



November 2017

# Financial Reporting Framework for Small- and Medium-Sized Entities

## Frequently Asked Questions - Small Businesses





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**1. Will the FRF for SMEs<sup>TM</sup> accounting framework deliver the information I need in a set of financial statements?**

The FRF for SMEs<sup>TM</sup> is intended to yield comprehensive, traditional, accrual-based financial statements including a statement of financial position, statement of operations, statement of changes in equity, and a statement of cash flows. In addition, sufficiently informative note disclosures are required. The financial reports prepared in accordance with the FRF for SMEs<sup>TM</sup> are meant to present only relevant and understandable information, without unnecessary complexity and extraneous narrative and details.

**2. How is the FRF for SMEs<sup>TM</sup> framework a cost-effective reporting option for a small- to medium-sized business?**

The FRF for SMEs<sup>TM</sup> framework is constructed of accounting principles that are especially suited and relevant to a typical small business. For example, the framework uses historical cost as its measurement basis and steers away from complicated and costly fair value measurements; the framework offers a simplified consolidation model ; the framework does not require complicated accounting for derivatives, hedging activities, or stock compensation; and the framework’s disclosure requirements are targeted without excess narrative. Moreover, the FRF for SMEs<sup>TM</sup> is concise, understandable and will be a stable framework. These factors and others produce a reporting option that is cost-effective for many entities.

**3. In what situations should a small- or medium-sized business prepare its financial statements in accordance with the FRF for SMEs<sup>TM</sup> instead of another basis of accounting?**

It comes down to each small business making an individual decision about what constitutes the best financial reporting option for themselves and those who rely on their financial statements. Deciding on using the FRF for SMEs<sup>TM</sup> should not be a complicated or difficult decision for a business’s owner-manager, the outside CPA firm and external financial statement users to make. The CPA firm will be equipped to explain the financial reporting under the framework and to demonstrate the kind of financial statements and information that stakeholders will receive.

When GAAP is not required and when the income tax basis or cash basis is not sufficient, the FRF for SMEs<sup>TM</sup> framework can be an ideal option for owner-managers who need financial statements that focus on cash flow, clearly present what an entity owns and owes, provide

information about the realizability of assets, and contain only relevant disclosures and financial metrics.

**4. Is there anything that would prevent an entity from adopting the FRF for SMEs™ accounting framework?**

The AICPA has no authority to prevent or require the use of a special purpose framework. The use of the FRF for SMEs™ is a decision to be made between private companies and users of their financial statements. Owner-managers of private companies, working with users of their financial statements, decide what reporting framework best answers their needs. When GAAP is not required, different non-GAAP reporting options are available to private companies. The FRF for SMEs™ is one of those non-GAAP options, intended as a relevant and cost-effective accounting framework for small- and medium-sized entities that delivers comprehensive and understandable financial information. The FRF for SMEs™ framework describes characteristics of typical entities that would utilize the framework. Owners and managers may refer to those characteristics as an aid in making a decision about adopting the FRF for SMEs™.

**5. Will my banker or other external financial statement user accept financial statements prepared under the framework?**

Owner-managers and their CPA practitioners will need to consult with lenders and other key external stakeholders about the use of the FRF for SMEs™ framework. With substantial relevance and cost-benefit factors, the AICPA believes that the lending community will accept financial statements prepared under the FRF for SMEs™ framework. Lenders are often very flexible in accommodating various financial frameworks for smaller entities. For example, many lenders today permit their customers to supply financial statements prepared using the cash or income tax basis of accounting. More important to lenders is the consistent application of the accounting principles underlying the financial statements. The FRF for SMEs™ framework consists of traditional accounting principles and accrual income tax accounting methods which are very familiar to lenders and have served the lending community well for many years. The FRF for SMEs™ framework is intended to be utilized by entities whose lenders base their decisions principally on reliable operations and cash flows. The framework will appeal to such lenders because it is a reliable financial framework, providing relevant information, is simplified, contains explicit and comprehensive accounting principles, and has been subjected to professional scrutiny. Moreover, the FRF for SMEs™ framework is a cost-beneficial financial reporting option for their customers.

**6. How difficult is it to learn and adopt the FRF for SMEs™ framework?**

The FRF for SMEs™ consists of traditional, accrual-based accounting methods and some accrual income tax methods. As such, its principles and requirements should be very familiar to many owners, managers and their CPA advisors. The framework is meant to be a cost-effective reporting option and as such avoids excess narrative and unnecessary complexity. In addition, the AICPA has provided many tools and resources to help owners and managers of a business better understand and implement the framework.

**7. Can an entity apply only part of the FRF for SMEs™ framework when preparing financial statements?**

There is no ability to adopt part of the FRF for SMEs™. If the FRF for SMEs™ is adopted then management would need to follow its principles and apply them in a way that is consistent with the criteria in cases where the criteria do not cover specific transactions or events.

**8. How does the FRF for SMEs™ differ from other bases of accounting?**

The FRF for SMEs™ is a non-GAAP (“generally accepted accounting principles”) accounting framework. Other non-GAAP frameworks include the income tax basis of accounting and the cash basis of accounting. The FRF for SMEs™ is different in that it has undergone public exposure and professional scrutiny. In addition, the FRF for SMEs™ framework provides financial reporting that is more standardized and comprehensive. The framework offers a more integrated financial picture of a business, providing, among other things, a statement of cash flow and informative disclosures. The FRF for SMEs™ enables owners, managers and others to assess a company's liquidity, financial flexibility and operating capabilities.

The principles and criteria comprising the FRF for SMEs™ accounting framework differ from GAAP in that the FRF for SMEs™ is tailored for the small business community and targeted to their specific financial reporting needs and those of their bankers and other external stakeholders. In addition, the FRF for SMEs™ generally does not make use of fair value accounting and also provides more flexibility in the areas of accounting for income taxes and consolidations.

**9. Why is the FRF for SMEs™ needed at this time?**

The AICPA's recent efforts to improve private company financial reporting revealed a clear need by small- and medium-sized businesses for a non-GAAP framework to better suit and answer their financial reporting needs. While some small businesses have found the cash or tax basis of accounting acceptable, these bases may be insufficient or inappropriate for other companies looking for more robust and relevant financial information. The FRF for SMEs™ accounting framework solves this marketplace demand by offering a cost-effective non-GAAP financial reporting option that is relevant, robust and reliable.

**10. What are the first steps a small business should take to begin using the FRF for SMEs™ accounting framework?**

Ask your CPA firm about the FRF for SMEs™ and express your interest in using it as the basis for your financial statements. The AICPA has provided its members with comprehensive tools to assist them in explaining the FRF for SMEs™ to clients and implementing it. In addition, the FRF for SMEs™ framework is available as a free PDF download on the AICPA website at [aicpa.org/FRF-SMEs](http://aicpa.org/FRF-SMEs) as well as other tools and resources to help owners and managers of small- and medium-sized entities learn about and adopt the FRF for SMEs™.

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