



# Study on the accounting regime of limited liability micro companies

## *EXECUTIVE SUMMARY*

A study prepared by CEPS in collaboration with LSE Enterprise and Bureau van Dijk for the European Commission, Directorate-General for Financial Stability, Financial Services and Capital Markets Union

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## **Executive Summary**

The objective of this study is to provide a quantification of the reduction of the administrative burden on micro companies that is associated with the introduction of a super simplified regime for financial reporting, as regulated in the Accounting Directive (2013/34/EU). This requires the estimation of both (1) the number of limited liability micro companies and (2) the reduction in costs of preparing the financial report.

The super simplified regime aims to reduce the administrative burden of limited liability micro companies. These companies are exempt at the EU level from the general publication requirement of annual accounts, provided that their balance sheet information is duly filed. They are also exempt from additional reporting obligations, such as notes to financial statements and management reports, as well as being allowed to draw up an abridged profit and loss account and an abridged balance sheet.

Member States have the freedom to decide about the degree of implementation of the provisions of the super simplified regime in the Directive, which has resulted in different regimes across Member States.

The super simplified regime is in principle only applicable to limited liability micro companies. Member States are allowed to decide on size criteria, but these cannot exceed the size criteria in the Directive. More specifically, limited liability micro companies are defined as limited liability companies that meet at least two of the three following criteria: less than 10 employees on average during the financial year, net turnover of up to EUR 700,000, and balance sheet totals of up to EUR 350,000.

## **Methodological approach**

The estimation of the two variables is based on a combination of quantitative methods.

First, the number of limited liability micro companies to which the new regime is applicable has been determined following the definition in the Directive and the national transpositions of the Directive. Companies must be active, located in one of the 28 EU Member States as well as meeting the size criteria and company status identified in the Directive or its transposition into national legislation as of 31 December 2016.

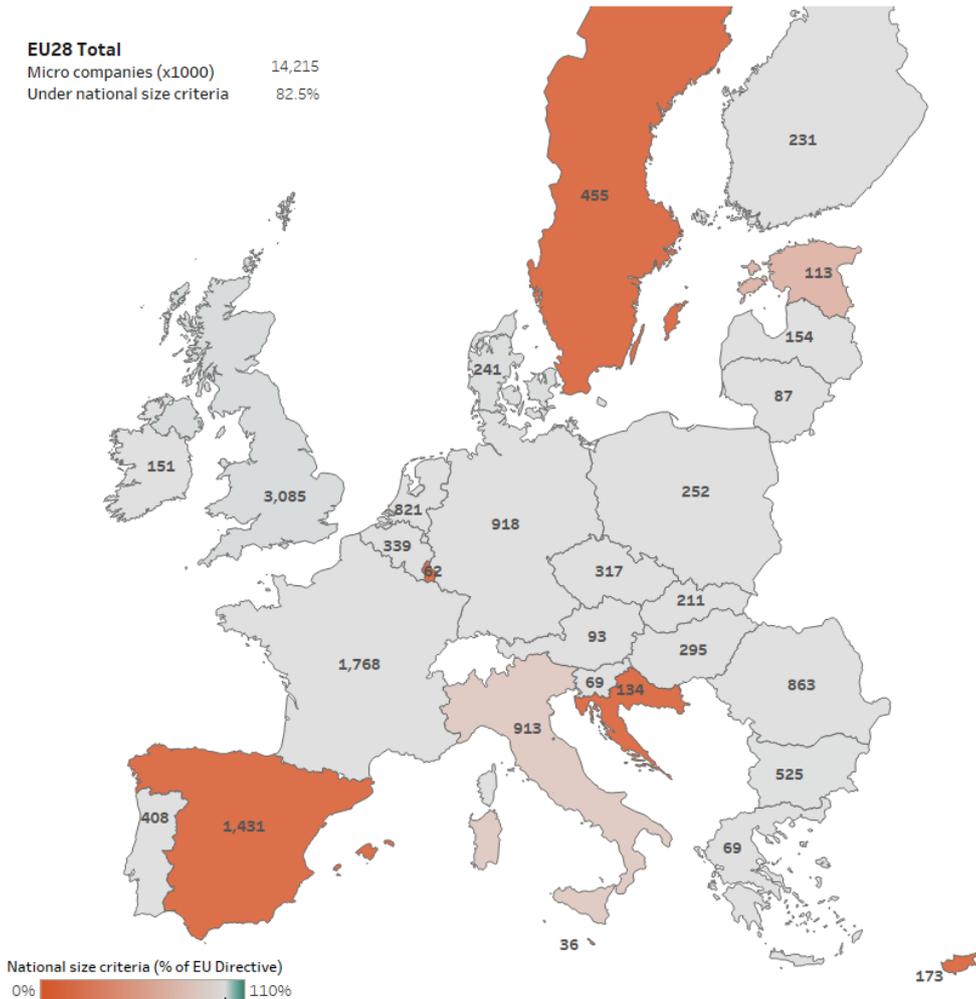
Second, the reduction in the administrative burden for micro companies brought about by the super simplified regime, and its monetary value, is estimated through a survey of the micro companies and their key stakeholders, including accountants, registries, banks and associations (Chapter 3).

The survey covers eight countries selected according to several criteria to ensure representativeness of the sample for the purpose of the evaluation. The outcome of the survey, in Belgium, Bulgaria, Czechia, Estonia, France, Germany, Greece and Portugal, is used to assess the costs and benefits of the super simplified regime, at the level of individual Member States. Using the cost estimates for the Member States in the survey (Chapter 5) and the estimated number of micro companies (Chapter 4), the actual and potential reductions in the administrative burden are calculated for each the EU Member States.

