13 A respondent queried whether FRS 105 could be applied to financial statements prepared for the purposes of submission to the tax authorities by unincorporated businesses and individuals that, if they were companies, would be eligible to apply the micro-entities regime. The form and content of financial statements prepared for tax purposes is a matter for the relevant tax authorities to determine and therefore it is not possible to explicitly permit or prohibit the application of FRS 105 for such purposes.

Presentation and disclosure

- 14 The micro-entities regime specifies certain minimum presentation and disclosure requirements. Financial statements that include the prescribed minimum accounting items are presumed in law to give a true and fair view and no further disclosures need to be made. FRS 105 reflects the legal minimum presentation and disclosure requirements.

Recognition and measurement

- 15 The micro-entities regime prohibits the use of the Alternative Accounting Rules or the Fair Value Rules set out in company law and therefore micro-entities are not permitted to revalue or subsequently measure assets or liabilities at fair value. To take account of the legal restrictions on fair value measurement, FRS 105 does not allow the subsequent measurement of any asset or liability at fair value. This affects in particular financial instruments and investment properties which a micro-entity has to measure at cost and depreciated cost respectively.

Further simplifications over and above the legal requirements

- 16 The micro-entities regime is intended to be deregulatory and therefore some of the accounting requirements applicable under FRS 102 were simplified for inclusion in FRS 105. Simplifications were made if:
- (a) the benefits of applying the accounting treatment in FRS 102 do not outweigh the burden for micro-entities and an alternative, more straightforward, treatment could be identified;
 - (b) the lack of detail in the formats of the financial statements and/or supporting disclosures would limit the understanding of the financial information presented; and/or
 - (c) transactions occur infrequently amongst micro-entities.
- 17 It was noted that permitting accounting policy options in FRS 105 would add complexity for preparers of a micro-entity's financial statements and could cause confusion to users due to the lack of detail in the formats of the financial statements and supporting disclosures to explain the policy choice taken. As a result, FRS 105 does not contain accounting policy options, except on first-time adoption of FRS 105, and in all cases, FRS 105 mandates the most straightforward and easy to apply option.
- 18 First-time adopters of FRS 105 are allowed to choose whether to apply the requirements of FRS 105 fully retrospectively or whether to apply one or more of the transitional exemptions. Although this introduced a degree of complexity for preparers and users, transitional exemptions are important for a smooth transition and not allowing a choice disadvantages micro-entities unnecessarily over entities that transition to FRS 102.
- 19 The key areas where simplifications were made were are follows:
- (a) Prohibition of accounting for deferred taxation on the basis that this is a complex area of accounting and the lack of disclosure in a micro-entity's financial statements would make it impossible to distinguish between current and deferred tax.
 - (b) Prohibition of accounting for equity-settled share-based payments prior to the issue of the shares, because of the prohibition on using fair value measurements and the lack of supporting disclosure in the financial statements.
 - (c) A requirement that the contributions payable to any post-employment benefit plans are accounted for as an expense, subject to a requirement for defined benefit plans to recognise a liability for a schedule of contributions to the extent that it relates to the

deficit. The simplification was made on the basis that very few micro-entities have defined benefit pension schemes.

- (d) The distinction between functional and presentation currency is removed as it will be very rare for micro-entities to have a different functional and presentational currency.
- (e) A requirement to use contracted rates to translate foreign currency denominated assets and liabilities rather than spot rates. This will simplify the accounting when micro-entities enter into foreign currency forward contracts.
- (f) All borrowing and development costs must be expensed, because this is the simplest treatment for these costs.
- (g) The application of the accrual model to account for government grants is mandated because this is considered the simplest method of accounting for these transactions.
- (h) Simplifications in the accounting for financial instruments in relation to the allocation of interest and transaction costs. The effective interest rate method is considered too onerous to apply by micro-entities.
- (i) Removal of the requirement to impute a market-rate of interest in lending arrangements conducted at non-market rates because the costs of mandating this requirement would exceed the benefits.
- (j) Simplified requirements for classifying financial instruments as equity or debt because most micro-entities will issue simple equity instruments.
- (k) Prohibition of the recognition of separately identifiable intangible assets in a trade and asset acquisition because these are not required items in the financial statements formats.
- (l) Removal of the requirements concerning accounting for hyperinflation because this is unlikely to be an issue for micro-entities.
- (m) Removal of accounting requirements relating to specialised activities including extractive activities, service concessions, heritage assets and funding commitments because micro-entities will not typically enter into these transactions.

Deferred tax

- 20 Some respondents highlighted that the recognition of deferred tax should be permitted or required in FRS 105. However, it was concluded that without additional disclosure the benefits of requiring micro-entities to account for deferred tax do not exceed the costs.

Government grants

- 21 Respondents' views on whether FRS 105 should require the performance or accrual model in relation to grant accounting were divided. The evidence provided by respondents suggested that the accrual model is, in practice, be easier to apply than the performance model and therefore FRS 105 mandates the use of the accrual model.

