



Implementation Guidance

Accounting 01/17

General Accounting Principles for Small and Medium-sized Entities (GAPSME) – some frequently asked questions

Since the enactment of GAPSME, the Institute has issued two sets of Illustrative Financial Statements and the accompanying Disclosure Checklists, for small and medium-sized entities. The scope of this Implementation Guidance is to assist members in complying with GAPSME by clarifying some frequently asked queries the technical department of the Institute received from its members, with reference to GAPSME.

This Implementation Guidance has been structured in such a manner as to: (a) identify the principle requiring clarification; (b) the question posed to the Institute for guidance; and (c) provide relevant clarifications, including cross reference to the particular paragraph in the GAPSME regulation.

We trust you will find the information useful however it is not intended to be a comprehensive review of the new GAPSME regulations. Readers are advised to refer to the full regulations included in subsidiary legislation S.L.281.05 Accountancy Profession (General Accounting Principles for Small- and medium-Sized Entities) Regulations.



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1. Introduction

The EU Single Accounting Directive 2013/34/EU (the Directive), replacing the Fourth and Seventh Directives, brought about a new set of financial reporting requirements, for both individual and consolidated financial statements. The aim of the Directive was to simplify the preparation of statutory financial statements for qualifying micro-, small- and medium-sized entities (SMEs). The technical accounting aspects of the Directive were thereafter transposed into Maltese law through the introduction of the General Accounting Principles for Small and Medium-Sized Entities (GAPSME), as well as through amendments to the Companies Act (Cap. 386).

GAPSME applies to financial reporting periods commencing on or after 1 January 2016. It should be adopted by all small- and medium-sized entities, with the exception of Public Interest Entities (PIEs) as defined by the Accountancy Profession Act (Cap. 281), as long as they satisfy the applicable criteria. On transposition of the Directive, GAPSME has now become the default accounting framework for SMEs for financial reporting periods starting on or after 1 January 2016. Nonetheless, small entities and medium-sized entities can still prepare financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, if the Board of Directors or its governing body, has passed a resolution to this effect.



2. Recognition and measurement

2.1. Change from GAPSE to GAPSME

If the financial statements of a company were previously reported under GAPSE, how would the transition be shown in the Statement of Changes in Equity when one reports under GAPSME?

GAPSE and GAPSME are two different financial reporting frameworks. As specified in paragraph 24 of the GAPSME regulations, an entity that is a first time adopter of GAPSME must prepare an opening GAPSME balance sheet at the date of the transition to GAPSME. The date of transition being the beginning of the earliest period for which the entity presents full comparative information in accordance with GAPSME. Therefore if the company is preparing the first set of financial statements under GAPSME for the year ended 31 December 2016, the date of transition is 1 January 2015. Consequently 1 January 2015 is the starting point for accounting under GAPSME.

Accounting policies that an entity uses in its opening balance sheet under GAPSME may differ from those it used before. All necessary adjustments shall therefore be recognized directly in retained earnings (or other components of equity) at the date of transition. A reconciliation note (reconciling equity and profit or loss under both frameworks) is always required since the company would be changing the reporting framework from GAPSE to GAPSME.

2.2. Long term liability

If a parent company lends € xxxx to its subsidiary, with no fixed date of repayment and at zero rate of interest, is it required to amortise the liability using the effective interest method? Can it be classified as a current liability in view of the fact that there are no fixed repayment terms?

If the loan has no defined repayment terms, then it should be treated as repayable on demand and classified as due within one year, in the accounting records of the subsidiary. On the other hand if the repayment terms are at zero interest rate and repayable within a fixed period but beyond one year, then the loan should initially be recorded in the accounting records of both the parent and the subsidiary at the present value of the future cash flows. The difference between the loan's face value and present value of the future cash flows is recognised as a capital contribution in the subsidiary and an increase to the cost of the investment in the parent. The discount is unwound annually throughout the term of the loan.

2.3. Biological assets under GAPSME

Biological assets are held at fair value less cost to sell under the IFRS reporting framework. Would these assets be held at cost or at fair value less cost to sell under GAPSME reporting framework?

As specified in paragraph 5.4 of the GAPSME regulations, in the absence of a paragraph in the GAPSME regulations that specifically applies to a transaction, event or condition, management



shall use its judgement in developing and applying an accounting policy that results in information that is relevant and reliable. Paragraph 5.5 gives further guidance, wherein it is specified that in making this judgement management shall refer to, and consider the applicability of the following sources in descending order: (a) the requirements and guidance dealing with similar and related issues; (b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses as specified in paragraph 3 of the GAPSME regulations and finally; (c) the requirements and guidance in generally accepted accounting principles and practice dealing with similar and related issues. In this instance, in the absence of specific requirements and guidance in the GAPSME regulations one should refer to International Financial Reporting Standards as adopted by the EU.