While the estimates above should provide a good indication about the likely net benefits, the primary information gathered for this study is limited. This is especially true for the information gathered through the survey on financial benefits. Only a few micro companies provided concrete information on the savings associated with the super simplified regime and there is quite some difference in the amounts, ranging

from nothing up to a couple of thousand euros. This implies that the numbers should be used with caution.

**Figure 1** Number of micro companies in EU Member States according to the new Accounting Directive



Note: The map shows the number of micro companies according to the size criteria of the EU Directive in each Member State and the micro companies according to the national size criteria as a share of the EU Directive size criteria.

Source: CEPS based on Orbis Europe.

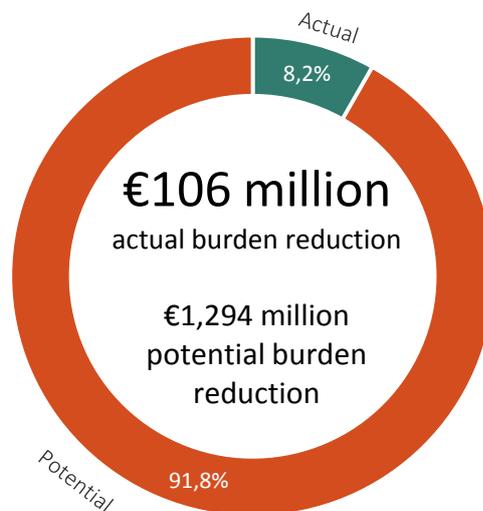
## Results

The total population of limited liability companies (all sizes included), based on the ORBIS Europe database, is about 16.8 million. Based on the EU definition there are 14.2 million micro companies or 84.4 % of all limited liability companies (see Figure 1). When using national size criteria to define micro companies, the total population of micro companies in the Member States that have implemented the super simplified regime is reduced to 11.7 million (or about 82.5 % of the EU definition) because these are sometimes more stringent. The smaller population also reduces the potential benefits of the super simplified regime as the cost reduction benefits fewer companies.

However, based on the outcome of the survey, besides the lower number of micro companies due to national size criteria, other parameters emerged as playing a critical role in limiting the total burden reduction: the actual use of the super simplified accounting regime. In addition, the survey outcome clearly pointed to limited awareness among micro companies of the super simplified regime for financial reporting and/or a certain degree of inertia leading them to stick to the pre-existing regime. Most micro companies seem not to be aware of the existence of the super simplified regime. This is particularly the case in some countries, but above all it is the case for micro companies that rely on external accountants for financial reporting. Both accountants and their clients indicated in the survey that there is limited to no information provided to clients on the super simplified regime and essentially no measurable impact on the prices of accounting services. In addition, of those micro companies that are aware of the new regime because they do the report themselves, only a portion of them apply the super simplified regime or perceive a substantial reduction in the administrative burden.

Based on these findings the cost reduction is estimated for the entire EU. Countries that have implemented the new accounting Directive to some extent but are not part of our sample are grouped with a surveyed country that most resembles the degree of implementation of the EU Directive and its prior legislation on micro company accounting requirements.

**Figure 2 Administrative burden reduction, per year, due to Super Simplified Regime**



Source: CEPS analysis.

Accordingly, we estimate the current one-off costs of becoming familiar with the new regime at EUR 27 million and the ongoing burden reduction at EUR 106 million per year. These amounts are estimated for the 11.7 million micro companies that were at the end of 2016 meeting the national size criteria of the 22 Member States that implemented the regime. If national size criteria were fully aligned with the Accounting Directive, the costs and benefits would increase. The one-off costs would be about EUR 32 million, and the annual burden reduction would increase to EUR 128 million for all the 14.2 million micro companies in the 28 Member States.

From these calculations, it clearly emerges that the extent of lack of awareness and use of the super simplified regime appears to have far more impact than the different

size criteria adopted in national legislation. If we assumed full awareness and use of the regime among the 14.2 million micro companies, the estimated benefits would increase by almost a factor of ten to EUR 0.32 billion in one-off costs and EUR 1.3 billion of ongoing reduction in administrative burden. In order to unlock the potential savings, awareness and use of the regime among the micro companies would have to be increased.

The potential savings could possibly be even higher when all Member States would fully implement the super simplified regime.

## **Conclusion and implications**

The initial expectation in terms of administrative burden reduction due to the introduction of the super simplified regime appear to have been too optimistic. It did not consider that many Member States would take up the simplification options only moderately or not at all. It did not sufficiently take into consideration the challenges of making sure micro companies are aware of the existence of the new regime, use it and take advantage of it. This turned out to be the most important factor driving low benefits, perceived and actual, of the super simplified regime for micro companies. Understanding why this happened helps identify potential improvements.

There are three explanations for the limited benefits.

First, micro companies relying on external accountants appear in many cases not to have been informed about the simplification of the financial reporting obligations.

Second, in some cases, even when micro companies or accountants were informed about the new regime they did not necessarily put it into practice. The former, possibly not to face the one-off cost of the change, the latter possibly to avoid reducing the fee charged to clients for their services. Both explanations point to a problem of inertia and reluctance to move to a new regime. The fact that the change was hardly noticeable to companies, or easy to hide for accountants, is likely to have made the inertia stronger.

The third explanation is linked to a broader result emerging from the estimation of the micro companies and survey. Financial reporting appears to be perceived of limited value to the micro companies and some other stakeholders such as banks. In addition, there are many micro companies for which there is no or only part of the key financial data available. This is either because the registries do not provide the data in a digital format or micro companies are not complying with reporting obligations. One option for overcoming this problem would potentially be to link or combine financial reporting with tax reporting obligations ("one stop shop" or "file-only once" principle).

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