Determining accounting policies when FRS 105 does not contain requirements

- 22 A micro-entity that enters into a transaction that is not specifically covered in FRS 105 is required to refer to the concepts and pervasive principles set out in Section 2 *Concepts and Pervasive Principles* in determining its accounting policies. It was noted that micro-entities are not required to refer to other accounting standards or authoritative guidance because these requirements may be inconsistent with the legal requirements of the micro-entities regime.

Transitional arrangements – Fair value / revaluation as deemed cost

- 23 The micro-entities regime requires micro-entities to apply the historical cost accounting rules, which require fixed assets to be initially recognised at purchase price or production cost. Therefore it would be inconsistent with the legal framework for micro-entities to provide a transitional exemption to allow micro-entities to carry forward previous revaluations of property, plant and equipment or the fair value of investment properties or investments in shares as deemed cost.
- 24 FRS 105 provides a transitional exemption in respect of the determination of the depreciated historical cost of investment properties. Under the transitional exemption a micro-entity is permitted, for the purposes of estimating accumulated depreciation at the date of transition, to treat an investment property as if it were a single asset with a useful economic life equal to that of its most significant component, which is likely to be comprised of its main structural elements such as foundations, walls etc. This exempts a micro-entity from having to determine the historical cost of each component that has been replaced in the past and the depreciation that would have been charged since their initial recognition.
- 25 It was noted that the micro-entities regime is optional and that if a micro-entity wishes to retain revalued amounts in its financial statement it could apply the small companies regime.

Residents' management companies (FRED 50)

- 26 It was noted that no clear consensus existed amongst respondents on the appropriate basis of accounting in the statutory financial statements of residents' management companies²⁴ that hold service charge monies on trust in accordance with section 42 of the Landlord and Tenant Act 1987. However, there was general agreement amongst respondents that no change should be made to FRS 105, or any other relevant financial reporting standard (including FRS 102), to address such a narrow and sector-specific issue.
- 27 The case for further intervention by reference to the FRC's published *Principles for the development of Codes, Standards and Guidance*²⁵ was assessed and, in particular, the extent to which the anticipated benefits from any changes to current practices would outweigh the costs incurred by the entities involved. The FRC agreed that this matter did not merit a change in accounting standards, and therefore no changes were made to FRS 105 (or FRS 102) in this regard.

Amendments to FRS 105 *The Financial Reporting Standard applicable the Micro-entities Regime – Limited Liability Partnerships and Qualifying Partnerships*

- 28 In March 2016, amendments were made to update FRS 105 in line with changes in UK legislation which have extended the micro-entities regime to limited liability partnerships (LLPs) and qualifying partnerships.
- 29 In accordance with the FRC's *Framework for developing Standards, Statements of Practice, Codes and Guidance*, these amendments were assessed as not requiring a formal consultation. FRS 105 was developed to support the existing micro-entities regime for companies, which as a result of a change in legislation was extended to LLPs and

²⁴ An organisation which may be referred to in the lease, which is responsible for the provision of services, and manages and arranges maintenance of the property, but which does not necessarily have any legal interest in the property.

²⁵ This can be found on the FRC's website.

qualifying partnerships, and these amendments simply extended the scope of FRS 105 (with some consequential amendments) consistently with the change in legislation.

- 30 The definition of a micro-entity and other related glossary terms were updated to reflect the extension of the micro-entities to include LLPs and qualifying partnerships.
- 31 The presentation and disclosure requirements applicable to LLPs and qualifying partnerships that adopt the micro-entities regime are almost identical to those applicable to the financial statements of companies that are micro-entities. Where there are differences these were reflected in these amendments to FRS 105.
- 32 The recognition and measurement requirements of FRS 105 were assessed to be suitable for LLPs and qualifying partnerships applying the micro-entities regime and therefore no amendments were made to the recognition and measurement requirements of FRS 105.

Triennial review 2017

- 33 In December 2017, FRS 105 was amended as part of the Triennial review 2017. The majority of the amendments were consequential in nature to ensure FRS 105 maintained consistency with FRS 102; however, other amendments were also made to align the standard with the legal frameworks in the UK and Republic of Ireland.

UK company law disclosures for the micro-entities regime

- 34 In addition to the consequential amendments, amendments were made to FRS 105 for further alignment with the company law disclosures for the micro-entities regime. The legal requirement to make these disclosures was effective for accounting periods beginning on or after 1 January 2016 in the UK. However, because an effective date of 1 January 2016 in FRS 105 would be retrospective, these amendments are applicable to accounting periods beginning on or after 1 January 2017, but a footnote was included to refer to the legal effective date.
- 35 Paragraph 3.8 of FRS 105 notes that for some of the disclosure requirements, disclosure is not required if the information resulting from that disclosure is not material. When no disclosure is provided on the basis that the resulting information is not material, a micro-entity is not required to state that fact.

