
SCR Reporting

Bulletin 2018 / 1

Amendments to FRS 102 and FRS 105

Just before Christmas, FRC issued amendments to FRS 102 and FRS 105. FRS 105 now requires additional disclosures, and these are required for periods commencing **on or after 1 January 2017**. This bulletin therefore outlines the changes, and the amendments to the SCR accounts disclosure checklist and illustrative accounts.

Auditing micro-entities

ICAEW has also issued guidance on drafting audit reports for micro-entities and we have incorporated that within this bulletin.

Update to SCR publications

Module 2 Micro-entities has been updated as follows:

- 2A – Micros - what you need to know (updated version (February 2018) replaces January 2017 version, now included in superseded versions)
- 2B – Micros - Accounting standards checklist (January 2107 version does not change)
- 2C – Micros - Accounts Disclosure Checklist (updated version (February 2018) replaces January 2017 version, now transferred to superseded versions.)
- 2D – Micros – Illustrative accounts updated version February 2018 (updated version (February 2018) replaces January 2017 version, now included in superseded versions)

In addition, an illustrative audit report for a micro-company has been added as Module 5G – Micros – Audit Report (new (February 2018))

We are currently working on the changes to Module 1 – small companies, and Module 3 – non-small companies and these will be issued shortly. These changes are effective for periods commencing 1 January 2019 but may be early adopted.

Once the financial reporting modules have been updated we will finalise updates to the Small Charity Reporting manual and review the contents and requirements for the audit procedures and compliance manuals.

Bill Telford

Editor

Revisions to FRS 105

Introduction

The principal change in FRS 105 is the incorporation of three disclosure requirements which probably should have been included previously, as they derive from the Companies Act 2006, rather than the accounting regulations. As with the previously required notes, these additional disclosure requirements must be shown at the foot of the balance sheet. This is generally considered to be above the signature block, and the statements relating to audit exemption, use of the micros regime etc.

Each of these notes has been included for small companies for periods commencing on or after 1 January 2016, so there is little need for guidance on preparing these notes.

Statutory information

Section 396(A1) of the Companies Act 2006 requires disclosure of the following information:

- (a) The part of the United Kingdom in which the micro-entity operates;
- (b) The micro-entity's registered number;
- (c) Whether the micro-entity is limited by shares or guarantee. Since a micro-entity cannot be a public company, it will have to disclose the fact that it is a private company;
- (d) The address of the company's registered office;
- (e) If relevant, the fact that it is being wound up.

This note has been required for FRS 102 1A for small companies for the last year or so, and a number of firms (and software suppliers) cross refer this note to the company information page, usually found at the front of the accounts. The danger with this approach is when the accounts are filleted for filing at Companies House. If the company information page is excluded from the filed accounts, they do not comply with the requirements of the Act. The safest option is to include this information at the foot of the balance sheet for micro-companies (and within the notes to the accounts for small companies).

Nature/purpose of arrangements not on the Balance Sheet

Section 410A (1) now requires a small company, and therefore FRS 105 now requires a micro-entity to include disclosure where the company is, or has been, party to an arrangement during the year that is not reflected on the balance sheet, where the risks or benefits are material.

The required disclosures are:

- (a) The nature and purpose of the arrangements; and
- (b) The financial impact the arrangements of the company.

For many micro companies this may be covered by the disclosure of commitments already required, although the fact that company law only requires disclosure of the aggregate amounts of such commitments may not sufficiently disclose the nature and purpose of the arrangements. For example, micro-entity accounts currently disclose the aggregate of commitments not on the balance sheet, including operating and finance lease commitments and capital commitments. This note may need to be expanded to disclose the nature and financial impact of the components of that note. There may be other arrangements, such as consignment stock, debt factoring or sale and repurchase arrangements not on the balance sheet, and not covered by the existing note requirements which now need to be disclosed.

Note, however, the requirement for the risks and benefits to be material.

Average number of employees

Section 411 CA 2006 has required disclosure of the average number of employees for many years. Prior to SI 2015/1980 this was prefixed by words "in the case of a company not subject to the small companies' regime", exempting small companies from this disclosure. These words were removed by the SI and we have therefore been disclosing this for small companies since then, and this is one of the mandatory disclosures in FRS 102 Section 1A. Since micro-companies are small, the removal of these words should have resulted in the note appearing in FRS 105! This has now been rectified by the triennial amendments.

Effective date

These disclosures must be incorporated in financial statements for periods commencing on or after 1 January 2017.

There is an error in FRS 105 in that the statutory information requirement above is included in section 3, and the requirement to include the notes from 1 January 2017 only relates to section 6. However, it is clear that since the requirements are imposed by the Companies Act, disclosure should be made earlier rather than later.

We would therefore recommend that, if the software has been updated, the information could be used for earlier periods.

Auditing micro-entities

General

By definition a micro-entity is a small company. Therefore, its shareholders can require an audit.

Accounting considers there are two reporting frameworks as follows:

- (a) A fair presentation framework; and
- (b) A compliance framework.

The audit report under Companies Act 2006 includes three explicit opinions:

- (a) The financial statements give a true and fair view – this is consistent with a fair presentation framework since there is a requirement that to achieve a true and fair view (or fair presentation) management may need to give disclosures beyond those required those in the Act or FRS.
- (b) The financial statements are prepared in accordance with GAAP – since GAAP for a small or large company includes a requirement to depart from the accounting standard if necessary to give a true and fair view this is consistent with a fair presentation framework. For a micro it is not, it is a compliance framework.
- (c) The financial statements have been prepared in accordance with the Companies Act 2006. As (b) above.

