

MICRO ACCOUNTING MODEL: A FINANCIAL REPORTING FRAMEWORK FOR MICRO ENTITIES



In developing and emerging countries, micro businesses are often the backbone of the economy. These businesses, which are owned and managed by the local population, have a vital place in an economy's ecosystem. The majority of these businesses, however, do not prepare a set of financial statements, but use some form of traditional cash accounting method to record business transactions and keep track of the financials.

The question then is, should this status quo continue? The answer would very much depend on whether the micro business aspires to expand and grow. Micro business owners who are entrepreneurs would envision their businesses growing, expanding and becoming big in the future. For this to happen, two key elements are essential – capital, and the ability to entrust stewardship responsibilities. In order for investors and banks to provide capital and invest, they need to understand the financial performance and financial position of the micro business. In a similar vein, business owners need financial accountability from the people they have entrusted with stewardship responsibilities.

Today, there are various accounting frameworks available, such as the International Financial Reporting Standards (IFRS), IFRS for Small and Medium-sized Entities (IFRS for SMEs), and United States Generally Accepted Accounting Principles (US GAAP). These accounting frameworks are the financial language of

businesses, enabling the recognition, measurement, presentation and disclosure of business transactions in a summarised form, via a set of financial statements, to depict the financial performance and financial position of a business. Notwithstanding the availability of these accounting frameworks, micro businesses in emerging and developing countries require a framework that caters to their needs without the burden of excessive cost and complexity of implementation.

With this in mind, ISCA has developed a self-contained financial reporting framework for use by micro market participants operating in ASEAN countries (micro entities). The Framework, known as the Micro Accounting Model (MAM), is intended for micro entities to transit from cash accounting to the most basic form of accrual accounting. Such micro market participants are typically sole proprietorship businesses that have no public accountability, are exempt from audit and are not required to comply with any stipulated accounting standard framework. MAM is thus intended to provide the building blocks to enable businesses to progress towards more comprehensive accounting frameworks, such as IFRS or IFRS for SMEs, as businesses grow.

MAM, in its approximately 50-page framework, applies basic accounting principles and contains significant simplifications while keeping within the confines of the pervasive principles derived from the International Accounting Standards Board's Conceptual Framework for Financial Reporting and from full IFRS. It also includes a set of illustrative financial statements and reconciliation to IFRS and IFRS for SMEs. Key simplifications have been applied especially in the area of financial instruments.

In the drafting of MAM, three overarching principles have been applied – the cost or burden of applying an accounting treatment must not outweigh the benefits to micro entities; the complexities in the recognition of an item and the degree of estimations and judgements in the measurement of assets, liabilities, income and expenses should be minimised where possible. MAM endeavours to be an intuitive and understandable framework for micro entities and the users of their financial statements. It lays out principles that encourage the use of judgement in the particular circumstances of a transaction or event. It can also be used to provide national accounting standard-setters with an illustrative framework in developing their accounting standard for micro entities in their jurisdictions.

MAM is a principles-based financial reporting framework, underlined by concepts such as materiality, qualitative characteristics of useful financial statements, accrual accounting, definitions of elements of financial statements and the recognition criteria. It provides the fundamentals for the preparation of financial statements. In addition to concepts and principles, MAM addresses transactions typically encountered by micro entities – property, plant and equipment; inventories; revenue; etc. If MAM does not specifically address a transaction, use of judgement is required to apply the general principles, concepts and criteria contained in the Framework when developing accounting policies.

The idea and conceptualisation of MAM came from ISCA President Dr Gerard Ee, who also penned the Foreword in the MAM document. Among other things, he had said, "I strongly encourage emerging and developing countries, in particular, the standard-setters and national professional accountancy bodies, to use this guide as a starting point towards eventually adopting international accounting standards. I envisage that the government of these countries will find MAM a useful tool in helping to raise the overall standards of the profession, thereby contributing towards stronger investor confidence towards the country. Furthermore, as more businesses are encouraged to use MAM to produce quality, reliable financial information, governments would also have greater assurance over tax collections".