Micro-entities in the Republic of Ireland

- 36 In June 2017, the Republic of Ireland implemented the EU Accounting Directive. The requirements are effective for accounting periods beginning on or after 1 January 2017, but early adoption is permitted for accounting periods beginning on or after 1 January 2015 provided that the financial statements have not yet been approved.
- 37 As a result, the micro-entities regime, as reflected in FRS 105, became available in the Republic of Ireland. However, there are some differences in the disclosure requirements applicable in the UK and the Republic of Ireland. Appendix B to Section 6 of FRS 105 was inserted reflecting the disclosure requirements for micro-entities in the Republic of Ireland.
- 38 FRS 105 does not contain accounting requirements specific to public benefit entities; micro-entities in Ireland that are charities will need to have regard to any specific requirements under the Charities Act 2009.

Consequential amendments

- 39 The main consequential amendments made to FRS 105, for consistency with FRS 102, are noted below.

Fair value measurement guidance

- 40 Minor amendments were made to the fair value measurement guidance in FRS 102 to emphasise that it is a methodology and to give further practical guidance.

Debt for equity swaps

- 41 FRS 102 was amended to include explicit guidance on how debt for equity swaps should be accounted for following feedback from stakeholders that when these transactions occur, they can be significant. FRS 105 was amended for consistency, by the insertion of paragraph 17.8A.

Revenue – agent and principal

- 42 Amendments were made to include guidance on how to determine whether an entity is acting as an agent or a principal in order to improve clarity. This additional guidance is consistent with FRS 102 and was based on guidance included in IAS 18 *Revenue*.

Gift aid

- 43 The FRC was made aware of significant differences in accounting treatment arising in practice in relation to the accounting for payments made, or expected to be made, by a subsidiary to its charitable parent that will qualify for gift aid (expected gift aid payments). This includes charitable parents that are exempt charities, eg they are not regulated by the Charity Commission, but have another principal regulator.
- 44 Although such payments are donations for tax purposes, they are a distribution from the entity to its owners for company law purposes (see ICAEW Technical release TECH 16/14BL REVISED *Guidance on donations by a company to its parent charity*). Therefore an expected gift aid payment shall not be accrued unless a legal obligation to make the payment exists at the reporting date. A board decision to make a gift aid payment to a parent charity, that has been taken prior to the reporting date, is not sufficient to create a legal obligation.
- 45 An amendment was made to allow a pragmatic exception that would permit the tax effects of the gift aid payment to be taken into account when it is probable that the gift aid payment will be made within nine months of the reporting date.
- 46 In addition, an amendment was made to clarify that the tax effects of distributions to owners shall be presented in profit or loss, rather than the same component as the underlying transaction. This is because when there is a tax effect arising from the distribution, it affects taxable profits.

Editorial amendments

- 47 Various editorial amendments were made to FRS 102 which were also made to FRS 105. These editorial amendments were not intended to change the requirements of the standards, but improve drafting, usability and update external cross-references. For example, they included:
- (a) improving the consistency of the scope sections throughout the standard to make it clearer what is within and outside the scope of each section;
 - (b) removing defined terms from the main body of the standard to reduce its length, as defined terms are set out in Appendix I *Glossary*; and
 - (c) improving the consistency of terminology and language in some areas.

Table 1**Exposure drafts and consultation documents**

Feedback to the following exposure drafts and consultation documents has been considered in the development of FRS 105.

More detailed information on the early development of the new UK and Republic of Ireland accounting standards can be found on the FRC website.

Exposure draft		Date of issue	Finalised as	Date of issue
FRED 50	<i>Draft FRC Abstract 1 – Residential Management Companies’ Financial Statements and Consequential amendments to the FRSSE</i>	Aug 2013	FRS 105 <i>The Financial Reporting Standard applicable to the Micro-entities Regime</i>	Jul 2015
Consultation Document	<i>Accounting for small entities – Implementation of the EU Accounting Directive</i>	Sep 2014		
FRED 58	<i>Draft FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime</i>	Feb 2015		
N/A			Amendments to FRS 105 <i>The Financial Reporting Standard applicable to the Micro-entities Regime – Limited Liability Partnerships and Qualifying Partnerships</i>	May 2016
Request for information	<i>Request for comments on the implementation of FRS 102 in order to inform the future development of FRS 102</i>	Mar 2016	Amendments to FRS 102 <i>The Financial Reporting Standard applicable in the UK and Republic of Ireland – Triennial review 2017 – Incremental improvements and clarifications</i>	Dec 2017
FRED 67	<i>Draft amendments to FRS 102 – Triennial review 2017 – Incremental improvements and clarifications</i>	Mar 2017		
FRED 68	<i>Draft amendments to FRS 102 – Payments by subsidiaries to their charitable parents that qualify for gift aid</i>	Sep 2017		



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