The question for the auditor is whether an audit report can be issued in true and fair terms!

An article in *Audit and Beyond* in February 2017 considered the issue and concluded as follows:

- (a) Company law allows audit of a micro and requires the auditor to disregard “any provision of an accounting standard which would require the accounts to contain information addition to” the minimum disclosure requirements. Note that is additional information is included, the auditors must have regard to any provision of an accounting standard which relates to that item.
- (b) ISA 230 *Agreeing the terms of audit engagement* identifies the risk that the audit report may be misunderstood as implying that the accounts have been prepared under a fair presentation framework, when, as noted above they have not. It is therefore suggested that this risk may be mitigated by the [prominent inclusion of an “other matter” paragraph in accordance with ISA 706.
- (c) Is this an acceptable risk?
- (d) Are there alternatives
 - (i) Agree a non-statutory audit on a compliance framework basis?
 - (ii) Offer some alternative limited assurance service?
- (e) If you agree to go ahead, consider the following:
 - (i) Tailor the engagement letter;
 - (ii) Consider content of letter of representation;
 - (iii) Tailor management letter;
 - (iv) Take care in drafting audit report;
- (f) Need accounts disclosure checklist.

Preparing an audit report

ICAEW has just published a helpsheet ‘Preparing an audit report for micro-entities. This is based on the illustrative audit report issued by FRC in the Bulletin: *Compendium of illustrative auditor’s reports on United Kingdom private sector financial statements for periods commencing on or after 17 June 2016* and provides guidance on adapting those reports. It recommends that all references to the ‘Companies Act 2006’ are amended to ‘Companies Act 2006 as applied to micro-entities.’

Opinion paragraph

ICAEW suggests the following wording to reflect the financial reporting framework:

The financial reporting framework that has been applied in their preparation is applicable law, and United Kingdom Accounting Standards, Financial Reporting Standard (FRS) 105 The Financial Reporting Standard applicable to the Micro-Entities Regime (United Kingdom Generally Accepted

Accounting Practice).

The opinion itself should be on the following lines:

In our opinion, the financial statements are in all material respects:

- properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, specifically FRS 105; and
- prepared in accordance with the requirements of the Companies Act 2006 as applied to micro-entities.

Therefore under section 495(3A) of the Companies Act 2006, in our opinion the financial statements give a true and fair view of the state of the company's affairs as at [date] and of its [profit / loss] for the [year / period] then ended.'

Use of PAASE

Where the auditor has used PAASE the basis for opinion paragraph should include an appropriate reference to its use and cross reference to the circumstances set out in note [X] to the financial statements.

Other matter paragraph

Since there is a risk that the use of the words 'true and fair' may be misunderstood by users, and in line with the suggestion in ISA 210, the helpsheet recommends the use of the following paragraph to be included **immediately after the basis for opinion paragraph**.

Other matter – application of true and fair view

The financial statements have been prepared under the micro-entities regime which does not require the directors or the auditor to consider the inclusion of any disclosures necessary to give a true and fair view where these go beyond the minimum disclosures required by the Companies Act 2006 as applied to micro-entities.

Going concern

There are no specific changes required to the standard wording – provided that the auditor has no concerns about the appropriate use of the going concern basis. There are of course no requirements for disclosure of uncertainties.

If there is an undisclosed material uncertainty, the auditor may be unable to give an unqualified opinion on going concern.

Other information

Since there is no requirement for either a strategic report or directors' report, the other information section may be excluded completely. Where a micro-entity includes additional information, the standard section should be included, but the words 'except as explicitly stated in our report' should be deleted as there is no statutory requirement for the auditor to report on non-statutory information.

Opinion on other matters prescribed by the Companies Act 2006

Again, on the assumption that the micro-entity does not include a strategic or directors' report, this section should be omitted.

Matters on which the auditor is required to report by exception

The paragraph 'in the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors report' should be deleted, unless the micro-entity has voluntarily prepared such documents.

ICAEW advises that the other implied terms of the audit report are required, notwithstanding that there is no requirement to make any disclosures concerning directors' remuneration but recommend that the final paragraph is amended. The section therefore reads as follows:

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not entitled to prepare the financial statements in accordance with the micro-entities regime and take advantage of the micro-entities' exemptions from the requirements to prepare a directors' report and strategic report.

Responsibilities of directors

No changes are required

Auditor's responsibilities for the audit of the financial statements

The easiest option is usually to cross refer this section to the FRC website.

Bannerman paragraph

Pending the updated version of Audit 1/03, the relevant paragraph is included after the auditor's responsibilities statement, adapted to add the words 'as applied to micro-entities' to in accordance with Chapter 3 of Part 16 of the Companies Act 2006.'

Signature and date

No changes required.

Feedback

We are always keen to hear feedback from our users. Please feel free to contact Bill or Mark with any suggestions, comments or ideas for new products or services. Bill is the principal contact for technical issues, Mark for administration, website and related issues. Bill's e-mail address is bill@scrreporting.co.uk while Mark can be contacted at info@scrreporting.co.uk