2.4. Intangible assets, other than goodwill, with an indefinite useful life

How would one account for an intangible asset, other than goodwill, with an indefinite useful life under the GAPSME regulations? The intangible asset does not represent development costs.

GAPSME regulations paragraph 11.12 requires that the cost less estimated residual value of an intangible asset shall be amortised and allocated on a systematic basis over the asset's useful life. Therefore under the GAPSME reporting framework there is a presumption that every intangible asset has a definite useful life.

3. Consolidated Accounts

3.1. Comparative figures

A group was exempted from the requirement to prepare consolidated financial statements in prior years. If in a subsequent financial year, a group is required to prepare consolidated financial statements for the first time under GAPSME regulations, does it need to include the comparative figures?

Paragraph 4.7 of the GAPSME regulations specifically require that comparative amounts for the previous financial reporting period shall be shown for every item presented in the financial statements, in the notes and in certain instances for narrative and descriptive information.

3.2. Consolidated financial statements of a Small Group

If a Small Group of companies is not exempt from preparing consolidated financial statements under GAPSME due to the fact the one of its subsidiaries is a Public Interest Entity (PIE), should the Statement of Changes in Equity and the Cash Flow Statement be prepared and included as part of the Group financial statements?

As determined by the EU Accounting Directive, a PIE shall be considered to be large, regardless of its balance sheet total, total revenue and average number of employees. Consequently if the subsidiary is registered in Malta and is a PIE it has to prepare financial statements by applying IFRSs as adopted by the EU.



It is suggested that in view of the fact that in substance the group is a single economic entity, then the group financial statements, which comprise a PIE, should include the Statement of Changes in Equity and the Cash Flow Statement.

3.3. Disclosure of exemption in the notes

If a small entity prepares its financial statements under the GAPSME reporting framework and is exempt from preparing consolidated financial statements, is it still required to give details of the exemption in the notes?

The presumption is that a group has to prepare consolidated financial statements, it is therefore being suggested that when a parent company, is eligible for exemption from preparing consolidated financial statements relevant details should be included in the notes to the financial statements.

4. Disclosure

4.1. Disclosure of additional notes

Can the directors elect to disclose additional notes, further to disclosure requirements included in the different paragraphs of the GAPSME regulations?

The GAPSME regulations include the minimum requirements; voluntarily including other information is permitted.

4.2. The Share Capital note

The GAPSME regulations do not specifically require a note supporting the share capital disclosure in the balance sheet. Does this also apply if there are movements in share capital such as if there is an increase in authorised and /or issued share capital? Would this also apply in cases when the company has unsubscribed capital?

Paragraph 9.46 of the GAPSME regulations requires that the share capital note is included for medium-sized companies. Therefore the note is not required for a small company. As detailed above the GAPSME regulations include the minimum requirements and voluntarily including other information is permitted.

4.3. First year of operation

Do we need to include the date of incorporation in the notes to the financial statements when the company is in its first year of operation?

GAPSME regulations do not specifically require this disclosure. Nonetheless, the date of the end of the financial reporting period or the period covered by the financial statements, whichever is appropriate to the component of the financial statements should be displayed prominently as required by Paragraph 4.2(d) of the GAPSME regulations.



4.4. Disclosure of the ultimate beneficial owner

If companies prepare the financial statements under the GAPSME framework, would the disclosure of the ultimate beneficial owner be required?

GAPSME regulations do not specifically require the subsidiary to disclose the identity of the ultimate beneficial owner if it is an individual/ natural person. Although one should refer to the applicable disclosure requirements referred to in paragraphs 20.5 and 20.9 in the case of an entity.

4.5. Fiduciary Company

If the shares in a company are held in a fiduciary capacity by another company on behalf of the ultimate beneficial owners (UBOs), should the former company disclose the name of the UBOs?

As above, GAPSME regulations do not specifically require the subsidiary to disclose the identity of the ultimate beneficial owner if it is an individual/ natural person. Although one should refer to the applicable disclosure requirements referred to in paragraphs 20.5 and 20.9 in the case of an entity.

4.6. Disclosure of transactions with close family members of key management personnel

The definition of related parties as specified in articles 20.1 and 20.2 of the GAPSME regulations also includes members of key management personnel, of the reporting entity or of a parent of the reporting entity, and their close family members. Does this mean that transactions between the entity and close family members of key management personnel have to be disclosed?

Paragraph 20.7, which is applicable to all entities, specifies that if an entity enters into transactions with specific categories of related parties (referred to below), the entity **shall** disclose the amount of the transactions, the nature of the related party relationships and other information about the transactions and outstanding balances necessary for an understanding of the financial position of the entity. The specific categories referred to within paragraph 20.7 shall include parties having control, joint control or significant influence over the entity, subsidiaries, associates and jointly controlled entities of the entity, and members of the reporting entity's board of directors.

However paragraph 20.11, which is applicable to medium-sized entities only, specifies that the disclosures referred to in paragraph 20.7 have to be made in respect of all categories of related parties of the entity, including key management personnel and close family members of key management personnel. Therefore disclosure of transactions between the entity and close family members of key management personnel have to be disclosed only in the case of medium-sized entities.



4.7. Disclosure of emoluments to members of the entity's board of directors

Is a small entity required to disclose emoluments to members of the board of directors?

Paragraph 20.7 specifies that if an entity enters into transactions with specific categories of related parties (including the reporting entity's board of directors), the entity **shall** disclose the amount of the transactions, the nature of the related party relationships and other information about the transactions and outstanding balances necessary for an understanding of the financial position of the entity.

As stated in paragraph 20.7(a), such disclosures may include the amount of transactions in aggregate for each significant category of transactions, except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial position of the entity. Consideration should also be given to paragraph 4.25 which addresses items of income and expenditure which are of exceptional size or incidence.

5. Other

5.1. Size criteria and the two consecutive year rule

In determining whether an entity shall be classified as small or medium in 2016, is there a limit to how many years one should go back to identify two consecutive years?

There is no limit to how many years one should go back. So much so that, in order to establish the size threshold in the first year of application of GAPSME, this could entail going back to the year of inception of the company. One must also remember that directors of companies qualifying as small companies who want to take advantage of any exemption granted to such companies by the Companies Act (Cap. 386) are required to make a declaration as referred to in Article 183 when submitting their companies' annual accounts to the Registrar. A template of this declaration may be downloaded from the Registry of Companies website.

5.2. Preparation of the Board Resolution

If a small/medium company wishes to prepare the financial statements under IFRS reporting framework, would the Board Resolution have to be filed every financial year?

Yes, a resolution has to be filed every accounting period. S.L. 281.05 "the GAPSME regulations" article 4 states that the Board Resolution should be prepared 'for that financial reporting period'.

5.3. Retrospective application of GAPSME

Can companies adopt GAPSME retrospectively?

GAPSME regulations cannot be applied retrospectively but are only applicable for financial periods beginning on or after 1 January 2016.

One should also note that as required by Paragraph 4.7 of the GAPSME regulations specifically require that comparative amounts for the previous financial reporting period shall be shown



for every item presented in the financial statements, in the notes and in certain instances for narrative and descriptive information. Therefore in the first year of application of GAPSME, unless the first year of application is also the first financial reporting period of the company, one should also include comparative information.

5.4. Applicability of GAPSME

If a company was incorporated after 1 July 2015, the first audited financial statements will cover the period from the date of incorporation up to 31 December 2016. Would the financial statements be prepared under IFRS reporting framework?

The financial statements would be prepared under IFRS as adopted by the EU or GAPSE framework as applicable.

5.5. Government Owned Entities

Could Government Owned Entities prepare financial statements under GAPSME framework?

Small and medium sized entities, falling within the applicable criteria, are required to prepare financial statements, for financial periods commencing on or after 1 January 2016 in accordance with the GAPSME regulations. S.L. 281.05 article 3(1) defines entities as “commercial partnerships as defined in the Companies Act and any other body, corporate or unincorporate, which carries on a trade or business and which is required to prepare financial statements in terms of the laws of Malta”. Therefore GAPSME regulations do not specifically make reference to Government owned entities, consequently one should also refer to the specific provisions on financial reporting included in applicable legislative acts in force in Malta related to the Government owned entity.

The information included in this Guidance is intended for general information only and should not be used in relation to any specific application/matter without independent examination and verification of its applicability and suitability by professionally qualified personnel. Those making use thereof or relying thereon assume all risk and liability arising from such use or reliance. The Malta Institute of Accountants shall not be held responsible for any loss or damage sustained by any person and/or entity relying on the content of this Guidance.